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DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
Washington, D.C. 20523

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189 pages

CAPITAL ASSISTANCE PAPER

Proposal and Recommendations
For the Review of the
Development Loan Committee

ECUADOR: LAND SALE GUARANTY

5180103

A.I.D.
Reference Center
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AID-DLC/P-854

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DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
Washington, D.C. 20523

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AID-DLC/P-854
June 24, 1969

MEMORANDUM FOR THE DEVELOPMENT LOAN COMMITTEE

SUBJECT: Ecuador: Land Sale Guaranty

Attached for your review are the recommendations for authorization of a loan in an amount not to exceed \$3,600,000 to the Government of Ecuador to assist in financing the sale of agricultural land to campesinos and the extension of production credit thereto.

Please advise us as early as possible but in no event later than noon on Monday, June 30, 1969, if you have a basic policy issue arising out of this proposal.

Rachel C. Rogers
Assistant Secretary
Development Loan Committee

Attachments:

Summary and Recommendations
Project Analysis
ANNEXES I-VIII

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ECUADOR - LAND SALE GUARANTY

TABLE OF CONTENTS

	<u>Page</u>
SECTION I - SUMMARY AND RECOMMENDATION	1
SECTION II - NATURE OF PROJECT	9
A. Introduction	9
B. Setting of the Project	11
C. Project Description	17
D. Program Justification	19
SECTION III - DETAILED DESCRIPTION OF THE PROJECT	23
A. The Borrower	23
B. The Administrator and Sub-Borrower - Banco Nacional de Fomento	24
C. Operation of the Project	33
D. Financial Analysis	52
E. Economic Analysis	62
F. Some Peripheral Problems	65
SECTION IV - LOAN ADMINISTRATION	70
A. Project Execution	70
B. Implementation Procedures	75
SECTION V - ISSUES	77
A. Alternative Approaches to Problem of Financing Land Purchases	77
B. Direct AID Financing Through SIC Procedure of Production Credit for the Project	78
C. Possible Negotiation Difficulties	79
ANNEX I - Certificate	
ANNEX II - Checklist of Statutory Criteria	
ANNEX III - Activities of USAID in Determining Attitudes of Persons and Groups Affected by the Project	
ANNEX IV - Lending Procedures of the Division of Supervised Credit and Other Data Relating to BNF	
ANNEX V - The Cooperative Movement in Ecuador and its Relation with USAID	
ANNEX VI - Per-Hectare Costs and Revenues (6 tables)	
ANNEX VII - Agrarian Reform in Ecuador	
ANNEX VIII - Draft Loan Authorization	

ECUADOR-LAND SALE GUARANTY

SECTION I - SUMMARY AND RECOMMENDATIONS

1. Purpose

The purpose of the proposed pilot project is to develop a program to facilitate the private sale of agricultural lands to cooperatives capable of carrying out effective farming enterprise given access to land, production credit and technical assistance but which are unable under present conditions to secure credit on reasonable terms. The philosophy underlying the program is that appropriately assisted, free market private enterprise activities can be the basis for reform of the land tenure structure thus eliminating politically traumatic recourse to expropriation or other nonconsensual forms of land title transfer.

2. Borrower

The Borrower will be the GOE thru the Ministry of Agriculture. Administration of the loan will be the responsibility of the Banco Nacional de Fomento, an autonomous agency of the GOE. The BNF will appoint a Project Coordinator who will manage all elements of the program including technical assistance operations.

3. The Loan

A loan will be for 40 years with a grace period on repayment of principle of 10 years. Of the 3.6 million dollars made available under the loan, \$2,750,000 will be disbursed under SLC procedures

to provide local currency for production credit purposes. \$650,000 will be held undisbursed forming a fund to guaranty the payment of land purchase obligations undertaken by the beneficiaries of the program. As agricultural production credit loan repayments are made, these funds will be substituted for the guaranty fund which will be drawn down for production credit operations, thus assuring full disbursement within three years while maintaining a guaranty fund. \$100,000 will be used to establish a revolving fund to support technical assistance and extension services for cooperatives involved in the program. \$100,000 will be disbursed under letters of commitment for the purchase of commodities of U.S. source and origin for use in the program.

4. Project Description

The project will establish a procedure under which campesino cooperatives can purchase land and obtain production credit and technical assistance in a "package" sub-project similar to a supervised agricultural credit operation. The BNF will be the organization which will administer the program. The BNF, with the assistance of the Ministry of Agriculture and USAID, will develop for each sub-project a farm plan setting out all requirements of an effective economic enterprise. In accordance with the farm plan, land will be purchased, production credit will be provided by BNF and technical assistance will be provided under BNF direction and control by GOE extension personnel. Land purchase will be accomplished through a three party arrangement under which the seller transfers title to the cooperative, the cooperative agrees to pay the purchase price less downpayment to the BNF over a period of 5 to 7 years and the BNF agrees to pay the seller on the basis of the amortization schedule of the payment of the obligation of the cooperative to the BNF. Production credit will

be provided by the BNF in an amount consistent with the farm plan. Finally, GOE technical personnel under BNF direction will provide and the cooperative will agree to utilize technical assistance in accordance with arrangements set out in the farm plan. In the event that a cooperative defaults on its obligation to pay the BNF for land purchased under the program, the BNF will have the right to claim against the guaranty fund for the amount paid by the BNF to the seller of the land in accordance with the contract between the seller and BNF provided the USAID is satisfied that BNF has in good faith made all efforts appropriate under the circumstances to realize an available security. Responsibility for formation and qualification of cooperatives will lie with Ecuadorean organizations including former USAID staff employees. The loan will also provide \$100,000 dollars for U.S. commodities required by the Ministry of Agriculture in carrying out its technical assistance responsibilities under the program. In addition to interest charges, the cooperative will pay certain user charges which will be paid into a revolving fund for the payment of local currency expenses of the GOE in carrying out the project. The project will thus be maintained in so far as possible as a self-financing operation.

5. Financial Plan

Costs of the project:

Land sale guaranty fund	\$ 650,000
Production credit	2,750,000
Commodities of U.S. source and origin	100,000
Revolving fund for local costs of technical assistance	<u>100,000</u>
	\$3,600,000

These inputs will result in the sale of approximately \$2,500,000 worth of land (25,000 hectares) to be farmed by 50 cooperatives of 50 families each.

6. Other Sources of Funds

The IRR describing this project has been circulated to other international financing institutions all of which have indicated that they are not interested in financing this project. As the project is experimental in nature and as absence of experience with such a project results in its being considered "high-risk", it is believed that this project is inherently suitable at this time only for AID "last resort" financing.

7. Statutory Criteria

As indicated in Annex II, the proposed project is consistent with all relevant statutory criteria.

8. Views of the Country Team

As reflected in the CASP and other statements of policy, a primary area of interest of the USG in Ecuador is in improving the economic and social conditions of lower income groups within the society. This project has been designed with a view to marshalling the resources and efforts of Ecuadoreans to achieve these objectives. The project is designed to test the feasibility of a new approach to agrarian reform and social and economic betterment of the rural population. The project is not only central to AID objectives in Ecuador but is

considered to have significant possibilities as an approach to agrarian reform and development beyond the borders of Ecuador. This loan carries the highest priority in the USAID proposed loan program.

9. Issues

A. Alternative Approaches to Financing Land Purchases

Alternative approaches to land purchase financing such as establishment of a mortgage banking operation were considered in intensive review. While the desirability of a more orthodox approach is recognized, it appears that financing schemes involving payment to the seller at the time sale are not feasible for lack of sucre resources within the economy. In short, it appears that the only way to finance land sales of this type is by the seller himself financing the operation. The project is built around this approach.

B. Local Cost Financing

Financing of local costs of production credit operations will be handled by means of generations under SLC procedures. There are not available within the public or private sectors sufficient resources to meet the requirements of the project. It is hoped, however, that when the project proves itself, that local resources can be attracted to support the production credit effort.

C. Possible Negotiation Problems

The proposed project represents a new departure in financing agrarian development. After extensive discussions with BNF, reservations have been expressed by individuals within BNF concerning certain elements of the operation, specifically the land guaranty procedure. Because of the novelty of the operation, it is clear that negotiation of various aspects of the project will be complex and indeed may require some changes from the project as presented herein. The Mission believes that the loan can be negotiated substantially in the form presented. In any event, the loan authorization will provide that if a loan agreement reflecting a project substantially as presented herein is not signed within six months of the date of authorization, the authorization will be terminated.

10. Loan Administration

The project will be implemented by the BNF which is considered qualified and capable of handling this program in light of its experience in supervised agricultural credit operations. Disbursement of dollars for conversion to local currency will be handled under SLC procedures. Procurement under the loan will be limited to commodities of U. S. source and origin. The Mission will be involved in the administration of the program in key activities such as cooperative formation and qualification, land valuation approval, and approval of claims against the guaranty fund. In addition to the foregoing, the Mission will carry out normal monitoring functions.

11. Recommendations

On the basis of the conclusions of the capital assistance committee that the project is technically, economically and financially justified, it is recommended that a loan to the government of Ecuador for an amount not to exceed U.S. \$3,600,000 be authorized subject to the following terms and conditions.

A. Interest and Terms of Repayment

1. Terms - 40 years with a grace period on repayment of principle of 10 years.
2. Interest - 2% per annum during the grace period and 3% per annum thereafter.
3. Repayment will be made in U. S. dollars.

B. Other Terms and Conditions

1. Equipment and materials financed under the loan shall be of

the U. S. source and origin.

2. Any other terms and conditions which AID may deem advisable.

Project Committee:

Charles S. Blankstein, Development Loan Officer
Richard Winters, Rural Development Officer
Eugene Braun, Chief Institutional Development
Lewis Townsend, Agricultural Cooperatives Advisor
Clarence Zuvekas, Program Economist
Guss Nolan, Controller
Edward Hirabayashi, Acting Assistant Director for Social Development

Drafting Officer: Charles S. Blankstein

SECTION II - NATURE OF THE PROJECT

A. Introduction

The problem of agrarian reform, a recurring theme throughout Latin America, is approaching a critical stage in Ecuador. While demands for distribution of land to campesinos have long been a feature of political activity as well as revolutionary agitation, the past year has seen a significant increase in the physical invasion of lands accompanied by violence. The GOE land reform effort has proven itself to be woefully inadequate to its task, not so much to failure of interest by the national leadership but because of opposition from powerful economic interest, lack of resources to make redistributed land productive and the administrative incapacity of the agrarian reform agency. While it would not be accurate to emphasize the immediacy of the threat of political instability inherent in the current situation, it would also be unwise to underestimate the long-run danger. Invasions are symptomatic of significant social unrest.

The country team is of the view that steps ought to be taken to relieve the pressure for land and satisfy legitimate demands for land reform in the form of a comprehensive program under which campesinos can obtain land and have access to other forms of inputs needed to conduct effective agricultural enterprise. If action is to be taken within a time frame which permits of success, efforts ought to be initiated now. Indeed now is a particularly propitious time for an effective and relatively low-cost initiative in agrarian reform. Detailed inquiries conducted by the Mission confirm that many land owners are very much interested in selling their lands before the threat that their properties will be invaded by campesinos or appropriated by the government becomes more pressing. The campesino generally understands and accepts the desirability of buying rather than taking land. The land for which the greatest pressure for land redistribution exists, the rice growing areas of the Guayas River Basin, is highly productive and capable of producing incomes necessary to pay off land purchase obligations over relatively short terms. Thus the need and the fundamental requirements of meeting the need exist. The problem is to combine these elements with assistance as appropriate in a workable program.

In approaching this problem, the reasoning of the Mission was along the following lines:

The most formidable barrier to the economic development of Ecuador and the basic reason for the country's social instability is the fact that a large proportion of the population is effectively precluded from full participation in the economic and political life of the country. While universal citizenship in the fullest implication of the term will be the work of generations, it is possible to facilitate in significant ways the movement of disadvantaged groups within the country toward economic independence. The economic and social analysis presented subsequently in this paper will deal in some detail with the nature of the problems faced by the Ecuadorean campesino. Suffice it to say at this point that a critical obstacle to economic and social and therefore political development of the campesino is his inability to obtain credit to buy and work agricultural lands at interest rates low enough to permit him to earn a decent living and save.

The resources required to deal with this problem in its totality appear clearly to be beyond likely availabilities of foreign aid. Indeed, the deprivation of resources for the campesino is so rooted in historical and cultural considerations that a solution to the problem depending exclusively on foreign aid would probably be socially unwise. Thus it appears that in attempting to deal with the problem it is necessary to think in terms of Ecuadorean resources: not only in terms of work and money but also in terms of the capacity of the economy to overcome long standing social and economic prejudices to learn to deal with the campesino as an independent economic man rather than an object of subtle or gross exploitation. In this connection, the Mission began to think of the tensions existing within the society, as exemplified by land invasions, as opportunities for advance rather than as difficulties to be overcome.

The analysis proceeded on the basis of identifying the type of land sale transaction which would be economically attractive to the parties concerned but for which significant social and cultural obstacles exist such as distrust and fear of the campesino's financial irresponsibility and its consequence, an economic structure which precludes the campesino's access to credit on reasonable terms. From this it followed that the AID intervention critical to the objective sought was an economic substitute to bridge the psychological gap preventing effective self-development efforts. The judgment of the Mission, contrary to that of the land owner interest, was that the campesino generally is credit worthy. Thus the requirements of the project became obvious: an assurance of payment of obligations credible to potential sellers of land and a program to provide reasonable assurance that the campesino buyers could carry out an enterprise

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which would permit them to pay their debts.

The proposed loan will provide guarantees of credit extensions by willing sellers of land for the purchase of land by campesino cooperatives and will provide a source of agricultural production financing. Its primary objective is to make it possible for campesinos capable of managing an agricultural enterprise to buy land and to obtain working capital to farm the land effectively. Technical assistance as appropriate to the particular case will be assured as a part of a "package" transaction.

The Mission in this paper proposes a new departure in agrarian reform. It is, in effect, a "private enterprise" approach to the problem. It is fundamentally an expression by the United States of its faith in the dignity and responsibility of the Ecuadorean campesino. This is a calculated risk but a sound one. USAID believes an ultimate consequence of the program will be to convince the dominant social elements of the country that this faith is well placed.

B. The Setting of the Project

1. Introduction

While projects under the proposed program may on occasion be undertaken in other parts of Ecuador, all but a few will be located in the rice growing areas of the Guays River Basi. There are a number of reasons for this. The immediate pressure of land invasions is primarily in that area. Land in the Guayas River Basin is particularly productive and hence would be land on which small buyers would be most likely to be able to succeed. An effective technical assistance program is feasible with presently operating organizations in that area. A tendency on the part of land owners to be willing to sell is most strongly noted in that area. Most important, there are in existence campesino groups capable of qualification for support under the program and the relative sophistication of campesinos in the area suggests that new group formations will take place more readily and effectively there. In consequence, the expectation is that the program will focus at least at the beginning in the rice growing area of the Guayas River Basin and will have as its main beneficiaries the members of the rice cooperatives and credit unions formed with USAID assistance. Thus a description of this area is necessary to an understanding of how the program will work.

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2. Geography and Economy of Guayas River Basin

The Guayas River Basin is an area of approximately 35,000 square kilometers which stretches from Santo Domingo in the North to the Naranjal River in the South, a distance of about 220 kilometers, and from the Andes in the East to Portoviejo and Jipijapa in the West, about 160 kilometers. There are about 15,000 square kilometers of good agricultural land in the Basin.

The southern area of the Basin constitutes some 9,500 square kilometers of mostly flat alluvial land which has excellent agricultural potential. Lack of irrigation facilities and adequate dams in the upper part of the Basin cause periodic losses of crops in the south because of too little or too much water. Some of the rivers that come down from the Andes offer excellent possibilities for irrigation and are also suitable for being controlled with the building of adequate dams upstream. These flat lands in the south of the Basin have been traditionally one of the main agricultural areas in Ecuador due to the fertility of its soil and good communications with Guayaquil and the rest of the country. The main crops grown in the area include rice, sugar cane, bannas, cocoa and cotton. The northern part of the basin is a large area of fertile volcanic soil and adequate rainfall. It is not subject to seasonal flooding. This area has been introduced to the agricultural economy of the country in the last 20 years with the building of new all weather roads in part financed by AID.

It is not an appropriate area for rice production; bananas are the main crop. Over 50% of this area is still covered by virgin forests.

The Guayas River Basin has been the mainstay of the agricultural export economy of the country in the last century. It was the main producer of cocoa for export in the 1920's and 1930's; in the 1940's and early 1950's it was the main producer of rice for export; and finally in the late 1950's and 1960's it has produced most of Ecuador's banana exports. The area also produces most of the rice which forms the basis of the diet in the coast and is widely consumed in the cities of the Sierra. The products of the Basin represent the bulk of exports that are shipped through Guayaquil, Ecuador's main port. There is

not an area of similar size in the country that approaches the economic importance of the Guayas River Basin.

3. Social Structure and Problems

The northern and southern areas of the Basin are not only different in their geography and production possibilities, but they are also different in terms of the people who live there and the relations that exist between the social groups. The northern part which has been recently settled is dominated by farms of various sizes which are usually owner operated. There, work that is not done by the owner is paid on a daily basis in cash. People that live in this area are mainly pioneers that have gone in and started agricultural enterprises or family farms from nothing. Investments of capital have been very large in some cases or non-existent in other cases, but the results of the effort and presence of farm owners are reflected everywhere.

The situation contrasts sharply with that which exists in the long settled southern area. In the alluvial lowlands of the south, the owners of the land form a distinct social group that lives mainly in the city of Guayaquil and farms its lands through share cropping or leasing arrangements. The people that work these properties are landless campesinos that live in some cases in small towns and in other cases in the places where they grow their crops. It is estimated that 80 percent of the rice growing enterprises in the area are carried on by landless campesinos.

The increasing population pressure on the land and the fact that many of the owners who inherited their properties are not real agricultural entrepreneurs is characteristic of this system in which the owner lives mainly on land rentals. The person that cultivates the land manages to survive on the basis of his labor without the assistance of capital or modern technology. The usual type of land use arrangement in the area involves the leasing of land for a fixed quantity of produce, mainly rice, which is paid by the renter at harvest. Thus typically the landowner and the renter make a verbal agreement that specified a rental payment of from 400 to 600 pounds of rough rice per cuadra, which is the equivalent of 525 to 800 pounds per hectare. This is the equivalent to

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450 to 600 sucra per hectare or \$20 to \$30. Often the owner charges for irrigation water and other services at high pre-determined prices as well.

To cover his operating expenses, the rice grower has to secure credit from rice millers or private money lenders. This credit usually carried the obligation to repay in rice at a specified price, usually one-fourth to one-half of the actual market value of the rice. Thus, the borrower pays in effect anywhere from 100% to 300% interest on a six month loan, depending on the market price of rice when it is harvested.

In 1967, a law limiting the maximum amount of produce that can be charged as land rent was promulgated. The law also provides that renters able to demonstrate that they have been cultivating the same land for twenty years or more have the right to force the owner to sell the land to them. Because of the provisions of this law, owners are often fearful to rent land. This fear has aggravated an existing acute scarcity of land for rental. Many of the campesinos who used to rent lands are at the present unemployed. Rising unemployment and the knowledge that the peasants have of their rights under the law have resulted in a situation of rising tension between owners and renters, each side determined to preserve what it considers to be its rights.

Land invasions are one consequence of this tension. If an escape valve is not found, the phenomenon of land invasions will become commonplace in the area. The landowners have organized in order to put pressure on the central government to stop such invasions by force. The present government has tried to keep the situation under control by encouraging the peasants not to invade lands and at the same time not using force to suppress land invasions when they have taken place. However, the situation could conceivable degenerate into a show of force in which case either the land invaders will be crushed or the Government will accept de facto situation where progressive as well as traditional owners will have to abandon their properties.

4. Prospects for Change in the Basin

The system of traditional agriculture has not only created a conflict-ridden land tenure situation but also it has perpetuated characteristics that result in a low productivity

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of main crops grown in the area. The production of rice averages about 14 quintales of milled rice per cuadra.^{1/} The crop is lost partially or totally approximately one year in every five due to lack of irrigation. The typical method of rice cultivation by renters is based on the use of manual labor. The land is not plowed. The farmer usually clears the land with his machete, burns the weeds, and makes holes in the soft ground with sticks to transplant the rice that is already growing in seed beds. Weeding and harvesting is done by machete. Varieties of rice used include a number of undefinable strains known as "camilla," "chilano" and "brasilerio." These varieties have low productivity, poor quality and are not resistant to "carbon," a fungus infection which is common in the rice growing areas. Production is low because in most cases not even the most elemental modern techniques of cultivation are used. It is calculated that by full application of modern rice technology and double cropping productivity should increase to about 100 quintales per cuadra per year.

A few large landowners have started to introduce innovations in rice growing such as the use of fertilizer, improved varieties, irrigation and drainage facilities and use of machinery. These innovators, however, are generally afraid to make any further investments because they are not sure that their lands will not be invaded.

The situation is further complicated because in some parts of the Basin the campesinos have been subjected to extremist propaganda. Some of them have been convinced that the only way to obtain lands is through invasions and the use of force. The majority of campesinos will think that that lands can be obtained through peaceful means. However, their numbers will decrease if some means are not found to permit them adequate access to land.

A significant number of land owners are willing to sell their lands to campesinos provided that they have a definite assurance that they will be paid in a reasonable period of time. Campesinos are also willing to purchase land, provided the landlords accept payment over 5 to 7 years terms. The landlords, however, do not have confidence in the campesino's capacity and willingness to pay.

^{1/} One cuadra=1.74 acres or 0.70 hectares, one quintal = 100 pounds.

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The land reform program of the GOE administered by the Instituto Ecuatoriano de Reforma Agraria y Colonizacion (IERAC) is resisted strongly by the owners as they are reluctant to accept government land reform bonds that mature in a period of 15 to 30 years and sell at a discount of up to 40 percent. Furthermore, the valuation of the land for purposes of expropriation is made on the basis of the declared value for tax purposes which is usually less than 50% of the commercial and productivity value of the land.

In order to avoid violence and to increase productivity in the area, it is necessary to provide some means by which the willingness of many landowners to sell land and the campesino's desire to purchase land can be translated into mutually acceptable transactions. The objective of the project is to provide a formula to achieve this end. If successful, the project will lead to a shift from the traditional land tenure system of large absentee owners and landless campesinos towards a system of a few large and many small agricultural entrepreneurs organized in cooperatives who live on and work the land.

The project will be concentrated in the main rice producing area in the southern portion of the Guayas River Basin, some 700,000 hectares of which approximately 100,000 hectares are used for rice growing. It is estimated by the National Rice Commission that from 65% to 75% of this area is worked under the leasing system described above. This means that the potential reach of the project would be from 65,000 to 75,000 hectares. On the basis of a determination by the Ecuadorean Land Reform Institute (IERAC) that the minimum family farm in the area should be 10 hectares and assuming 6 of those 10 hectares in rice, the potential clientele for the program in the area would be from 10,800 to 12,500 families.

The project is scheduled to be started with people who have formed rice growing and marketing cooperatives under a project sponsored and financed by USAID. By the end of 1969, cooperatives that will be organized and able to handle the credit of the nature will have approximately 520 members. That is, it will be possible for cooperatives in existence to purchase over 5,000 hectares in the first year of operation of the project. It is estimated that, considering the past rate of formation of cooperative and the availability of personnel, it will be possible to attain cooperative membership of 2,500 families within the

next three years. This figure represents approximately twenty percent of farmers that might be possible beneficiaries of the project.

C. Project Description

The loan will assist in financing a program to promote agricultural development by making available to campesino cooperatives the requisites for successful agricultural enterprise: land, production credit, and technical assistance. The project will involve an integrated effort by public agencies of the Government of Ecuador and USAID to assist qualified cooperatives in securing land and developing on such land viable farm businesses thus making it possible to pay for land purchased and other inputs such as production credit and technical assistance.

The Borrower will be the Government of Ecuador. The administrator of the project will be the Banco Nacional de Fomento, an autonomous GOE agency with long experience in agricultural development operations. Technical assistance will be provided by personnel of the technical services of the Ministry of Agriculture and other government agencies and by the Supervised Agricultural Credit Department of the BNF all under the direct management of the BNF's Project Coordinator. The Project Coordinator will also be responsible for coordination with USAID and any other organization which may be involved in the project. The Project Coordinator will be responsible to a policy making board composed of representatives of the Ministry of Agriculture and BNF.

The objective of the project is to induce the sale of tracts of land held by landowners willing to sell their land to cooperatives and to provide credit facilities and technical assistance which will reasonably assure the capacity of these buyers to pay land purchase obligations. The land sales will be financed by the seller accepting 5 to 7 year payment contracts from BNF. The cooperatives in turn will enter into contracts to pay BNF the purchase price obligations. A portion of the loan will be held undisbursed as an ultimate guaranty against losses sustained by the BNF should a buyer cooperative fail to pay its debt and should it prove impossible to realize fully on the other forms of security available. To assure that the buyer of land will be able to work his property effectively and pay off his mortgage as soon as possible, the loan will also provide funding for the granting by BNF of production credit to buyers. Initial activity will be focused on the Guayas River Basin area in order to facilitate administrative effort, utilize highly productive land and relieve some of the most severe pressures for land distribution in Ecuador.

The project will be experimental in nature in that it is intended that the basic sub-project scheme described in this paper will be varied from time to time as opportunities arise. However, sub-project planning in a manner similar to the following typical transaction will always be insisted upon.

Identification, formation and qualification of a cooperative for assistance under the project will be the responsibility of Ecuadorian organizations but no sub-project will be approved without USAID clearance of the cooperative's qualifications.

When the cooperative is qualified for assistance under this program by reason of its capacity to carry out an effective enterprise, it will identify a property which it wishes to purchase from a willing seller at a reasonable price. The technical services of the Ministry of Agriculture and the Banco Nacional de Fomento Supervised Agricultural Credit Department will be called upon to analyze all aspects of the situation under direction of the Bank. If it appears upon analysis that the sub-project has the potential to achieve a viable enterprise in a manner consistent with the objectives of the program, appropriate personnel of the BNF and Ministry of Agriculture will develop a farm plan which will include a detailed analysis of technical agricultural considerations as well as financial planning. The proposed land tenure pattern for the property will be submitted in accordance with law to IERAC for approval. The project will then be submitted to the BNF management for its review and approval. USAID will satisfy itself as to the fairness of the purchase price through independent appraisal based on a land use and soil classification assessment.

When the qualifications of the cooperative, the farm plan and the purchase price of land are approved, the BNF will handle the execution of all necessary transactions to initiate the sub-project. Personnel of government agencies will continue to provide technical assistance in agricultural matters in accordance with the farm plan under BNF supervision.

The financial transaction to be handled by the BNF will be as follows: With respect to the purchase of land, the buyer cooperative will be expected to invest a minimum of 10% down-payment. The farm plan will reflect an appropriate period for amortization of the land purchase debt. Rather than a direct transaction between the seller and the buyer, the BNF will undertake to pay the purchase price to the seller over the same period as the buyer's amortization schedule for payment for the land. In turn, the buyer will undertake to pay to the BNF an amount equivalent

to the purchase price less downpayment in accordance with financing arrangements set out in the farm plan. This obligation will be secured by a mortgage on the land, crop liens and other appropriate forms of security.

In a simultaneous transaction, the BNF will enter into an agreement with the cooperative to provide production credit and any other type of credit found necessary under the farm plan to assure the economic viability of the enterprise. Production credit lending by the BNF will be secured by crop liens and will be carried out in the same fashion as the bank's usual supervised agricultural credit operations.

To assure that all necessary services are obtained by the buyer, a contract will be entered into between the buyer, the BNF and the Ministry of Agriculture in which the obligations of all parties concerned will be stipulated. This will include not only financial obligations but also the obligations of the BNF and the Ministry of Agriculture to provide technical assistance, the obligation of the cooperative in good faith to utilize the assistance provided, the agreement of the cooperative to handle marketing arrangements and similar aspects of farming operations during the period of the amortization of the land purchase obligation as agreed in the farm plan. Approximately \$100,000 of the proposed loan will be used to purchase vehicles and other equipment to service the program. A \$100,000 revolving fund for the payment of non-salary costs of administration of technical assistance provided by agencies of the GOE other than BNF will be established to be replenished from user charges included in the interest payments to BNF.

D. Program Justification

1. The Impact of the Project on Economic Development of Ecuador

Ecuador is and will remain in the foreseeable future an agricultural country. The richest and most important agricultural area of Ecuador is the Guayas River Basin. This is true despite present patterns of land tenure and restrictive economic relations between rich and poor which unfortunately have tended toward a limitation of production. As is demonstrated in more detail in the Economic Analysis, Section III E, any effort tending toward the improvement of agricultural production in the Guayas River Basin, particularly in the rice growing

areas, necessarily will result in economic benefits for the country. Various schemes dealing with development and improvement of agriculture in the Guayas River Basin have been proposed. While these proposals have been economically feasible, they have often centered on the increasing of the gross production of rice and other crops in the Basin without taking into account the social implications involved.

The proposed project will focus on the development of rice cooperatives and the improvement of the capacity of low income farmers to operate farm enterprises. While the basic objective of the program is social in nature, this should not mask the underlying economic rationale in support of the program. The balanced economic development of Ecuador is largely dependent upon the improvement of agricultural production and rice is one of the key commodities the production of which needs to be increased. This project will promote this objective. What is different about this proposal is that although it pursues meaningful economic ends, it deals with the social implications of economic development which if ignored will lead to social and political chaos even if substantial gains in gross agricultural production were otherwise obtained.

2. The Social Development Dimension of the Project - Title IX Implications

A unique feature of the proposed project is the strong Title IX orientation of a project otherwise justifiable entirely in economic terms. AID has strongly supported the development of the cooperative movement in Ecuador, not only through grant funded community development type activities but also through a dollar loan which established the Cooperative Bank and through PL-480 assistance of various types. This project will give a further strong impetus to the development of cooperatives in the Guayas River Basin as it will make cooperatives the vehicle for the campesino to obtain the means of making a decent living and owning his own land. The project will stress in implementation the assurance that the cooperatives involved are in fact operating on a basis fully consistent with the standards of sound cooperative enterprise.

As more cooperatives come into existence, secondary re-enforcement of the movement in Ecuador will follow. More cooperatives will join the Cooperative Bank, machinery pools, milling facilities

and other service organizations will become financially feasible as the total members of cooperatives and people actively engaged in cooperativism increase and the general desirability of this approach to development becomes apparent to more independent campesinos throughout the country.

The strong initiative toward agrarian reform generated by this loan will tend to put pressure on other institutions within the society, particularly the Church, to cooperate with and support social development activities. Both the Church and Government may thus be induced to distribute or make available for sale lands now held by these institutions for rental to campesinos.

Finally, a successful program of this nature will tend to increase confidence in the campesino as a businessman in the minds of the dominant elements in the society. As resistance to carrying on normal business relations with campesinos as an economic man becomes more apparent, the possibility of a fundamental shift of attitude toward the presently disaffected and alienated campesino group may make a true mutual acceptance on part of various elements in the society a fact.

3. The Place of the Project in the Country Program

The primary elements of AID strategy in Ecuador are (1) to promote and assist in effecting improvements in the social and economic conditions of lower income groups within the country and (2) to assist in meeting near and middle term threats to the economic stability of the country by promoting economic activities tending to improve the balance of payments position in Ecuador. The relation of the project to the first objective is, of course, obvious. The second objective is also supported by this program since the effect of land ownership, credit and technical assistance will be to improve agricultural production of export crops and reduce the dependence on imported agricultural commodities for which substitutes can be provided from within the economy.

This loan has the highest priority in the Mission program and is considered critical to AID's strategy in Ecuador. As such it has the Country Team's complete support.

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4. Relation of the Project to CIAP Objectives, U. S. Economy and Activities of Other Lending Institutions

The proposed program is wholly consistent with the CIAP country review position. The program has only a minimal direct effect on the U. S. economy in terms of procurement, but the economic development resulting from the project will open new markets for American products. There will be no immediate net balance of payments effect because the loan will be disbursed primarily through the special letter of credit procedure. In the event that claims against the undischarged portion of the loan (the guaranty fund) exceed local currency income from project operations, dollars will be disbursed under the SLC procedure to generate local currency for payment of such claims.

5. The Capacity of the Government of Ecuador to Carry Out the Project and Repay the Loan

As reflected in the Director's Certificate in Annex I, the Government of Ecuador is considered capable of carrying out its obligations under the project. As reflected in the Economic Analysis, Section III E, the Government of Ecuador is considered capable of repaying the loan in accordance with its terms.

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SECTION III - DETAILED DESCRIPTION OF THE PROJECT

A. The Borrower

The borrower will be the GOE, through the Ministry of Agriculture which is responsible for developing and implementing the agricultural policy of the GOE. The Ministry has representatives on the Board of Directors of all autonomous institutions that are involved with the agricultural sector, including BNF. A organization chart of the Ministry is provided in Annex IX.

An evaluation of the management capability of the Ministry of Agriculture necessarily will have to be made at the political and technical levels separately. The Ministry of Agriculture has proven to be a very unstable institution at the political level. The current Minister Dr. Angel Duarte Valverde, is the third since the Velasco government came into power on September 1, 1968. There have been three sub-secretaries as well. There have been no changes of Department heads however. The current top officials of the Ministry appear to be highly capable men but it must be conceded that it is entirely possible that these men will be out of office in the near future.

Below the two top men, the Ministry has remained quite stable. Department heads have remained in their jobs for a number of years in most cases. Most of these people are specialists in their field, and many have received training outside of the country. The Mission considers the Ministry to be competent at the middle management level.

At the technical level, the Ministry has a number of trained personnel to undertake a program of technical assistance such as the one contemplated under this project. Primarily because of budgetary problems, the technical staff of the Ministry in many cases does not have the opportunity to do an adequate job of technical assistance to agriculture. Often, technicians cannot go to the field because of the lack of transportation facilities and funds to pay per diem and other expenses. These technicians will form the core of the staff that will provide technical assistance to the beneficiaries of the project. The project assures that they will be able to carry out their responsibilities by providing for procurement of vehicles and supplies and a revolving fund for local currency costs of these services which will be financed from user charges. (See generally under Technical Assistance)

It can be concluded that although the Ministry of Agriculture has proved to be a very unstable institution as far as top personnel is concerned, it is a stable and competent institution at the operating level. It is not an effective institution at the technical level for financial reasons to which the loan will address itself. In the view of the Mission, properly assisted the Ministry can handle the technical assistance job.

B. The Administrator - The National Development Bank (Banco Nacional de Fomento)

1. Organization and Administration

The BNF was given its present organization as a private institution with administrative and financial autonomy, by Executive Decree No. 2767 of December 1, 1964. The Bank is a financially and administratively autonomous institution of the GOE, whose principal purpose is "to promote and accelerate the country's economic development through broad and adequate credit activity"; it has authority to perform the following functions:

- (1) grant credit to promote agriculture, fishing, small industry and crafts;
- (2) receive long and short-term financial and savings deposits;
- (3) accumulate domestic savings through the issue of credit documents negotiable in the securities market;
- (4) obtain loans, discounts and advances from the Central Bank and other national financial institutions;
- (5) obtain credit from international financing agencies;
- (6) administer, as a trust, special funds established by the GOE, national and international financing agencies for specific purposes of agricultural development;
- (7) implement technical assistance programs to improve the conditions of rural workers;
- (8) promote the organization of farming, fishery and handi-craft production cooperatives;

- (9) encourage stabilization of agricultural and commodity prices at levels remunerative to the producer by eliminating an excessive number of middlemen in marketing, or seeking solutions to storage problems;
- (10) engage in any activity designed to expand agricultural productivity and rural welfare.

A general reorganization of Ecuadorean development institutions was carried out in 1964 on the basis of recommendations by a team of foreign experts partially financed by AID. This operation was contracted in 1962 by the then Development Credit System later superseded by the BNF in 1964. The contractor presented its recommendations at the end of 1963. The BNF's present organization generally reflects the result of this technical assistance operation. Various operating procedures adopted since the Bank's establishment incorporate almost all the principal recommendations made.

The decree reorganizing the banking system and creating the BNF made several important changes into then existing system. It removed from the Bank responsibility for sponsoring major industrial development schemes. It provided for the creation of a Division of Supervised Credit thereby establishing the Bank's responsibility to help out the weaker sectors of the agricultural, artisan and industrial economy through the provision of Supervised Credit and it converted the semi-independent provincial banks of the system into branch banks of the BNF, totally under headquarters control.

The BNF is domiciled in Quito and has 35 branches in the provincial capitals and other important cities. The Bank has 926 employees - 196 work at headquarters in Quito and the other 730 in the 35 branches. Two hundred eight of the Bank's employees are professionals, and ninety-seven have had specialized courses. Approximately 33% of the Quito staff has taken advanced courses, but only 20% of the staff of the branches have done so. Because of a recognized

shortage of professional personnel in the various branches with the capacity to carry out the proper evaluation of credit applications and control of project execution, the Bank has organized a series of specialized courses for branch managers and inspectors.

The BNF is directed and administered by a Board of Directors, an Executive Committee and a General Manager. The Board of Directors is the highest authority of the BNF and is composed of seven regular members, one appointed by the President of the Republic, three by the three regional Chambers of Agriculture, one by the Planning Board, and one by the Monetary Board. The regular members elect the Chairman of the Board of Directors for a two-year term. He may be reelected indefinitely. The other members, with the exception of the one appointed by the President of the Republic, hold office for a period of four years and may be reelected only after a four-year period has elapsed. The Board determines the Bank's general policy and each year elects from among its membership the regular members of the Executive Committee; it also appoints the General Manager for a four-year term; which may be renewed indefinitely.

The Executive Committee is composed of a General Manager, who presides and two regular members elected by the Board of Directors. The Commission distributes the available resources among the various branches of the bank, sets the autonomous operating limits for each, and appoints their managers.

The Bank has recently made important changes in financial administration. The operations of its 35 branches have been centralized, the system has been unified, a new code of accounts has been issued, and the movement of resources among the different offices has been systematized. In addition, accounts have been mechanized at headquarters with IBM equipment which will provide better control over the loan portfolio. This is an important step forward because previously the Bank did not have an accounting system which allowed strict control over its loan portfolio or which would provide information as a basis for dividing the portfolio by degrees of age and delinquency, by type of borrower, geographic area or economic sector.

2. Operating Problems

The Bank has had some serious problems which it is now trying to overcome. The most serious are (1) the annual amount of unrecovered amortization payments, which has averaged about 25% of annual amounts during the last four years, and a high percentage of renewals, which declined from 21.8% of the due portfolio in 1965 to 14.9% in 1967; (2) high operating costs, which amounted to about 6% of the total portfolio in the last few years; (3) a rather unsatisfactory record on profits, which represented 1.7% of capital funds in 1965, 2.3% in 1966, and declined to 0.9% in 1967; and (4) professional weakness at the branch level.

The delinquent loan problem has several causes. The Bank, being an institution heavily dependent on the Central Government for its capital (see below), is not invulnerable to political pressures by large land-holder-borrowers. The fact that three of the seven members of the Board of Directors must be representatives of the three regional Chambers of Agriculture--as well as the fact that the designees of the Planning Board and the Monetary Board are usually large landholders--does not help to insulate the Bank from this pressure. The proposed project has been designed so as to protect it from this possible source of landholder pressure by requiring that (1) AID make its own evaluation of land price; (2) have a veto power over the granting of a guaranty transaction that is considered above a reasonable price and (3) make an independent screening of the borrower and have veto power over his approval.

Another important factor contributing to the Bank's high delinquency ratio relates to the shortage of capital with which the Bank operates and the consequent tendency to lend for shorter periods than are justified given the anticipated productivity of the project being financed. As shown in the table below, 14.9% of the Bank's payments due in 1967 were recovered by loan renewals. These renewals usually resulted from the fact that the Bank originally scheduled unrealistically short amortization periods. In that the proposed project requires AID and Ministry of Agriculture technical assistance in preparation of the farm plans, there will be outside controls on the land and credit amortization periods granted by the Bank.

The Bank's unsatisfactory collection record reflects the fact that not all members of the Board of Directors in the past endorsed the idea that a government-sponsored bank, set up to stimulate development in agriculture and industry, should be a profit-earning institution. Since the proposed project will require that the Bank demonstrate before it can make a claim on the guaranty fund that it has sought and obtained a judgment and has attempted to act upon it, it is believed that there is sufficient assurance that the Bank will exert full efforts to collect the land amortization payments under this project. Finally, it should be noted that the percentage of BNF loan delinquency rises with the size of the loan - indicating that it is the large rather than small borrower who is the major contributor to this problem. In that the proposed project will deal exclusively with small borrowers, the delinquent loan problem will be correspondingly less serious.

The Bank has shown improvement on one delinquent loan question in recent years. Year-end delinquencies in 1967 represented 28.6% of payments falling due in that year; by the close of 1967, this proportion had dropped to 23.8% (see table below). In addition, the Bank has committed itself, under the newly authorized IDB loan for US\$6 million, to undertake a comprehensive program of delinquent account collection (see Annex IV). As part of this program, and as condition precedent to the annual disbursements under the loan, the Bank has committed itself to reduce the proportion of its delinquent portfolio by a fixed percentage each year so as to arrive at no more than 15% by 1972.

The Bank's low profits are to a considerable extent a function of its high operating costs, which result in part from the necessity of the Bank to maintain branches in certain areas for developmental reasons even though the volume of business may be insufficient to justify a branch on purely commercial grounds. Although the Bank's profits are low, they represent an improvement over the pre-1965 period, when it was recording repeated annual losses--S/6,655,000 (US\$369,722) in 1963, and S/3,066,000 (US\$170,333) in 1964. The improvement in the profit situation since 1965 is basically a result of the decrease in the interest paid by the Bank on the money that it borrows; which has come

down from a level of approximately 3.5% in 1964 to 1.9% in 1967. This has enabled the Bank to continue accumulating profits, though at a low level, despite its relatively high administrative costs.

With reference to the problem of professional weakness at the branch level, the Bank has recognized the problem of attracting professional personnel to its branches. To this end, it has organized training courses and has sent three professionals abroad for advanced studies. Moreover the Bank has seen to it in recent years that the post of inspector in the branches has been filled by graduates of the practical agricultural schools and technical trade schools located in the branch region.

It is the Mission's belief that the Bank is fully aware of the problems outlined above and is making serious attempts to deal with them. In September, 1966, an Ohio State University Team, contracted by AID to conduct an analysis of the Bank, reported that despite the type of problems outlined above, the Bank (1) was not in critical financial condition or in danger of bankruptcy, (2) was held in good repute by farmers, private bankers, the Central Bank, and the Superintendent of Banks, and (3) had made substantial improvements in management both at headquarters and the branches. The Inter-American Bank, in its evaluation of the Bank's performance under two past loans totalling US\$7.4 million equivalent, reported that the Bank (1) had fulfilled virtually all the conditions set forth in the loan contracts, (2) had met all payments of principal and interest, (3) had demonstrated great ability in channeling the distribution of resources, and (4) had improved its financial administration in recent years, owing largely to measures adopted to increase the level of recoveries and reduce the percentage of renewals.*

3. Sources of Financing

The sources of BNF finances are as follows:

(a) Central Government Revenues. Decree No. 2767 provides that the authorized capital of the BNF shall amount to S/1 billion (US\$55,550,000), contributed entirely by the Central Government. As of December 29, 1967, the capital account amounted to S/485,132,763 (US\$28,118,486).

Three Executive Decrees establish the compulsory contributions to the Bank's capitalization to be made annually by the Central Government.

- (1) 80% of the 25% of proceeds from the 40-centavo tax on each stem of bananas exported by El Oro Province (Decree 674, March 31, 1964); in 1968, the Bank received S/397,100 (US\$22,100) from this source;
- (2) up to S/30,000,000 (US\$1,660,000) annually from export taxes (Decree 252, May 13, 1966); the Bank received this amount in 1968; (3) S/20,000,000 (US
- (3) S/20,000,000 (US\$1,100,000) annually from the proceeds of the monetary stabilization surcharges, or, in their absence, from direct allocation in the Central Government budget; the Bank received this amount in 1967 and 1968.

Total contributions to the BNF by the Central Government from these sources have been S/27.2 million (US\$1,150,000) in 1964; S/29.9 million (US\$1,660,000) in 1965; S/62.9 million (US\$3,490,000) in 1966; and S/50.5 million (US\$2,805,333) in 1967 and in 1968.

(b) Access to the Central Bank. The BNF obtains resources from the Central Bank for short term programs through the system of advances and rediscounts of negotiable documents from its own portfolio. These operations are carried out for terms of not more than one year, and the interest rate charged to the BNF by the Central Bank is 3%. As of June 30, 1968, the BNF obligations to the Central Bank for advancements and rediscounts amounted to S/144,000,00 (US\$8,000,000).

(c) Public Sources. The BNF may utilize financial services of the Securities Commission-National Finance Corporation for rediscounts of credit documents for the purpose of loans to crafts and small industries. These operations are conducted on terms of up to five years, and interest rates of up to 4% per annum.

(d) Private Sources. Savings and sight deposits constitute a short-term source of funds for BNF credit. As of December 29, 1967, these deposits amounted to S/28.8 million (US\$1.6 million).

(e) External Loans. In 1961, the Interamerican Development Bank approved a loan of US\$2,365,000 equivalent to the then National Securities Commission for the financing of a general program of credit for African Palm cultivation. In 1967, US\$1 million was deobligated because of a smaller demand than was initially anticipated, due to the heavy per hectare investments required, and the long gestation period (up to six years for initiating production). Of the remaining total of US\$1,365,000 equivalent, almost all was disbursed as of December 31, 1968. In 1962, the IDB granted a US\$6 million loan to the then National Securities Commission for financing with intermediate and long-term credit the development, diversification and systematic organization of farming, livestock, forestry, fishing, industrial and craft activities in Ecuador; by June 1967, the loan had been totally disbursed. In 1969, the IDB authorized a third loan to the BNF for US\$6 million to continue its program of financing the development of agriculture, as well as small industry. Apart from IDB loans, the BNF has two lines of credit from French and Czech suppliers, amounting to approximately US\$1 million equivalent. The French credit were initiated only recently.

4. Financial Position

The following table summarizes the balance sheets of the Bank as of the close of 1965, 1966, 1967 and 1968. The Bank's assets have increased modestly in recent years. The decrease of S/ 19.8 million (US\$1.2 million) in 1966 is a result of the Bank's adjustment of its capital account and assets in that year by S/112.0 million

BNF: SUMMARY BALANCE SHEETS, 1965-1968^{a/}

(Equivalent in US\$millions)

<u>Assets</u>	<u>1965</u>	<u>%</u>	<u>1966</u>	<u>%</u>	<u>1967</u>	<u>%</u>	<u>1968</u>	<u>%</u>
Cash and banks	3.3	4.9	5.2	7.7	4.9	6.5	6.2	7.2
Investments	14.1	20.8	13.1	19.7	11.4	15.4	13.4	15.7
Portfolio	43.7	64.5	43.4	65.2	51.6	69.7	56.1	65.8
Other assets	<u>6.7</u>	<u>9.8</u>	<u>4.9</u>	<u>7.4</u>	<u>6.2</u>	<u>8.4</u>	<u>9.5</u>	<u>11.1</u>
Total Assets	<u>67.8</u>	<u>100.0</u>	<u>66.6</u>	<u>100.0</u>	<u>74.1</u>	<u>100.0</u>	<u>85.2</u>	<u>100.0</u>
<u>Liabilities</u>								
Callable on demand	9.7	14.3	10.6	16.0	11.6	15.6	13.5	15.8
Callable on short term	6.4	9.4	7.7	11.6	7.8	10.5	12.2	14.3
Callable on long term	19.5	28.7	17.9	26.9	21.5	29.0	17.2	20.2
Other liabilities	4.6	6.8	5.0	7.5	5.1	6.9	7.0	8.2
Net Worth	<u>27.6</u>	<u>40.8</u>	<u>25.4</u>	<u>38.0</u>	<u>28.1</u>	<u>38.0</u>	<u>35.3</u>	<u>41.4</u>
Total Liabilities	<u>67.8</u>	<u>100.0</u>	<u>66.6</u>	<u>100.0</u>	<u>74.1</u>	<u>100.0</u>	<u>85.2</u>	<u>100.0</u>

a/ As of 12/31

C. The Operation of the Project

1. Identification and Formation of Beneficiary Cooperatives

The beneficiaries of the program will be legally organized cooperatives. In the formation of such cooperatives, various types of organizations such as corporations, labor unions, communes and villages, or traditional groups of indigenous population may be considered; but, at the request of the GOE, the cooperative legal form will be required.

The basic plan of the project involves Ecuadorean organizations undertaking responsibility for the identification and formation and development of cooperatives to the level where they meet the criteria for support for organizations under the program. As noted subsequently, development agencies will be invited and encouraged to participate in the program in connection with the identification and development of qualified cooperatives. An organization of Ecuadorean personnel previously employed by the USAID for cooperative formation activities will be the key agency for this activity.

In assessing the validity of the approach taken in this project and the capacity of ex-USAID personnel to handle the cooperative formation function, a description of the current grant funded programs of this nature would be useful. USAID experience in cooperative formation and development dates back to 1961. A general survey of the Ecuadorean Cooperative Movement and USAID's experience with it is provided in Annex V. With respect to the Guayas River Basin rice lands, USAID interest has been substantial and its experience particularly appropriate to operations under the proposed Project as reflected in the following paragraphs.

In early 1968, USAID formed a team of cooperative fieldmen to begin the organization of cooperatives among small rice growers in the Guayas River Basin. Although the original intention of the program was to organize marketing cooperatives similar to the coffee cooperatives in which USAID/CLUSA had had extensive experience, a study of the situation of the small rice growers in Ecuador--who grow perhaps as much as 75% of the country's rice--led to the conclusion that new methods of production would have to be emphasized along with marketing arrangements. It was also recognized that the willingness of the small rice farmer to adopt methods of production would be limited unless he was assured more secure tenancy arrangements, or even better, land ownership. Most important for this project, it was found that there are good prospects for small rice farmers

to purchase land because many landowners in the Guayas River Basin are willing to sell land at prices that are favorable to small farmers in comparison with the rentals they are now paying. The major obstacle to land sales to small farmers has been the lack of an effective mechanism for bringing together buyers and sellers.

In sixteen months of operation, the USAID/CLUSA project has assisted in the organization of nearly 20 cooperatives of which nine are now fully legalized under Ecuadorean Cooperative law. Two of these cooperatives have entered into land purchase agreements for a total of 980 hectares and a third cooperative organized by credit union extensionists purchased some 350 hectares. Additional details on these transactions are provided in the Financial Analysis, Section III, D. The USAID/CLUSA agricultural cooperative program provided the assistance necessary for preparing and processing loan requests for these purchases to credit institutions. This work included topographic studies, plans for irrigation and drainage and plans for production improvements. Similar surveying and irrigation design was done on production capitalization plots in a number of other cases where cooperatives were able to secure long term leases.

Through agreements with the National Rice Commission and the Extension Service of the Ministry of Agriculture, two experienced rice technicians paid by their GOE agencies have been assigned to work with the USAID/CLUSA team. Some travel and per diem expenses of these technicians were covered by USAID grant funding. Use of GOE personnel through such arrangements has proven to be highly satisfactory.

As the program began its second year, the team reached its full personnel strength of sixteen: a project director, a coordinator of legal, educational and public relations matters; five extensionists; two accountants; two agronomists; a civil engineer; two topographers and two secretaries. This represents a total budget of about \$60,000 per year. With this team it is expected that twelve new cooperatives averaging 50 members working about 10 hectares of land each can be organized in a year. Of these cooperatives, about eight will probably be in a position to buy land.

Until the present, the rice cooperative program has concentrated on creating strong base level support for the formation of a Federation of Rice Cooperatives. The selection of cooperative groups for USAID attention has been made to date on the basis of their potential support of this Federation.

In relation to the present loan project, or course, new criteria would enter the picture for the selection of possible beneficiary groups.

In addition to the currently operating team, USAID will provide additional resources of perhaps equal size and cost to the cooperation described above to handle the land sale program. The field teams will concentrate on locating groups interested, willing and able to enter into land purchase arrangements and then assist them to take advantage of various government and private resources in the proper use of their new land. The formation of a Federation would still be a significant aim but would be secondary and thus allow more time for the supervision of land transfer. The present rice cooperative group plus additional personnel could handle the support necessary for the transfer of 5000 hectares the first year and 10,000 the second year.

While the basic plan calls for the USAID spin-off handling the entire job of cooperative identification and formation, this arrangement will hopefully be only a temporary measure, principally during the pilot project period, in order to simplify procedures and assure necessary resources for the early stages. There are a large number of other organizations in Ecuador involved in providing various forms of technical assistance to rural groups. Many of these could take an active part in locating, promoting and strengthening cooperatives for the project. These organizations vary in experience and resources. It is hope that as soon as possible several can join in the project. Certainly after a year's experience, others can be encouraged to prepare personnel and take over part of this responsibility.

At present, the most capable organization of this kind in the rice area is Centro Ecuatoriano de Servicios Agrarios (CESA). This non-profit group hires technical personnel to provide legal counsel, accounting and other services for cooperatives in the Guayas area charging the use only part of the costs of these services. As the program carries to other geographical areas, groups like Centro Ecuatoriano de Accion Social (CEAS) in Riobamba, the Instituto Campesino of Ibarra, Centro de Reconversion Economica de Ambato (CREA) and others which are currently providing assistance to cooperatives can form part of the program. In the future, various other cooperatives can form part of the program. In the future, various other cooperative service organizations can also provide assistance

such as the Federacion de Cooperativas Agropecurias de Produccion y Mercadeo, Union de Cooperativas de Ahorro y Credito, and the Federacion de Cooperativas Arrosceras. In addition the rural labor movement can also play an important role. Federacion Nacional de Organizaciones Campesinas (FNOC) of the Catholic labor family and Federacion Nacional de Campesinos Libres del Ecuador (FENCLE) of the free labor movement are possible candidates.

The problem of the Institute for Agrarian Reform (IERAC) is discussed in Section III G, but several points should be mentioned here. The Agrarian Reform Law provides for establishing procedures for the Institute to implement and encourage land distribution under private initiative. Little was done to put this part of the law into practice due to lack of financial and political support. However, this is an aspect of agrarian reform that should rightfully fall under the control of the Institute. This is not to suggest that (IERAC) can or should immediately assume the responsibility for part of this program. The Institute is presently thoroughly disorganized, demoralized and decapitalized. It may be moved from autonomous status to a dependency of the Ministry of Agriculture. Therefore, it is impossible at this time to establish any mechanism for IERAC's participation. However, when IERAC is ready to enter into serious commitments, it should become a part of the program. It is hope that during the pilot phase of the program working relations with the Institute will develop and the technical expertise in land tenancy of that organization can be drawn upon more and more, thus providing the field base and practical operational experience for future formal IERAC participation.

Another resource that may be drawn upon to support this program is that of private Ecuadorean consulting firms. Such companies may be contracted in specific cases to provide part or all of the technical assistance for cooperatives under the supervision of the BNF and the USAID.

Whatever may be the nature of an organization seeking the benefits of this project and whatever the source of assistance in formation and development of this organization as a cooperative, USAID will be responsible for determining its qualifications for participation in the program. This is in effect a veto which is considered necessary at this time to assure that chances of success are maximized. The project will stand

or fall on the quality of the cooperatives assisted and there does not appear to be an alternative to USAID exercising its judgment on the cooperatives qualifications.

The criteria to be applied in determining whether or not the organization is qualified will include the following:

1. Potential cooperative buyers must furnish proof that they own less than the amount of land considered sufficient for subsistence. Such proof can be provided by a certificate from the office of property registration.
 2. There must be an adequate legal basis for land ownership. The legalization of the cooperatives provides this basis.
 3. Educated leadership.
 4. Established accounting system.
 5. Paid manager.
 6. Cohesive membership participating in cooperative activities as exemplified by attendance at meetings and capacity for group decision making.
2. Project Development and Approval

When a cooperative (identified or formed by any organization) receives preliminary clearance as a candidate from USAID, the process of project development will be initiated.

The BNF Project Coordinator will be notified by USAID of preliminary clearance and he in turn will notify all interested agencies that the qualified cooperative will be a candidate for a sub-project. The Ministry and BNF will have the right exercise a similar preliminary clearance and he in turn will notify all interested agencies that the qualified cooperative will be a candidate for a sub-project. The Ministry and BNF will have the right exercise a similar preliminary clearance. When preliminary clearance has been obtained from all interested organizations, the Project Coordinator will take over administration of the sub-project and will be responsible for coordination of matters affecting the sub-project with all interested agencies.

The project development process will involve three major activities: locating and negotiating for an appropriate piece of land, determining the value of the land through standard land classification and evaluation procedures, and developing of a farm plan which will include not only a financial plan for the enterprise but also a detailed analysis of all necessary agricultural inputs, technical assistance requirements and the like.

Locating and negotiating for land will primarily be the responsibility of the cooperative. It is anticipated that in most cases the cooperative will be able to handle this element of the project itself with little more than technical assistance and advice from cooperative advisors and the Federation of Cooperatives of which it is a member. The foregoing has been experience of the USAID cooperative advisory personnel in the three transactions of this nature carried out to date. Assistance was rendered in each case in such matters as negotiations with financing institutions but for the most part the cooperative handled negotiations with the seller itself. Indeed the capacity to carry out this aspect of the project may well be indicative of the ability of the cooperative to carry on other business transactions related to the project and hence bears on the question of the qualification of the cooperative for support. It is recognized, however, that under certain circumstances assistance may be required in finding land or in negotiations. Provided that in the judgment of USAID the rendering of assistance in these matters does not lead to a situation of expensive dependence by the cooperatives such assistance will be provided. The Project Coordinator will be in charge of obtaining and coordinating such assistance as is required.

It is anticipated that in the usual case the land to be purchased will be occupied by the cooperative or some of the cooperative members as renters or that the land will be located near the homes of the cooperative members. If the land is located at some distance from the homes of cooperative members, consideration will be given to the question of whether the distance will affect the feasibility of the project. In any event, the farm plan will take into consideration where appropriate the problem of the transportation of cooperative members to the land to be worked.

As noted in the IRR, USAID considers the question of land valuation to be one of the most important problems involved in the implementation of the program. This problem is discussed in Annex VIII. Clearly, an excessive valuation of land with guaranty backing would not only make it more difficult for the cooperatives to carry out their undertakings but also there is implicit in overvaluation an invitation to collusion. The Mission is of the view that the safeguards built into the program as now conceived fully resolve the concern expressed in the IRR.

At the outset, the determination of price through the free market system is itself the best guaranty of pricing. The BNF as a responsible and experienced banking institution can, in the Mission's opinion, be depended upon to be a reliable judge of land prices which it will be obliged to pay. An expensive land price will threaten not only the land purchase payment but also the production credit element of the transaction with respect to which the BNF also carries the risk. The direct involvement of USAID personnel will be still another safeguard in this matter. Notwithstanding the foregoing, the Mission considers it appropriate to add one additional objective safeguard to assure the validity of guaranteed land purchase prices. Each transaction under the program will be subject to land use classification evaluation by an independent contractor which will be responsible only to USAID. The land use classification operation will be established by the Mission with TDY assistance from the Agricultural Division of AID/W, LA/DR. A contract will be entered into with an engineering firm with appropriate personnel to carry out this type of activity. In operation, each proposed transaction will be submitted for appraisal by the Contractor. If the negotiated price exceeds the appraised value by a determined amount, the USAID will refuse to approve the deal. At this point, the parties may negotiate further or the cooperative can seek land clearance.

The key activity in sub-project development will be the development of the farm plan. This plan is seen not only as the legal basis for approvals but also as a device to help the cooperative organize data about its farm in such a way so as to help it make the best possible decisions regarding the business enterprise. Thus the farm plan is conceived not merely as a prerequisite to be filed with a loan application but as an educational instrument by which the cooperative can

realize its true potential to make decisions as an organization. If it fails to realize this potential, it probably will continue to be a poor and unproductive enterprise.

The farm plan will involve a full statement of business inputs and outputs. Inputs include the farm inventory and all those resources available to it at the time. It will consider information about its land, such as soil fertility and classification; labor supply; and all existing capital items such as tools, machinery, building, and livestock; and those items available in the marketplace such as credit, seed, and fertilizer. Output items considered will include farm yields and sales value of all products leaving the farm experienced and projected. In addition, information can be secured from experimental stations about potential yields, markets and prices. The basic function of the plan is to divide the farm operation into all its component parts and then to analyze each of these parts so as to be able to make necessary changes to establish an efficient commercial operation. A special kind of technical assistance will be required in preparing the plan. Cooperatives are ideally set up for this effort in that they assume the necessity of an educational effort and a change from traditional forms of agriculture. As noted, agents of various institutions can be trained in this approach which is part of the current USAID cooperative training program. Improvement in technical assistance practices of GOE technicians will be an extra dividend of the project.

When the farm plan has been developed, it will be submitted to all interested agencies for their approval or comments. The BNF will review the farm plan in its Supervised Agricultural Credit Department. As noted in the analysis of the BNF presented in Section III B. 2, this department is a working organization with experience in supervised agricultural credit. The usual procedures of this organization will be applied and through the normal workings of the bank approval of the various transactions which the BNF must undertake will be obtained from bank management. A description of these procedures is provided in Annex IV.

The Ministry of Agriculture will not be required to approve the farm plan although in all likelihood it will insist upon approval of the farm plan before the BNF will be allowed to sub-lend under this program.

The proposed farm plan will be submitted to AID for its information. However, it is intended that USAID's contractual rights to approval of specific transactions will be limited to approval of the qualifications of the cooperatives, approval of the purchase price of the land sale to be guaranteed, and a legal clearance to assure the consistency of the project with the terms of the loan agreement. The USAID considers a detailed review and approval of the farm plan to be unnecessary in light of the capacity and experience of Ministry personnel and the BNF in these matters, the excessive and unnecessary administrative burden on USAID and finally because approval at that level would be an unjustified incursion into a decision making process which should be to the maximum extent feasible entirely within the Ecuadorean Government and its agencies. It is considered that the specific points of approval retained by AID and the general involvement of USAID personnel in the cooperative formation process is a more than adequate protection of USAID interests in the program.

3. Technical Assistance

The technical assistance operation under this program is considered to be of great importance even though, as demonstrated in the financial analysis, the program would be economically feasible even assuming that only traditional methods of agriculture were utilized by the buyer cooperatives. Increases in production and income of cooperatives when improved farming methods are utilized by the buyer cooperatives. Increases standard of living of cooperative members. It is felt that nothing can bind disaffected campesinos to the economy and to society as a whole as effectively as this. In consequence, the project has been designed in such a fashion to assure the availability of sound technical assistance. Once the financial responsibility of a cooperative participant in the program is established, continuing efforts will be made to up-grade the technological level of the farming activities carried on.

A number of organizations within the Ecuadorean Government presently have on their payrolls competent and interested technical advisors who are capable of carrying out the type of work which is considered desirable under this project. The reason that technical assistance from these organizations under present circumstances is ordinarily rather ineffective is the fact that budgetary restraints on the organizations in question tend to make impossible for the technicians to get into the field on a regular basis to do their work. Thus it is quite common for competent field men to sit in offices in Quito rather than working the field because of the unavailability of vehicles, gasoline, travel expenses, and the like. The project is designed to assure that these requirements are available.

The financing of local currency costs of technical assistance will be handled in the following manner. \$100,000 of the loan will be available for disbursement into a technical assistance expense revolving fund through SIC procedures. This fund will be operated by the Coordinator of the project, a BNF employee. Approximately 30 employees of the Ministry of Agriculture, the National Rice Commission and IERAC will be assigned to the program. These individuals will continue to receive their salaries from their parent organizations. However, costs of travel and related expenses will be paid by the BNF from the

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revolving fund. It is estimated that these costs will amount to approximately \$2500 per man per year. The employees will be responsible to the Project Coordinator rather than their parent organizations. The revolving fund will be replenished by the BNF from the interest payments made by the cooperatives on the basis of 2% of total production credit outstanding. Vehicles and other commodities required for the program which can be secured in the U.S. will be purchased by the Ministry of Agriculture from the \$100,000 allocated under the loan for that purpose and assigned to the Coordinator for use in this project.

Several types of technical assistance will be financed under this procedure including survey engineering, agricultural engineering, farm planning, and agricultural technical assistance. Land surveying engineering will be carried out by two groups each of which will be composed of an agricultural or civil engineer, two topographers, one axeman, one chainman and one draftsman.

The program will also require one agricultural engineer land and soil expert to make soil and land capability surveys and gather soil samples for chemical analysis. The work of this individual will duplicate the land classification and soil analysis carried out independently by a contractor for the USAID. However, it is felt that this work should be handled within the GOE for general purposes of the project while the USAID contract for these services is intended solely as an advisory service to the Mission to assure the accuracy of valuation of the land to be purchased.

Development of farm plans will be the responsibility of another technical group composed of an agricultural economist, an agricultural engineer, and animal husbandry specialist, a rural planner and a forestry specialist. These five technicians will work as a team in the preparation of farm plans for the cooperatives involved. The group will also work with any BNF supervised credit technicians who the bank may assign to a specific sub-project.

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three cooperative extensionists and three accountants who will be assigned to particular sub-projects by the Project Coordinator as needed from time to time.

The Mission is of the view that with the foregoing technical assistance, the availability of which is assured by the establishment of a revolving fund, the payment of user charges and the assurance of the appropriate utilization of such technical assistance by management control through the technical assistance has been provided.

Each of these teams can process approximately 500 hectares per month. Since it will be virtually impossible for these teams to work during the rainy season because of the inaccessibility of most areas of the basin during that time, it is estimated that each team will be able to work for 8 months thus processing a total of 8000 hectares per years. This exceeds during the first year the area which probably will be under consideration for financing since the limiting factor in program progress is cooperative formation rather than capacity to give technical assistance or credit availability but lead time will be required for this work. During the second and third year an additional team of 5 members will be put in the field to meet the anticipated increase in demand for technical assistance services.

4. Financial Transactions

When all appropriate reviews and approvals have been obtained, the BNF will take over administration of all financial elements of the project. The individual sub-project will involve three elements: the purchase of the land, the providing of production credit and the assurance of availability of technical assistance. The sub-project is a package deal and no one element will be available without the other two. However, for purposes of analysis in this paper these three elements will be dealt with individually.

The most complicated element is that involved in the land sale transaction itself. It is to this transaction that the "guaranty fund" pertains and involved in this transaction is a fairly complicated series of legal arrangements. But this

level of complexity is to be expected. It is, after all, the availability of land titles which has been identified as the central cultural and institutional obstacle to the social and economic development of the campesinos affected. The existence of such structural obstacles suggests that simple solutions are not available, and indeed they are not. This project is designed to overcome these structural barriers within the Ecuadorean society which to date have seriously limited access of campesinos to land ownership.

Various legal dispositions and policy decisions by the BNF as well as the desire of USAID to keep the transactions involved inasmuch as possible within the control and responsibility of BNF have resulted in the conclusion that the land purchase transaction must be handled as follows: The land sale transaction will be a three party agreement with the BNF, the seller and the cooperative buyer as signatories to the agreement. Under this agreement the seller will transfer title to the buyer; the buyer will agree to pay to the BNF the purchase price of the land (less minimum down payment of 10%) on a schedule determined by the farm plan to be an economically feasible amortization period; and the BNF will agree to pay to the seller the purchase price over the same period as the BNF will receive payment from the buyer. Under this tripartite agreement, the mortgage and any other security made available will run in favor of the BNF. The seller will look exclusively to the BNF and will not retain rights against the cooperative in the event that the BNF defaults in its obligation to the seller. The seller will not retain rights against the cooperative if the cooperative defaults on its obligation to BNF.

USAID has satisfied itself that the foregoing type of transaction will be satisfactory to sellers. In this connection, see Annex III which describes the evaluation of land-owner attitudes undertaken by the Mission as part of the intensive review of this project. It is recognized that it might be desirable for social reasons as well as simplification of the transaction that the seller and buyer deal with each other directly with mutual obligations supported by a third party guaranty from BNF. Unfortunately, legal dispositions prevent BNF from entering into guaranty transactions of this nature. Of course, the transaction could also be simplified if the seller was paid in full upon sale from bank funds but such an

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arrangement would amount to nothing more than the establishment of a mortgage banking service with AID financing. No leverage effects would obtain and the scope of the project would thus be seriously limited. It appears that the only way to achieve the "money creating" effect of the seller accepting a time obligation rather than cash for the sale of his land is to handle the transaction as outlined above.

The transaction will be secured by a standard mortgage and such other security as may be available including crop liens. As noted in the following paragraph, the ENF will be wholly at risk with respect to production credit in contrast to the "shared risk" procedure in the land sale transaction and hence it is appropriate that crop liens run initially to the benefit of the ENF for credit extended for production credit purposes. However, the secondary beneficiary of crop liens and the primary beneficiary of all other security obtained in the transaction will be the ENF land purchase obligation. Under Ecuadorean law, crop liens can run with the land thus assuring a claim relating to the land purchase transaction in the event of default.

The second element of the sub-project financing package will be the provision of production credit in accordance with the farm plan. The ENF has a well established and experienced Supervised Agricultural Credit Department. The procedures of this department are set out in Annex IV. Review of the Department's procedures relating to production credit during intensive review did not reveal any problems. ENF has agreed to provide adequate staff to handle the increased business resulting from the project.

The program plan is based on the assumption that initial production credit arrangements will involve only financing of such inputs as fertilizer, improved seed, implements and other inputs appropriate to the use of the land in the condition in which it is purchased. As reflected in the Financial Analysis Section III D a sub-project will be feasible with only such limited support. It is not anticipated that it will be necessary to provide credits for land improvement and similar capital investments at the outset of any sub-project.

From time to time sub-projects may be developed in which additional capital improvements appear to be desirable. If the interested agencies conclude that the cooperative should be granted additional

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financing for capital improvements, such credits can be extended under this program. Similarly, after several years of operation, a farm plan can be revised to increase credits for capital improvement purposes. It is hoped that upgrading operations will often be possible under this program.

While under certain circumstances noted above and subject to the specific approval of the USAID a farm plan can call for immediate capital improvements as a part of basic financing arrangement, wherever possible capital improvements will not be financed until such time as a cooperative has demonstrated a record of financial responsibility under the program or under the operations.

The third element of the sub-project transaction will then be incorporated into the agreement of the farm plan. This carries several implications. First, the cooperative will thereby agree to operate in accordance with the farm plan. This will provide some assurance that the plan will be carried out as developed by experts. Violation of the farm plan in effect becomes a violation of the financial arrangements which will give to the ENF the right to declare an event of default. The incorporation of the farm plan will also result in an undertaking by the Ministry of Agriculture to the cooperative and to the ENF to provide agricultural technical assistance during the pendency of the financing of the project. This would provide additional protection for the ENF in that any failure by the Ministry to provide agricultural assistance as agreed upon in the plan will enable the ENF to place the financial responsibility on the Ministry of Agriculture insofar as failure to provide technical assistance as appropriate was a significant cause of the failure of any given project.

5. Operation of the Guaranty Fund and Claim Procedure

The original plan for this project as presented in the IRR proposed the disbursement of the loan into a guaranty fund held by a U.S. custodian bank from which fund claims might be paid in the event of default by a cooperative of any of its obligations under the project. While such an approach is considered feasible, it has been concluded that it would be preferable, given the scope of the project as presented in this paper,

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that a portion of the loan merely be held undisbursed for a period of three years as the guaranty fund for land sale transactions. The primary reason for shaping the proposal in this fashion is that the more complex procedure does not appear to be necessary at this time. As originally conceived, the entire loan would have been disbursed as a guaranty operation. As noted elsewhere, it is necessary at this time to utilize most of the loan for generation of local currency for production credit,

Thus, for purposes of this project \$650,000 of the proposed loan will be held undisbursed for period of 3 years except insofar as claims are made by BNF in accordance with the procedures described below. In effect, the undisbursed portion of the loan will constitute a guaranty fund and disbursements will be made from this amount as any other loan disbursement. At the end of the three year period, repayments of agricultural production credit in appropriate amounts will be substituted for the undisbursed dollar guaranty fund and the dollars then disbursed for agricultural production credit purposes.

The Banco Nacional de Fomento has indicated that it is willing to extend land purchase credit in an amount equivalent to four times the amount of the guaranty fund. In consequence, the guaranty fund will become available for claims by the Bank to the extent of 25% of land sale credit extended by BNF. Conversely, to the extent that land sale credit is not fully extended, the guaranty fund will not be available for claims. However, it is not intended that the BNF will be required to accept 75% of initial losses. To the contrary, the Bank may claim 100% of losses sustained up to the total amount in the guaranty fund which is available for claims. Thus, for example, at such time that the Bank has extended \$1,000,000 in land purchase credit, \$250,000 of the guaranty fund will be available for claims. If there is a \$200,000 loss at that point, the Bank may draw down \$200,000 from the fund. If an additional \$200,000 is lost before additional extensions of land purchase credit are made, the BNF may draw down only \$50,000 from the guaranty fund. It may not draw down the other \$50,000 until such time as \$200,000 of new land purchase credit is extended.

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The possibility of "risk-sharing" by the Bank with respect to all losses rather than the last 75% of possible losses has been explored but rejected. This is considered a point of minimal importance for the project in light of other protection. However, the land sale guaranty is considered a serious risk by the Bank. As the resources potentially to be lost would limit other important development operations and the gain involved marginal, it was decided not to press this issue in negotiations.

In the event that payments on a guaranteed land sale are not maintained by the recipient of that credit, the procedures for asserting and collecting a claim against the security fund will be as follows:

Determination of what constitutes an event of default will be based on the two objectives of identifying as soon as is reasonably possible a transaction which cannot be expected to be successful while at the same assuring that a buyer-borrower is not defaulted where there is a reasonable prospect for his being able to carry out the transactions. Where there are mitigating circumstances tending to suggest that the cooperative's failure to keep up payments is based not on its unwillingness to do so but rather upon circumstances beyond its control, moratoria will be provided.

As a practical matter payments must be scheduled on the basis of harvest of the crops to be grown by the cooperative. Unless a cooperative repudiates a debt guaranteed under the project, obligations should be considered to be due only at specific times of the year corresponding to crop harvest. Such periods will be identified in the contract.

If the buyer fails to make a payment in accordance with the obligation, a prima facie default will have taken place. The BIF in order to maintain the validity of the guaranty, must notify AID and the Ministry of Agriculture of the cooperative's failure to make the payment. A determination will then be made by the interested agencies if failure to pay was based on factors beyond the buyer's control such as severe adverse weather conditions, epidemic in the community, unusually adverse marketing conditions or other such mitigating circumstances. If the bank is willing to postpone payment or scale down payment over a period of time it will so indicate to

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USAID, which will upon assuring itself of the soundness of the proposal renew the guaranty under the new terms proposed. If the bank is unwilling to continue the obligation and AID determines that the default was made for reasons wholly beyond control of the cooperative, AID may consider processing the claim against the security fund without requiring the bank to take steps to remove the cooperative from its property or to realize on another form of security. In any event, the bank need not continue the obligation against its will. If AID determines that an event of default did not take place, but the bank refuses to accept the AID determination, the BNF may transfer the debt to the Ministry unless it appears that the non-payment was collusive in which case the guaranty may be voided.

If with respect to any land purchase debt default mitigating circumstances are not present, the Bank will be called upon to take normal steps to realize on available security. Failure to pursue other forms of security as agreed upon in the guaranty contract will constitute grounds for voiding the guaranty.

The obligation to attempt to realize upon other forms of security will involve the following. Procedures to enforce all loans and mortgages on real and personal property must be initiated within two weeks after declaration of an event of default and approval of this declaration by USAID. The Bank must attempt to remove the debtors from the land in question. However, if the debtors refuse to move voluntarily - which must be anticipated the Bank's claim will not be thereby prejudiced. If the land is vacated, the Bank must put the property up for sale and the sale price of any such sale must be approved by AID. If the debtors refuse to leave the property, the Bank's rights in the transaction will be transferred to the Ministry of Agriculture. It will then be responsible for removal of the occupants from the premises and liquidation of the property. An approved sale of the land by the Bank or a transfer of the Bank's right in the transaction to the Ministry will constitute a maturing of the Bank's claim against the security fund whereupon processing payment of the claim will proceed forthwith.

Claims against the security fund will be submitted by the Bank to the Ministry and the Mission which will make a determination as to the

claim and the consistency of the Bank's actions with the contract of guaranty. There will be a time limit on Mission review so as to assure BNF that its legitimate claims will not be unduly delayed. The Mission will forward approved claims to AID/W which will release undisbursed loan funds in amount sufficient to cover BNF payments from time to time to the seller under the land purchase contract. The failure of the cooperative to pay its obligation to BNF will not accelerate BNF's obligation to the seller or AID's loan obligation to BNF.

If the AID Mission denies the claim it will so notify the Bank and other parties affected along with a statement of the reasons why this action has been taken.

D. Financial Analysis

1. Feasibility of Sub-Projects

In developing the financial analysis to demonstrate the economic feasibility of this project, a number of problems were encountered. The fundamental difficulty, of course is that this is a pilot project. It is intended that variations on the basic scheme will be explored. Furthermore, it is the financial feasibility of the individual sub-project as reflected in the farm plan which is critical to the project and these farm plans will tend to vary considerably in terms of the nature of the land purchased, the soils and crops involved and so forth. It was decided to base the financial planning of the project on model sub-projects which in the opinion of USAID personnel and CLUSA contractors represented a reasonable, conservative picture of three typical sub-projects.

Tables 1-6, Anex VI show the costs, revenues, and net income from rice production under three different methods of rice cultivation: (1) subsistence farming under traditional methods; (2) commercial farming under semi-mechanized methods and (3) commercial farming under irrigated and mechanized methods of production. The first two methods permit the growing of only one rice crop annually, while the third method enables the producer to grow two crops a year. The paragraphs below describe the assumptions underlying the data in the tables.

At the outset it is assumed that the cooperative buyer will have 50 members and will purchase 500 hectares of land. Of this land the 300 hectares will be devoted to rice production, 140 hectares to other crops and 60 hectares to non-productive uses including houses, roads and the like. For purposes of the analysis, only rice production is taken into account. Thus in the model the entire financial burden of the sub-project will be carried by the primary cash crop despite the fact that substantial areas of the farm will be devoted to subsistence and other cash crops. This simplifying assumption is highly conservative in nature and in the view of the Mission leaves considerable room for error in the analysis of the economics of each alternative.

Turning then to the assumptions which apply within the model, the first and most important assumption has to do with land price. The model assumes the purchase of 500 hectares at 2,000 sucres per hectare or a little less than \$100. In view of the

rentals paid for rice lands, this price appears to be rather low. In fact, however, this price has been carefully checked and is considered to be a sound estimate. Apart from discussions with individuals knowledgeable in matters of land prices in the Guayas River Basin, USAID has participated, as noted elsewhere, is assisting cooperatives in three purchases of land. The transactions are as follows:

- (1) In November 1968 the "Jujan" Rice Cooperative with 44 members purchased a hacienda of 563 hectares for \$/794,530 including a \$/200,000 down payment with the balance payable in 5 years at 8% interest. This is an average of \$/1,411 sucres per hectare.
- (2) In June, 1968 the Rice Cooperative "El Roblecito" with 41 members purchased a 360 hectare hacienda from the Banco de Fomento. The sale price was \$/2,000 per cuadra or a total of \$/1,008,000 with a 10% down payment. Payment terms were five years at 6% interest.
- (3) The "Senor de los Milagros" Irrigation Cooperative, an offshoot of the Daule credit union, was formed for the purpose of purchasing 700 hectares of unused land at \$/1,300 per hectare. A down payment of 20% was made with remainder to be paid in 3 years with no interest. It is interesting to note that the seller in this case possesses substantial additional properties and has expressed willingness to sell additional lands under the proposed program.

The relationship between land rental and land sale price is in part explained by the factors stated in section II B. At the same time, it is connected that to a degree the land prices reflect an absence of effective demand; that is, an absence of people who want land and have the access to credit to purchase it. Nonetheless, for the period of this project it would seem that the amount of available land far exceeds the number of potential effective purchasers. Thus, in the opinion of the Mission, the existence of the project will not result in significant upward pressure on land prices and clearly will not affect the validity of the assumption of \$/2,000 per hectare on which the financial analysis is based.

Prices. Alternative price assumptions (low, medium, and high) are made for each of the three different methods of farming. Under traditional methods, the prices per quintal (qq.) of rice are assumed to be \$110, \$135 and \$160. Under semi-mechanized and irrigated mechanized farming, the price levels are \$110, \$130, \$155, and \$180 reflecting premium payments of approximately \$20 per qq. for the improved varieties of rice that would be grown under these methods of production. The price of \$110 per qq. is somewhat higher than the average price paid to producers in the early 1960's, but lower than the high prices prevailing since 1967, when shortages of rice for domestic consumption began to exert an upward pressure on prices. Though prices should fall as production recovers, it is unlikely that prices will fall below \$110 for producers who are part of the program proposed in this loan. In the first place, it has already been demonstrated that cooperative rice marketing can result in significantly higher prices than individual-farmer marketing. / Secondly, even if production rises significantly above present levels, a strong demand for rice from Peru is likely to continue for the foreseeable future. Though much of the Peruvian trade will probably be converted from contraband to official channels, with a corresponding decline in prices, the demand for rice by Peru seems strong enough to set a floor under domestic prices which we are estimating to be approximately \$110 per qq. Thirdly, the government has set an official price of \$160 per qq. for purchase of rice by the Piladora Modelo, which is owned by the government-affiliated Banco Regional De Fomento. At present, the Piladora Modelo does not have sufficient storage facilities or legal powers to enforce this price on a nationwide basis. While average prices exceeded the \$160 figure for much of 1968, they have now fallen below this level as the present rice crop--which seems to be a moderately good one despite draught and flood damage--is being harvested, milled, and marketed. However, BNT will purchase rice from project cooperatives at the official rate applicable. Hence, a minimum price is assured.

1/ A recent report indicates that USAID-assisted rice cooperatives are obtaining as much as \$50 per qq. more than small farmers marketing individually through middlemen. In addition, the cooperatives are turning in 10-15% less rough rice in order to be credited with a given amount of milled rice. While this very likely is an extreme case, it is a good example of the degree of exploitation suffered by small farmers and of the benefits that can be obtained from cooperative farming.

The current official price of \$160 (\$180 under modern methods of production with improved seeds) has been chosen as the upper limit for the calculation in the tables below. While it is conceivable that the GOE will attempt to enforce the official price, it is doubtful that it has the power to undertake such a step. Also, if rice production begins to increase rapidly as a result of the program anticipated under this loan as well as other public and private efforts, the official price of \$160 may become quite unrealistic and could well be lowered. Nevertheless, this figure serves as a useful purpose as an approximation of the upper limit which rice prices can be expected to reach. It should be mentioned that prices at this level are more a function of adverse weather conditions than of strong demand by Peru and that as a result when such a price is reached not all farmers would benefit from it, as adverse weather would damage or cause a total loss of many plantations.

The medium price figure of \$135 per qq. (\$155 under modern methods of production with improved seed) could be achieved either through an exceptionally strong demand for rice from Peru, or through the milling of rice by the cooperatives themselves, or through a combination of these effects. Rice milling by the cooperatives, one of the eventual goals of the program outlined in this loan paper, would increase the income of cooperative members by about \$15 per qq.

Size of the Farm and Family Labor Force. The tables below assume an average individual farm within a cooperative to comprise 10 hectares, of which 6 hectares will be devoted to rice. These are the average figures expected under the program proposed in this loan paper, based on the experience with the rice cooperatives organized under the USAID/CLUSA program.

The family labor force is assumed to comprise the head of household (one full-time-equivalent worker), his wife (0.6 full-time-equivalent worker), and one child (0.5 full-time-equivalent). This results in a total family labor force of 2.1 full-time-equivalent workers. The crop season is assumed to be six months or 120 working days. This results in a total availability of 252 days of family labor.

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Table 1 shows that labor requirements under traditional rice farming methods total 82.5 man-days per hectare per crop. For six hectares of rice land, this amounts to 495 man-days. Thus almost half the farmer's labor requirements will have to be met with hired labor at various periods of the crop cycle in accordance with the schedule on Table 1.

For semi-mechanized and irrigated-mechanized methods of production, family labor requirements are lower as production is more mechanized and family labor is increasingly devoted to managerial functions. In the case of semi-mechanized farming, hired labor costs are higher, due entirely to increased labor requirements at harvest time. Higher yields result not only in more manpower requirements at harvest time but also in higher unit labor costs as the greater density of the plants makes harvesting somewhat more difficult. Total labor requirements under semi-mechanized farming are slightly less than those under traditional methods of farming.

In the case of the irrigated and mechanized farming, total labor requirements are significantly lower than is the case under the other two methods, and hired labor costs are minimal.

Labor Costs and Net Family Income. For most types of labor, the prevailing daily wage in the rice areas of the Guayas River Basin is \$20. For some operations it is higher (e.g. application of herbicides) while for others it is lower (e.g. harvesting).

Tables 2, 4, and 6 include imputed costs of family labor at the prevailing wage rates for the various farming operations. In determining net income from rice farming, Tables 2, 4, and 6 present two alternative methods of calculation. The first includes under costs the imputed costs of family labor, while the second method excludes these costs. In view of the lack of alternative employment opportunities for small rice farmers in the Guayas River Basin, it is highly questionable to attempt to separate labor income from profits, and thus the second method of calculation seems to be more appropriate for determining the net income of these farmers.

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Using the first method of calculation, rice farming is seen to yield negative returns under traditional farming methods and using the low and medium price assumptions. In all other instances, the returns are positive. The second method of calculation shows rice farming to yield positive returns in all instances, with those returns increasing dramatically as the farmer shifts from subsistence to semi-mechanized production and then from semi-mechanized to fully mechanized and irrigation production.

Although the positive cash return under traditional methods of production appear to be too small to justify a continuation of rice farming by lower income groups, particularly at the lower end of the price scale, it must be remembered that these farmers also grow other crops for subsistence and in the off-season seek gainful employment to increase their cash income. Even in instances where rice farming yields negative returns the farmer prefers a situation where he has a place to live and grow other crops for his family to the status of a landless worker.

Yields. The average yield under traditional methods of production is approximately 20qq. per hectare for the farmers who would be organized into cooperatives under the program proposed in this loan paper. Under semi-mechanized methods of production with improved seed varieties, productivity can be expected to increase to 40qq. per hectare. Fully mechanized irrigated rice farming with improved seed varieties would raise yields to 70 qq. per hectare. In Tables 2,4, and 6 it is seen that such dramatic increases in yields make it economically feasible--despite higher costs--to progressively improved methods of production.

Interest Rates. Interest rates assumed in the analysis are 8% for both long and short term credit. 8% is the legal maximum interest rate for this type of credit allowed under ICF by law. Total financial charges are not allowed to exceed this percentage.

Conclusions. While the feasibility of each sub-project must be determined in light of the conditions applicable in the particular case, it appears that a wide range of feasible sub-project conditions exist.

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2. Project Costs and Sources of Funding

a. Inputs

Land Sale Credit (extended by sellers)	\$2,500,000 ^{1/}
Annual Credit Requirements (loan funded)	\$2,750,000 ^{2/}
Technical Assistance to Cooperatives	
GOE Costs (3 years)	\$ 400,000
Revolving Fund Local Cost Support (loan fund)	\$ 100,000
U.S. Commodity Support (loan fund)	\$ 100,000
Technical Assistance to Cooperative Bank (USAID funded)	\$ 150,000
	<u>\$6,000,000</u>

b. Sources

U.S. Government Resources	
AID loan	\$3,600,000 ^{3/}
USAID grant funds	150,000
Ecuadorean Resources	
Credit Extensions of Local Sellers	\$2,500,000 ^{3/}
GOE	400,000
	<u>\$6,650,000^{3/}</u>

1/Land Sale Guarantee Fund

500	(avg. no. of ha. per coop.)
50	(no. of coops.)
<u>25,000</u>	(no. of ha. to be guaranteed)
2,000	(price per ha, in sucres)
<u>50,000,000</u>	(total cost of land in sucres)
5,000,000	(down payment-10% of total cost)
<u>45,000,000</u>	(sum of annual installments, excluding interest)
25	(Payment of annual installments to be kept in guaranty fund)
<u>11,250,000</u>	(amount to be kept in guarantee fund)

S/11,250,000 ÷ 18.18 = \$618,812 or say \$650,000 (dollar equivalent or guaranty fund)

2/ Annual Credit Requirements (assuming semi-mechanized farming on all 25,000 hectares)

25,000	(total number of hectares)
<u>.60</u>	(percentage of total land area for which credit will be necessary)
15,000	(total number of hectares requiring credit)
<u>3,260</u>	(amt. of credit per hectare in sucres-from Annex VI Table 3)
48,900,000	(total credit needs)

$S/48,900,000 \div 18.18 = \$2,689,769$ or may \$2,750,000 (dollar equivalent of annual credit requirements)

3/ As \$650,000 of the loan is held as a reserve against loss on land sale credit extensions of \$2,500,000, the total of sources exceeds inputs by \$650,000.

3. Prospects of Loan Repayment

The capacity of the project to be self-financing is discussed above. In the event that the project fails, it still appears that the GOE can repay the debt.

Ecuador's ratio of foreign debt service to total exports in 1968 was approximately 10.4%. However, debt service payments are expected to rise from US\$21.9 million in 1968 to US\$53.1 million by 1973^{1/} as grace periods on foreign loans contracted during the 1960's begin to run out, while export proceeds are not expected to increase by more than 3.5%-3% annually. This will put the debt service/export ratio at about 20-21% in 1973. Thereafter, the rate of increase in debt service payments is expected to come down, while at the same time the rate of increase of commodity export earnings should increase. This project debt-service/export ratio is quite high but it is not out of proportion with other LA countries. It is expected to decrease sharply thereafter as reflected in the Economic Analysis. Ecuador has always had a good record on meeting its loan payments and no special problem with the dollar repayment of the proposed loan is anticipated. On the basis of the foregoing, the Loan Committee has concluded that Ecuador has the capacity to meet the repayment obligations of this loan.

1/ Financing Board's Estimates.

4. Justification of Local Currency Financing

This is a highly experimental development operation undertaken by the GOE at a time when it is faced with serious budgetary problems. For the past several years, the GOE has had such difficulties as revenues have been insufficient to cover rising expenditure demands. Even with austerity policies on budgeted expenditures, sizeable budget deficits have been incurred. The 1968 cash deficit is estimated at S/560 million or about 18.5% of total expenditures. The technical and political difficulties of correcting this situation are such that several years will be required to effect a significant improvement in public finances through improved tax administration. The present government, in office only eight months, has not had time to make significant progress in this field. In addition to these difficulties, Ecuador is now in the midst of a balance-of-payments crisis and has just received a \$18 million standby from the DF. The standby requires Ecuador to limit the size of its budget deficit. Other sources of local currency are not available. In consequence, the project is impossible to undertake without dollar financing of local currency costs.

5. Justification of Concessionary Terms

This proposal calls for granting the loan to the GOE on the most concessionary terms available, 3% for 40 years with a 10 year grace period during which interest will be 2%. The nature of the financial problems facing the Ecuadorean Government has been referred to previously. The Government is presently facing a serious budgetary crisis and it is anticipated that critical needs for government expenditures will continue to absorb financial resources available to the government well into the future. While substantial improvements in certain elements of the GOE financial picture are anticipated during the next decade, the requirements for financing will probably continue to outrun available resources through the end of the century. All previous AID financing in Ecuador in recent years had been on the most concessionary terms available and other international lending institutions pursue a similar policy. Further, this loan has a substantial social development orientation with only minimal economic benefit to the GOE.

On the basis of the foregoing, the Loan Committee has concluded that this loan should be made on the most concessionary terms possible.

E. Economic Analysis

Agriculture is by far the most important sector of the Ecuadorean economy, accounting for approximately 35 percent of the GDP (1963-67 average) and about 56 percent of total employment (1962 census). Furthermore, it accounts for close to 95 percent of Ecuador's total export earnings, with bananas, cacao, and coffee together accounting for about 35 percent. These figures make it clear that the general health of the economy is very much dependent on the strength of its agricultural sector.

From 1960 to 1967, total GDP grew at an average annual rate of 4.5 percent (all growth rate figures are in real terms); but given an annual rate of population growth estimated at 3.4 percent, GDP per capita increased at only 1.0 percent a year, well below the Alliance for Progress target of 2.5 percent. A major reason for this mediocre record has been the poor performance of the agricultural sector, which grew at an average rate of only 3.1 percent over the same period. A good indication of the importance of this sector is the fact that a five percent sector growth rate during the period 1960-67. (assuming no change in the growth rates of the other sectors) would have resulted in a 5.2 percent increase in total GDP and a 1.8 percent increase in GDP per capita. Preliminary ECLA estimates for 1968 indicate an aggregate GDP increase of 4.3 percent, with the increase for the agricultural sector being only 1.5 percent, largely due to drought conditions in the first half of the year.

The slow growth of the agricultural sector has also had adverse effects on the balance of payments, though these effects have not been too serious as yet. Food imports are still relatively small, with wheat and fats and oils being the only major imports. Some efforts have already been taken to increase domestic production of these items. For example, INIAP has successfully developed new wheat varieties, through dissemination of the new seeds to farmers has been slow. With regard to oils and fats, the BNF received a loan from IDB in 1961 for the development of African oil palm, and plantings under this loan have recently come into production. However, in the face of rapidly growing food demand, additional efforts will have to be made to reduce imports of these items.

Recent export performance has been satisfactory, with the 1963-68 rate of growth averaging 6.8 percent annually, following a period of stagnation from 1959 to 1963. However, the export outlook for

the next few years is rather bleak, with bananas in serious competitive difficulties, coffee exports limited by the International Coffee Agreement, and cacao prices likely to fall soon from their relatively high levels in the last few years. For 1968, the Central Bank estimates that total exports rose by only 4.5 percent, and this only because of heavy Japanese purchase of bananas due to crop damage in Taiwan, a special factor that cannot be counted on to the same degree for 1969. Banana exports are likely to fall in 1969 by 10 percent and total exports by 5 percent. Thus even with the recently signed IMF standby of \$18 million, the balance-of-payments difficulties that appeared in late 1968 largely as a result of rapidly rising imports (16.7 percent in 1968 and 18.4 percent in 1968) are likely to persist, and additional measures to restrict imports will probably have to be taken.

Under these circumstances, export diversification is imperative. While Ecuador has many good possibilities for developing major new export items, not all of these commodities will be able to make a significant contribution to remedying balance-of-payments difficulties within the next four to five years. This is true, for example, of livestock, lumber and lumber products, fish and seafood, petroleum, and possibly vegetable oils. Rice, in contrast, could become a major export item within two to three years.

This has been recognized by the Government of Ecuador, which also seems to be realizing the need for greater government support to agriculture generally. Specifically with regard to rice, the GOE's interest in increasing rice production has been demonstrated by (a) creation of the Comision Nacional de Arroz (CNA) in 1967 as a semi-autonomous agency under the Ministry of Agriculture; (b) the construction of a rice experiment station in the Boliche area by the Instituto Nacional de Investigaciones Agropecuarias (INIAP), with the assistance of Rockefeller Foundation rice experts from Colombia; and (c) increased lending for rice production by the Banco Nacional de Fomento (BNF), directed at small farmers and cooperatives as well as to medium and large farmers. The BNF has also shown an interest in contributing to technical assistance efforts to raise the productivity of rice cultivation.

USAID/Ecuador's recent document, "Suggestions for a Comprehensive Rice Development Program for Ecuador", shows that the adoption of modern rice production technology on 20,000 hectares could result

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in Ecuador's exporting as much as \$10.5 million of rice in 1971, compared with no exports in 1967 and 1968. If adoption of the new technology is more widespread--as seems very likely in view of the recent activities not only of the GOE but also of the private sector--exports could be even higher.

As the USAID document points out, much of the increase rice production could come from small rice farmers, the great majority of whom do not presently own their land, but who account for an estimated 65-75 percent of Ecuador's total rice production. A program aimed in large part at these farmers could be an important vehicle not only for improving income distribution but also for achieving some of the non-economic objectives of Title IX.

The USAID has already become involved with these small farmers through the formation of rice cooperatives, a project being carried out under a contract with the Cooperative League of the U.S.A. (CLUSA). This project, initiated in early 1968, has thus far looked very promising. Especially encouraging has been the fact that several cooperatives have been able to purchase their land. Another has purchased its own rice mill, while several have received loans for irrigation pumps. Sources of credit have included the BNF, the Banco de Cooperativas del Ecuador, and private banks.

However, sufficient credit is not presently available to meet the objectives of a large-scale program such as that described in the USAID's "Suggestions for a Comprehensive Rice Development Program for Ecuador." The loan package proposed in this document thus contributes to achieving the larger objectives of such a program.

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F. Some Peripheral Problems: IERAC, Land Invasions and the Rice Policy of the Government of Ecuador

1. IERAC - The Agrarian Reform Agency of the Government

The role of IERAC in the proposed project has been a particularly vexing problem to deal with. It is clear that the legal responsibility for agrarian reform in Ecuador falls on that organization. It is equally clear for reasons discussed in Annex VII that involving IERAC in the program at this point would be tantamount to failure because of the organization's lack of financing, public support and competent staff. The Mission was saved a very complicated negotiating problem by a decision on the part of the Minister of Agriculture that the program should be carried out by the BNF rather than by IERAC. Indeed, the Minister reflected a sympathetic understanding of AID's disinclination to become involved in the political complications in the problem. Hence, there will be no problem of IERAC involvement being forced on this project. Of course, by law certain types of transactions, such as land tenancy arrangements and the like, must be submitted for IERAC approval. It is not anticipated that compliance with these statutes will be the cause of any complications.

On the other hand, it is the Mission's view that at such time as IERAC proves itself capable of undertaking its full responsibility with respect to agrarian reform that the Mission should make every effort to cooperate with it. It is not inconceivable that IERAC will improve substantially in its performance. Indeed, it could hardly do otherwise. Thus one possible variation on the project theme would be attempting to work with a IERAC cooperative. The Mission will maintain a positive, sympathetic attitude toward the Government land reform agency, but will not at this point involve IERAC more than is required by law as an organization. As noted elsewhere, IERAC personnel under BNF direction will be involved in technical assistance operations. This may be a first step in the direction that the Mission hopes to move.

2. The Land Invasion Problem

Like many other nations in Latin America, Ecuador has experienced a number of land invasions.

But of course, land invasions are not in themselves the problem. They are symptomatic of the general level of social

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tensions existing in the areas where they take place. It must be recognized that there are socially legitimate as well as socially illegitimate claims for land which are expressed through land invasion.

It is not the intention of this project to deal with the problem of land invasions as such. Apart from the invasions being merely symptomatic, the phenomenon is far too complex, far too sensitive to be dealt with through the medium of foreign aid. However, the project will operate in a society within which invasions have become not uncommon events. To the extent that invasions are a part of the Ecuadorean social ambiente, there are relationships to the project some aspects of which should be noted.

As far as the impact of the phenomenon on the project is concerned, on the negative side the existence of land invasion as an "alternative" to purchase poses a threat to the stability of sub-project financial transaction. If a cooperative sees land being taken without payment it may be inclined not to pay its debts. Conversely, campesinos are aware that default would cut off access to legitimate sources of production credit. But the threat exists. On the positive side, the atmosphere of invasion threat doubtless will be a useful additional inducement for land-owners to sell at reasonable prices.

Concerning the impact of the project on the land invasion phenomenon, very little can be expected unless the project proves to be successful and is substantially expanded in the future. If this happens, a great deal can be expected. By making it possible for those with a legitimate claim to land to obtain it on reasonable terms, the aura of legitimate social protest with which some invaders clothe their otherwise purely criminal activity would be stripped away. The hand of the Government would be strengthened in dealing with such elements if those with legitimate claims to land were in a position to obtain it in a manner consistent with law. Finally, the extremist agitators who have provoked some of the land invasions in recent months would presumably find their task more difficult, thus perhaps lowering the propensity to invade throughout the spectrum of those concerned.

While this project may, if successful, have a positive effect on the land invasion situation, the project itself does not look on improvement in the invasion problem as an objective nor does it contemplate taking into account for operational purposes the level of land invasion threats (although presumably many potential land sellers will do this without prompting from project officials). The project impacts on the phenomenon and the phenomenon impacts on the project but the medium is not the message.

Whatever may be the implications of the land invasion problem, the project is designed to benefit those who can and will carry out viable economic enterprise on the land acquired. Guarantees will be made selectively on the basis of such standards as the skill to form effectively, the capacity to organize and carry through in economic activities, the soundness in terms of cooperative principles of the organization and the like. This project is not intended to assist the desperate. To that extent, it will not deal with many people interested in land invasion and will not have an effect on many types of land invasion problems. It will, however, tend to relieve some of the pressures of those with the most legitimate claims for land reform which in the view of the Mission is the furthest that this type of activity can be carried by foreign aid.

3. Government Rice Policy

As is reflected in Section III D, the financial feasibility of the project is related to the price of rice obtained by the beneficiary cooperative. To the extent that beneficiary cooperatives must depend on open market prices, a risk exists but as explained in Section III D, these cooperatives will be able to sell rice at prices fixed by the GOE. Nonetheless, the overall rice policy of the GOE is significant as any significant expansion of this program in the future will probably require an overall rationalization of the rice economics of Ecuador.

The Government of Ecuador intervenes in the rice market in several ways. A short discussion of these interventions is provided to indicate their extent and ineffectiveness. It is not considered desirable or feasible to attempt to intervene with the Government with respect to its rice policies in the context of this pilot project. However, the Mission

is mindful of long-term requirements for rice economy rationalization, not only in terms of the possibilities for expansion of this project but also as an overall economic development requirement of the country.

Producer prices and wholesale prices for rice are presently established jointly by the Ministry of Industry and Commerce and the Ministry of Agriculture. The latest determination of price is set forth in Decree No. 584-A, dated April 14, 1969. Producer prices range between S/140 and S/160 per quintal, while wholesale prices range from S/155 to S/185 per quintal. The Banco de Fomento's Piladora Modelo in Guayaquil stands ready to purchase rice from producers at the prices set by the government decree. However, the Piladora Modelo's handling, drying, and storage facilities are insufficient to enforce the official prices through market pressures, and the government has not other effective means to control the prices paid by the other mills, which operate on a supply-demand basis. For much of 1968 and in early 1969, prices paid by private rice mills to producers exceeded the official prices (which had been lower than they are now), and as a result very little rice was brought to the Piladora Modelo. At present, the situation is reversed -- the winter crop now being harvested is a reasonably good one despite some drought and flood damage, and private mills are paying less than the official prices. They can continue to do this because the Piladora Modelo is unable to handle sufficient quantities of rice to influence market prices.

Retail prices are set by municipalities, which have the authority to establish maximum prices for basic food items. Again, though prices tend to be determined by supply and demand, as the municipalities have no power to prevent retailers from selling at prices above the legal maximum.

Exports of rice are not permitted unless the GOE determines that there is a surplus of rice over and above the amounts needed to satisfy domestic consumption needs and to maintain a normal level of stocks. Under present arrangements, the Superintendency of Rice Mills and the National Rice Commission conduct survey of rice mills and make periodic reports on entries, withdrawals, and stocks to the Directorate of Internal

Trade of the Ministry of Industry and Commerce. The Directorate review these reports and sends them along with its comments to the Minister of Industry and Commerce, who makes the final decision whether or not to authorize the exportation of rice.

Data on entries, withdrawals, and stocks are subject to considerable error. Legislation passed on July 1, 1967, required only large rice mills with polishing operations (piladoras) to register entries, withdrawals, and stocks with the Superintendency of Rice Mills. Small rice mills that were considered "incomplete" because they lacked polishing facilities (molinos) were exempted from these requirements. As of July 31, 1967, 95 mills were classified as piladoras and 546 as molinos.^{1/} The latter probably account for as much milling as the former. Some molinos, incidently, are now using Japanese equipment which both husks and polishes rice in the same operation.

The incomplete accounting of rice entries, withdrawals, and stocks makes the decision on whether or not to export largely a matter of guesswork. Although market price movement can help in the guessing game, it must also be recognized that price increases may be partially a reflection of withholding of stocks from the market for speculative purposes instead of being entirely a reflection of scarcity.

As in the case of price controls, export controls are also ineffective. In the last few years, substantial quantities of rice have been illegally exported to Peru, where severe shortages of rice have resulted in high prices.

It is highly unlikely that the GOE will be in a position to enforce price and export regulations in the foreseeable future unless it increases its capacity for regulating supply. This would require investments in handling, drying, and storage facilities by the Piladora Modelo and perhaps the construction (or purchase) of additional milling facilities.

In any event, the project is protected by assurance of the right to sell at the fixed minimum price to the Piladora Modelo. While the fixed price will almost certainly fall from its present levels, it is considered unlikely that it could fall below the S/110 minimum price assumption of the financial analysis.

^{1/} Office of the Agricultural Attache, Quito, Report No. AGR-26, February 8, 1969.

SECTION IV - LOAN ADMINISTRATION

A. Project Execution

1. Introduction

The proposed loan will finance a pilot project in agrarian reform. It is intended to approach this project with flexibility with a view to defining procedures suitable for financing a broader program in the future. In consequence, the presentation of administrative plans in this paper should be considered an initial plan subject to revision when and if events suggest the desirability of making revisions.

2. Execution Plan

While it is intended that ultimately guaranty proposals will be developed, approved and executed on a case basis as each case is ready for processing, initial guarantees under this loan will be made in two groups of four or five cases during the first year. This will be done to conserve administrative effort required for working out various details of program operations and also to assure a sufficient variety of cases to provide administrators with an adequate insight into operating variables. On the basis of this experience, it is believed that permanent procedures can be defined with maximum effectiveness.

The first group of five guarantees will be made to cooperatives already in existence with an established business record so as to minimize initially the problem of buyer selection. Buyer selection is an aspect of the program which, it is believed, can be dealt with more or less separately from other administrative problems and should not be defined until more is known about the financial

ambiente of the program.

It is anticipated that if the loan is authorized by June 30, 1969, the loan will be signed by September 30, 1969. As the BNF Supervised Agricultural Credit Department is an established organization, there will be no immediate organizational problems within the Bank. The GOE will assign technical personnel to the BNF as required for field operations. The head of the Supervised Agricultural Credit Department will be appointed Project Coordinator and in that capacity will supervise not only BNF employees working on the project but also GOE employees assigned thereto. He will also be in charge of the revolving fund for local costs of technical assistance and all commodities purchased under the loan for support of the project.

While the foregoing operations are being established the AID Mission staff which works with the cooperative movement in Ecuador will select five cooperatives which in the judgement of the Mission staff are best available candidates for this program. Selection will be on the basis of determining those coops which are functioning most effectively in terms of business capacity, agricultural skills, and the ability to work as a cooperative. The following are the cooperatives which have been identified at this point as the most likely candidates for this activity: La Camela, Las Mercedes, El Roblecito, Yaguachi and Jujan.

USAID/CIUSA personnel will advise the cooperative in the process of identifying lands to be purchased, the negotiation of the

purchase and the negotiation of production credit. However, every effort will be made not to interfere with the operation of the transactions. The role of USAID will be limited primarily to learning as much as possible about the nature of this type of transaction so as to provide guidance for similar operations in the future when perhaps less well developed cooperatives will be the purchasers.

Particular emphasis will be placed on the problem of evaluation of properties to be guaranteed. In this connection, arrangements will be made to obtain land use and soil classification survey data with respect to each purchase. On basis of this data policies will be established with respect to the question of the maximum prices of properties which will be guaranteed under this project.

The first group of five guaranties will be executed more or less simultaneously. It is anticipated that these transactions will be completed by March 31, 1970.

While the initial effort referred to above is taking place, the selection of five cooperatives for the second group of guaranties will be effectuated. Those cooperatives to be guaranteed in the second groups will by definition be less attractive in terms of criteria stated said above. This being the case, a greater effort will probably be required on the part of USAID/CNUSA employees and appropriate staffing steps will be taken to assure that an adequate amount of support will be available for this effort. It is hoped that the second group of guarantees can be made by September 30, 1970.

In November of 1970 a general review of activities under the loan will take place and final operating procedures will be developed. After this point it is hoped that a regular procedure for guaranteeing cooperatives on a case by case basis will be possible. Representatives of AID/W will be asked to participate in the project review at that time.

3. Primary Responsibility for Action

Primary responsibility for action under this loan will lie with the head of the Supervised Agricultural Credit Department of the ENF. AID's involvement with the office will be rather deep at the outset. It is anticipated that AID's involvement will tend to be reduced over time until AID no longer will have a role in administration other than to approve guarantees and claims. It is anticipated that two years will be required for AID to remove itself entirely from the administrative element of this program.

USAID involvement with the cooperatives themselves will remain very close throughout the period of the execution of the project. At the present time AID has an extensive involvement in the cooperative movement in Ecuador and because of this loan the present close relationship will probably be deepened. In any event, in the process of the formation of cooperatives, the rendering of technical assistance and other matters relating to cooperative operation, the involvement of USAID will be not less at any point during the project that it is at the present time.

Responsibilities for these relations will be vested in USAID division chiefs but in all likelihood the actual contact work

will be carried out primarily by USAID/CLUSA local hire employees in order to maximize the degree of Ecuadoreans participating in the program. It is hoped that at some point in the future AID will be able to step out of the program entirely, but this will depend on how effective the Ecuadorean employees prove themselves to be in the operation of the program.

4. USAID Monitoring Responsibilities

At the outset USAID monitoring responsibilities will extend to all aspects of the establishment of the program. The Rural Development Division, the Institutional Development Division and Capital Development and Engineering Office will be the elements primarily responsible for surveillance activities. In each case it is anticipated that the persons directly involved will be Ecuadorean employees reporting to American division chiefs. The Institutional Development Division by means of a contract with CLUSA is fully staffed to handle any requirements involved in this program at the present time. Capital Development and Engineering Office will be expanded to carry out its responsibilities with respect to this and other programs. As this loan project is an integral part of the overall AID effort in cooperative development and rural development activities, it is not anticipated that staffing will cause a serious problem in the execution of this loan. Generally speaking, personnel are available though involved in related activities at the present time. It is the intention of the Mission to shift emphasis of various other activities to the extent necessary to develop this program. Additional funding and contract personnel will be provided as needed.

5. Technical Assistance

Most of the technical assistance requirements associated with this project are available at the present time and involvement of technical personnel in the program will require essentially a shift from present activities to activities under this loan or relating to this loan. This includes personnel working in cooperative formation and operation, agricultural technical assistance advisors, and the like. The ENF is in a position to render technical assistance in certain matters relating to financial aspects of the program. The loan provides some funding for commodity support of technical assistance operation by the Ministry. To the extent that professional services are to be procured for this activity, they will be handled primarily by Mission operating funds and grant funded contracts as appropriate. To the extent necessary, the loan technical assistance element will provide an additional source for contracting for technical assistance.

B. Implementation Procedures

1. Target Dates

It is anticipated that the loan will be signed by September 30, 1969. Initial conditions precedent should be complied with by December 31, 1969. All conditions precedent will be fulfilled before initial guaranties are issued. The disbursement of the loan will take place as soon as possible after the signing of the loan and the meeting of the initial conditions precedent.

There will be about \$100,000 of procurement of commodities of U.S. source and origin under the loan for which letters of commitment will be opened.

2. Disbursement Procedures

\$2,750,000 will be disbursed as required under SLC procedures for production credit uses. \$650,000 will be retained undisbursed unless and until claims for default losses are made in which case disbursements will be made under SLC procedures.

SECTION V - ISSUES

A. Alternative Approaches to the Problem of Financing Land Purchases

In the AID/W comments on the IRR for this project, the Mission was urged to consider alternative procedures to the guaranty mechanism to accomplish the basic objectives of the program. In accordance with these comments, the Mission reanalyzed this question fully during intensive review but again arrived at the conclusion that the guaranty fund mechanism was the only practicable approach which appeared to be available in light of the economic conditions prevailing within Ecuador and the anticipated levels of US assistance which might be available for this program.

The fundamental problem with any direct financing scheme would, of course, be the absence of sufficient resources to make a significant contribution to the overall problem faced. Furthermore, balance of payments imperatives suggest that to the extent feasible local currency conversions could be limited. Direct financing would, of course, involve 100% conversion under SIC procedures.

The leverage possibilities inherent in the establishing of a mortgage bank or the support of existing mortgage banking operations within the country was recognized as an attractive theoretical alternative. Unfortunately, however, the problem here would be the same as the problem encountered with respect to production credit financing. In short, there are no resources available within the Ecuadorean economy for the specific purpose of the program. The nature of this problem in the context of production credit financing is discussed under issue B below. In the context of the mortgage bank financing, it is apparent that the Government is not in a position to make significant sucere resources available for this purpose and the private sector is unwilling, at least at this stage, to enter into this type of operation. The only institution which appears to be willing to undertake the program at this stage is the ECB.

It was thus concluded that the only source of financing for land transactions which is practicable at the present time is the owner of the land to be sold. Financing by the owner has a money creating effect in a circumstance where the basic problem is the non-availability of money. Furthermore, this approach

retains the leverage benefits that a mortgage banking operation would create were local financing resources available for a more orthodox arrangement.

It should be noted that the possibility of obtaining financing from the GOE is completely out of the question in light of the budgetary crisis which it is now facing and can be expected to face for a number of years to come. Issuance of bonds for this purpose would of course be difficult not only because of the substantial discount at which GOE bonds are now selling but also because of the restrictive IMF Standby Agreement to which the GOE is a party.

B. Direct AID Financing Through SLC Procedures of Production Credit for the Project

As presented in the IRR, this program contemplated guarantees not only of land purchase obligations but also production credit as well. Thus it was hoped that the loan would be disbursed entirely into a guaranty fund and that actual local currency financing could be handled within and by resources of the Ecuadorean economy. Initial discussions with bankers indicated that this arrangement would be difficult although not impossible. BNF indicated interest in the program, but also pointed out that its total resources were limited. In consequence, if it were to finance the operation directly, it would be at the cost of reducing availabilities of credit to customers of the same social and economic classes which this program seeks to benefit. Private domestic banks indicated an interest in the program but took an understandably conservative position with respect to participation at the outset of the program. The association of private banks is studying the matter and may in light of experience under the program agree to provide resources at some time in the future. However, at the present time, there appears to be no likelihood of obtaining support from this source. Private foreign banks, including two U.S. banks operating in Ecuador, indicated strong interest in the program. However, recently the GOE passed a law requiring substantial amounts of foreign bank assets to be invested in housing bonds to be issued by the Government. This unfortunate legislation has placed severe strains on bank assets and operations quite apart from any possibility of participation in this program. In consequence, the foreign banks indicated that it would not be possible for them to consider active participation in this program at the present time.

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In light of these developments, it became apparent that there was no adequate source of local currency for production credit purposes available within Ecuador to be guaranteed. This left the Mission no choice but to revise its proposal as reflected in this paper to call for the generation of local currencies for production credit purposes through SIC procedures. The program is not considered to be feasible unless such sources of local currency are made available.

C. Possible Negotiation Difficulties

The proposed project represents a new departure in financing agrarian development. After extensive discussions with BNF, reservations have been expressed by individuals within BNF concerning certain elements of the operation, specifically the land guaranty procedure. Because of the novelty of the operation, it is clear that negotiation of various aspects of the project will be complex and indeed may require changes from the project as presented herein. The Mission believes that the loan can be negotiated in the form presented or that alternative arrangements consistent with the objectives of the project can be secured. In any event, the authorization will provide that if the loan cannot be signed within six months after the date of authorization, the authorization will be terminated.

DRAFT
C E R T I F I C A T E

I hereby certify to the Administrator of the Agency for International Development that Ecuador possesses both the financial and human resources effectively to maintain and utilize the pilot project to be undertaken pursuant to the terms of the A.I.D. loan proposed in this paper for Agricultural Land Sale and Development between the Government of Ecuador and the United States of America. In so certifying I have taken into account the maintenance and utilization of projects in Ecuador previously financed or assisted by the United States.

Date

Robert J. Minges
Director
A.I.D. Mission to Ecuador

(Signed original on file in official IA/DR Loan Folder)

EQUADOR

AID 1240-2 (1-69)

LOAN FOR PILOT PROJECT FOR AGRICULTURAL
LAND SALE AND DEVELOPMENTCHECKLIST OF STATUTORY CRITERIA

(Alliance for Progress)

In the right-hand margin, for each item write answer, or, as appropriate, a summary of required discussion. As necessary, reference the section(s) of the Capital Assistance Paper, or other clearly identified and available document, in which the matter is further discussed. This form may be used a part of the Capital Assistance Paper.

The following abbreviations are used:

FAA - Foreign Assistance Act of 1961, as amended by the Foreign Assistance Act of 1969.

App. - Foreign Assistance and Related Agencies Appropriations Act, 1969.

COUNTRY PERFORMANCEProgress Towards Country Goals1. FAA 5.203; 5.251(b).

A. Describe extent to which country is:

(1) *Making appropriate efforts to increase food production and improve means for food storage and distribution.*

Ecuador has placed high priority on agricultural activities, although its efforts have been hindered by serious fiscal problems.

(2) *Creating a favorable climate for foreign and domestic private enterprise and investment.*

Legislation favorable for private enterprise and investment is in force, and the private sector is healthy and active in Ecuador.

AID 1240-2 (1-69)

(3) Increasing the public's role in the developmental process.

Ecuador has a constitutional government which is responsive within the limits of budgetary restraints to active public interest sectors in various types of developmental activity.

(4) (a) Allocating available budgetary resources to development.

Despite severe budgetary restraints, and inefficiencies in the establishment of priorities in public sector expenditures, the public sector as a whole is allocating significant budgetary resources to development.

(b) Diverting such resources for unnecessary military expenditures (See also Item No. 19.) and intervention in affairs of other free and independent nations. (See also Item No. 17.)

The GOE is not diverting budgetary resources for unnecessary military expenditures.

(5) Willing to contribute funds to the project or program.

Willingness to contribute funds to the project consistent with budgetary restraints has been expressed.

AID 1240-2 (1-69)

(6) *Making economic, social, and political reforms such as tax collection improvements and changes in land tenure arrangements, and making progress toward respect for the rule of law, freedom of expression and of the press, and recognizing the importance of individual freedom, initiative, and private enterprise.*

As a constitutional democracy, the rule of law, freedom of expression and of the press, individual initiative and private enterprise exist in Ecuador. Economic, social and political reform are objectives of the government although progress has been slight.

(7) *Adhering to the principles of the Act of Bogota and Charter of Punta del Este.*

Ecuador adheres to the principle of the Act of Bogotá and Charter of Punta del Este.

(8) *Attempting to repatriate capital invested in other countries by its own citizens.*

Ecuador attempts to repatriate capital primarily by trying to promote a sound climate for investment in the country and maintaining the stability of the sucre.

(9) *Otherwise responding to the vital economic, political, and social concerns of its people, and demonstrating a clear determination to take effective self-help measures.*

The GOE appears to have good intentions, but its performance has been limited.

B. *Are above factors taken into account in the furnishing of the subject assistance?*

The support of the GOE of the proposed loan indicates the GOE's affirmative position with respect to these factors which were taken into account in the consideration of the proposed loan.

AID 1240-2 (1-69)

Treatment of U.S. Citizens

2. FAA U. 620(c). If assistance is to government, is the government liable as debtor or unconditional guarantor on any debt to a U.S. citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) debt is not denied or contested by such government?

3. FAA U. 620(c)(1). If assistance is to a government, has it (including government agencies or subdivisions) taken any action which has the effect of nationalizing, expropriating, or otherwise seizing-ownership or control of property of U.S. citizens or entities beneficially owned by them without taking steps to discharge its obligations toward such citizens or entities?

4. App. U. 106. If country attempts to create distinctions because of their race or religion among Americans in granting personal or commercial access or other rights otherwise available to U.S. citizens generally, what steps (will be) (have been) taken during loan negotiations to influence elimination of such distinctions?

The USAID and the Embassy are investigating a potential 620 (c) situation involving two contracts. If 620 (c) is determined to be applicable, the loan agreement will not be signed until the GOE satisfied the requirement of 620 (c).

It has not been determined that the GOE has taken any steps which require the application of the sanctions prescribed by this Section.

Ecuador does not take such action.

AID 1240-2 (1-69)

5. FAA §. 620(o); Fishermen's Protective Act. (U.S.). If country has seized, or imposed any penalty or sanction against, any U.S. fishing vessel on account of its fishing activities in international waters,

a. has any deduction required by Fishermen's Protective Act been made?

b. has complete denial of assistance been considered by A.I.D. Administrator?

Since January 1, 1968, arrest incidents have been reported as follows: March 20, 1968, 1 boat; August 7, 1968, 4 boats; December 10, 1968, 1 boat. Protests have been lodged with the GOE.

With respect to the boat arrested and fined after August 12, 1968, (the effective date of Section 5 of the FPA, as amended) no amount has yet been expended by the United States and thus no deduction is required at this time by this Section.

The loan will not be authorized unless the A.I.D. Administrator considers denying assistance to the GOE and determines nevertheless to permit the authorization.

Relations with U.S. Government and Other Nations

6. FAA §. 620(d). If assistance is for any productive enterprise which will compete in the U.S. with U.S. enterprise, is there an agreement by the recipient country to prevent export to the U.S. of more than 20% of the enterprise's annual production during the life of the loan?

It is not contemplated that the proposed assistance will result in competition in the U.S. with U.S. enterprise.

7. FAA §. 620(j). Has the country permitted, or failed to take adequate measures to prevent, the damage or destruction by mob action, of U.S. property?

No.

AID 1240-2 (1-69)

8. FAA §.620(l). If the country has failed to institute the investment guaranty program for the specific risks of expropriation, in convertibility or confiscation, has the A.I.D. administration within the past year considered denying assistance to such government for this reason? Ecuador has instituted such a program
9. FAA §.620(a). Is the government of the recipient country in default on interest or principal of any A.I.D. loan to the country? No.
10. FAA §.620(v). Has the country covered diplomatic relations with U.S.? If so, have they been resumed and have new bilateral assistance agreements been negotiated and entered into since such resumption? No.
11. FAA §.620(w). What is the payment status of the country's U.N. obligations? If the country is in arrears, were such arrears taken into account by the A.I.D. Administrator in determining the current A.I.D. Operating Year Budget? 11. Ecuador is not up to date in payment of UN obligations. The loan will not be authorized unless the Administrator takes into account the status of the GOE with respect to its UN obligations, and determines nevertheless to permit the authorization.
12. FAA §.620(a); App. §.107(a) and (b). Does recipient country furnish assistance to Cuba, sell strategic material to Cuba, or permit ships or aircraft under its flag to carry cargoes to or from Cuba. 12. No.
No.

AID 1240-2 (1-69)

13. FAA §. 620(b). *If assistance is to a government, has Secretary of State determined that it is not controlled by the international Communist movement.* The Secretary of State has determined that Ecuador is not controlled by International Communist movement.
14. FAA §. 620(f), App. §. 109. *Does recipient country have a communist government* No.
15. FAA §. 620(i). *Is recipient country in any way involved in (a) subversion of, or military aggression against, the U.S. or any country receiving U.S. assistance, or (b) the planning of such subversion or aggression.* No.
16. FAA §. 620(n); App. 107(b) and 116. *Does recipient country furnish goods to North Viet-Nam or permit ships or aircraft under its flag to carry cargoes to or from North Viet-Nam?* No.

Military Expenditures

17. FAA §. 620(s). *What percentage of country budget is for military expenditures? How much of foreign exchange resources spent on military equipment? Is U.S. P.L. 480 or development assistance used for military purposes? Are country's resources devoted to unnecessary military expenditures to a degree which materially interferes with* The Military budget is approximately 9% of the GOE budget. A marginal amount of foreign exchange is spent in military equipment. PL-480 or other development assistance is not used for military purposes. The country's resources are not devoted to military expenditures to a degree that materially interferes with its development.

AID 1240-2 (1-69)

its development? (Consideration of these points to be coordinated with PPC/MAS.)

18. FAA §.620(v). App. O. 119. *How much spent by country during current U.S. fiscal year for sophisticated military equipment purchased since January 1, 1968? Has corresponding amount been deducted from current OYB, or is the weapons purchase determined by the President to be important to U.S. national security? (Responses to these questions to be coordinated with PPC/MAS.)*

Sophisticated military equipment has not been purchased since January 1, 1968.

CONDITIONS OF THE LOAN

General Soundness

19. FAA O.201(d). *Information and conclusion on reasonableness and legality (under laws of country and U.S.) of lending and relending terms of the loan.*
20. FAA §.251(b)(2); §.251(c). *Information and conclusion on activity's economic and technical soundness. If loan is not made pursuant to a multilateral plan, and the amount of the loan exceeds \$100,000, has country submitted to A.I.D. an application for such funds together with assurances to indicate that funds will be used in an economically and technically sound manner.*

The terms and conditions of the loan are considered reasonable and consistent with the laws of Ecuador and the United States.

The activity is considered economically and technically sound and the GOE has submitted an application for the loan.

AID 1240-2 (1-69)

21. FAA 8.251(b). Information and conclusion on capacity of the country to repay the loan, including reasonableness of repayment prospects.
22. FAA 8.611(a)(1). Prior to signing of loan will there be (a) engineering, financial, and other plans necessary to carry out the assistance and (b) a reasonably firm estimate of the cost to the U.S. of the assistance?
23. FAA 8.611(a)(2). If further legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of purposes of loan?
24. FAA 8.611(c). If loan is for capital assistance, and all U.S. assistance to project now exceeds \$1 million, has Mission Director certified the country's capability effectively to maintain and utilize the project?
25. FAA 8.251(b). Information and conclusion on availability of financing from other free-world sources, including private sources within the United States.

The borrower has made an application for this assistance and has provided assurance to indicate that the funds will be used in an economically and technically sound manner. The borrower is considered capable of repaying the Loan.

All necessary plans for the project, including a reasonably firm estimate of the cost to the U.S. of the assistance have been prepared.

No further legislative action is required within Ecuador for the Loan.

The Mission Director's certification appears in Annex I of the Loan Paper.

On the basis of appropriate inquiry, it appears that financing for this project is not available from other free-world sources.

AID 1240-2 (1-69)

Loan's Relationship to Achievement
of Country and Regional Goals

26. FAA §.207; §.251(a). Extent to which assistance reflects appropriate emphasis on; (a) encouraging development of democratic economic, political, and social institutions; (b) self-help in meeting the country's food needs; (c) improving availability of trained manpower in the country; (d) programs designed to meet the country's health needs, or (e) other important areas of economic, political, and social development, including industry; free labor unions, cooperatives, and voluntary agencies; transportation and communication; planning and public administration; urban development; and modernization of existing laws.
27. FAA §.209. Is project susceptible of execution as part of regional project? If so why is project not so executed?
28. FAA §.251(b)(3). Information and conclusion on activity's relationship to, and consistency with, other development activities, and its contribution to realizable long-range objectives.

The proposed loan reflects emphasis on these criteria since it is concerned with improving the position of the campesino in the economic structure of Ecuador.

No.

This project is clearly consistent with other development activities in Ecuador as reflected in the project description and contributes to reliable long-range objectives.

AID 1240-2 (1-69)

29. FAA §.251(d)(7). *Information and conclusion on whether or not the activity to be financed will contribute to the achievement of self-sustaining growth.*

As reflected in the paper, the activity will contribute to the achievement of self-sustaining growth in Ecuador.

30. FAA §.281(a). *Describe extent to which the loan will contribute to the objective of assuring maximum participation in the task of economic development on the part of the people of the country, through the encouragement of democratic, private, and local governmental institutions.*

The project will contribute directly to the stated objectives as it will enhance the acquisition of land by and the extension of production credit to campesinos.

31. FAA §.281(b). *Describe extent to which program recognizes the particular needs, desires, and capacities of the people of the country; utilizes the country's intellectual resources to encourage institutional development; and supports civic education and training in skills required for effective participation in governmental and political processes essential to self-government.*

As reflected in the Loan Paper the project meets all the stated criteria.

AID 1240-2 (1-69)

32. FAA §.601(a). Information and conclusions whether loan will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; (c) encourage development and use of cooperatives, credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture, and commerce; and (f) strengthen free labor unions.

This project clearly will encourage the efforts of Ecuador relating to criteria b), c), and e); and e),f) may be indirectly encouraged.

33. FAA §.619. If assistance is for newly independent country; is it furnished through multilateral organizations or plans to the maximum extent appropriate?

Not applicable.

34. FAA §.251(h). Information and conclusion on whether the activity is consistent with the findings and recommendations of the Inter-American Committee for the Alliance for Progress in its annual review of national development activities.

The activity is consistent with the recommendations of the CIAP.

35. FAA §.251(g). Information and conclusion on use of loan to assist in promoting the cooperative movement in Latin America.

The project will assist the promotion of the cooperative movement in Latin America since most of the land purchasers will be cooperatives.

AID 1240-2 (1-69)

36. FAA §.209; §.251(b)(8).
*Information and conclusion
whether assistance will
encourage regional development
programs, and contribute to the
economic and political
integration of Latin America.*

This project does not relate
directly to regional activities.

Loan's Effect on U.S. and A.I.D
Program

37. FAA §.251(b)(6); §.102.
*Information and conclusion on
possible effects of loan on
U.S. economy, with special
reference to areas of sub-
stantial labor surplus, and
extent to which U.S. commodities
and assistance are furnished in
a manner consistent with improv-
ing the U.S. balance of payments
position.*

The proposed loan will not directly
affect the U.S. economy.

38. FAA §.601(b). *Information and
conclusion on how the loan will
encourage U.S. private trade
and investment abroad and how
it will encourage private U.S.
participation in foreign
assistance programs (including
use of private trade channels
and the services of U.S. private
enterprise).*

The proposed loan will not directly
encourage U.S. private trade and
investment abroad or encourage
private U.S. participation in
foreign assistance programs.

AID 1240-2 (1-69)

39. FAA §.601(d). *If a capital project, are engineering and professional services of U.S. firms and their affiliates used to the maximum extent consistent with the national interest?*

The project does not contemplate engineering or professional services.

40. FAA §.602. *Information and conclusion whether U.S. small business will participate equitably in the furnishing of goods and services financed by the loan.*

The Loan Agreement will contain the standard provisions to insure that U.S. small business will participate equitably in the furnishing of goods and services financed by the Loan.

41. FAA §.620(h). *Will the loan promote or assist the foreign aid projects or activities of the Communist-Bloc countries?*

No.

42. FAA §.621. *If technical assistance is financed by the loan, information and conclusion whether such assistance will be furnished to the fullest extent practicable as goods and professional and other services from private enterprise on a contract basis. If the facilities of other Federal agencies will be utilized, information and conclusion on whether they are particularly suitable, are not competitive with private enterprise, and can be made available without undue interference with domestic programs.*

Assistance will be furnished to the fullest extent practicable as goods and professional and other services from private enterprises on a contract basis.

AID 1240-2 (1-69)

43. FAA §.252(a). Total amount of money under loan which is going directly to private enterprise, is going to intermediate credit institutions or other borrowers for use by private enterprise, is being used to finance imports from private sources, or is otherwise being used to finance procurements from private sources.

The proposed loan will be used to facilitate the establishment of small private enterprise operations.

Loan's Compliance with Specific Requirements

44. FAA §.201(d). Is interest rate of loan at least 2% per annum during grace period and at least 3% per annum thereafter?

Yes.

45. FAA §.608(a). Information on measures to be taken to utilize U.S. Government excess personal property in lieu of the procurement of new items.

The loan agreement will provide for compliance with excess property procurement regulations.

46. FAA §.604(a); App. §.108. Will all commodity procurement financed under the loan be from U.S. except as otherwise determined by the President?

Yes.

AID 1240-2 (1-69)

47. FAA §.604(b). What provision is made to prevent financing commodity procurement in bulk at prices higher than adjusted U.S. market price?

The loan agreement will provide for compliance with bulk commodity procurement regulation.

48. FAA §.604(d). If the host country discriminates against U.S. marine insurance companies, will loan agreement require that marine insurance be placed in the U.S. on commodities financed by the loan?

The loan agreement will provide that if it is determined that discrimination exists against U.S. marine insurance companies the requirement will be imposed that marine insurance be placed in the U.S.

49. FAA §.604(e). If off-shore procurement of agricultural commodity or product is to be financed, is there provision against such procurement when the domestic price of such commodity is less than parity?

The project does not contemplate the procurement of any agricultural commodity or product.

50. FAA §.611(b); App. §.101. If loan finances water or water-related land resource construction project or program, is there a benefit-cost computation made, insofar as practicable, in accordance with the procedures set forth in the Memorandum of the President dated May 15, 1962?

The project does not involve water or water-related land resources construction projects or programs.

51. FAA §.611(c). If contracts for construction are to be financed, what provision will be made that they be let on a competitive basis to maximum extent practicable?

No construction contracts will be financed under the loan.

AID 1240-2 (1-69)

52. FAA 0.620(a). What provision is there against use of subject assistance to compensate owners for expropriated or nationalized property?
- An appropriate provision will be included in the loan agreement to insure that proceeds of the proposed loan will not be used to compensate for expropriated or nationalized property.
53. FAA §.612(b); §.636(h). Describe steps taken to assure that, to the maximum extent possible, the country is contributing local currencies to meet the cost of contractual and other services, and foreign currencies owned by the U.S. are utilized to meet the cost of contractual and other services.
- As reflected in the financial plan, maximum feasible local contributions have been sought and obtained.
54. App. §.104. Will any loan funds be used to pay pensions, etc., for military personnel?
- No.
55. App. §.111. Compliance with requirements for security clearance of U.S. citizen contract personnel.
- Requirements for security clearance of U.S. citizen personnel will be complied with.

AID 1240-2 (1-69)

56. App. §.112. *If loan is for capital project, is there provision for A.I.D. approval of all contractors and contract terms?*

A.I.D. will approve any firms or individuals providing services under the loan and the terms of contracts under which such services are provided.

57. App. §.114. *Will any loan funds be used to pay U.N. assessments?*

No.

58. App. §.115. *Compliance with regulations on employment of U.S. and local personnel for funds obligated after April 30, 1964 (Regulation 7).*

Not applicable. The project to be financed under the proposed loan does not involve construction contracts.

59. FAA §.636(i). *Will any loan funds be used to finance purchase, long-term lease, or exchange of motor vehicle manufactured outside the United States, or any guaranty of such a transaction?*

No.

60. App. §.401. *Will any loan funds be used for publicity or propaganda purposes within U.S. not authorized by the Congress?*

No.

AID 1240-2 (1-69)

61. FAA §.620(k).. If construction
of productive enterprise, will
aggregate value of assistance
to be furnished by U.S. exceed
\$100 million?

No.

ACTIVITIES OF USAID IN DETERMINING ATTITUDES OF PERSONS AND GROUPS
AFFECTED BY THE PROJECT

Because of the nature of this project, it is apparent that the attitudes of particular groups within the Ecuadorean society and the government toward the program are fundamental to its success. Unlike a construction project where the opinion of technical personnel is critical, it was apparent to the Mission that the intensive would require a detailed inquiry into such factors as the views of land owners, the attitudes of potential buyers, and the relative enthusiasm of key government officials. In consequence, the initial phase of the intensive review focused upon a series of direct inquiries carried out by Mission employees and by Dr. Carlos Camacho Saa' previously associated with the University of Wisconsin Land Tenure Center.

The survey was directed at the following groups: 1) landowner groups and landowning individuals 2) cooperatives 3) private Ecuadorean banking institutions 4) foreign banks, specifically the two U.S. banks operating in Ecuador 5) GOE officials 6) officials of the Banco Nacional de Fomento and the Cooperative Bank.

1. Landowners

Several meetings were held with the Sociedad de Productores Proprietarios de Tierras Agricolas del Litoral (SIPPTAL), an organization which was considered particularly important as it was the political influence of members of this group which more than any other single factor led to the emasculation of IERAC described in Annex VII. At the initial meeting with this organization it was indicated that the GOE and USAID should not involve themselves in the distribution of settled land but rather should provide credit and other facilities to present owners in order to increase productivity.

The general position of SIPPTAL was that resources, instead of being used to change ownership pattern in "already settled and cultivated land", should be used to foster colonization schemes. After a few points of view were expressed, the real fear of the landowners as far as the effects of the project came to the surface. The landowners were afraid that if the cooperatives were formed, they will loose laborers, and face a more acute scarcity of labor than the one they face at the present. Their argument

UNCLASSIFIED

ANNEX III, Page 2 of 8
Exhibit 1 - Page 2 of 6

is that given present internal and international prices for the main products grown in the country, they will be unable to absorb an increase in wages that could conceivably come about if the project is implemented. Strong criticism of U.S. policies regarding the lack of actions to help Ecuador to get a better price for export products was made.

An extreme view expressed was that the U.S. introduced the "poison of land reform" into Ecuador. One member even made the point that what the U.S. wants is to get rid of "us",--meaning the oligarchy--who are the only capable Ecuadoreans, in order to be able to use and exploit the country as they wish. In general, this position received no comments, favorable or unfavorable from the rest of the audience.

As the points that were made were answered one by one, an agreement reached was that although there were better ways to use the money according to their way of thinking, they will not oppose the project, and possibly they will support it, if the government commits itself to implement it.

After the formal meeting in which the foregoing views were expressed, the Director of SIPPTAL called USAID personnel to an informal meeting at his home. At this meeting the Director indicated that in fact a large number of absentee landowners would be willing to sell land under the project. Apparently, the previous position reflected primarily a disinclination of landowners to appear to be eager to sell lands in view of the threat of land invasion. Thus the indication that SIPPTAL will not oppose this project was reinforced.

In light of the assurances of SIPPTAL neutrality, Mission representatives proceeded to interview a number of landowners individually. Generally speaking, landowners actively engaged in agriculture were not interested in selling their lands under the program but were generally favorable toward the project because of its tendency to reduce pressures of land invasion. Discussions with several absentee landlords revealed a positive interest in selling land under the program. In this connection, the positive interest of Juan X Marcos, a man owning vast stretches of land within the Guayas River Basin, was considered particularly interesting. Eight private owners of land identified 3600 hectares of land which they will be willing to sell at prices consistent with the analysis on this paper. Further, another land owner who had previously sold good agricultural land at 700 sucres per hectare (a figure well below the 2,000 sucres per hectare reflected in the analysis) indicated an interest in selling

UNCLASSIFIED

UNCLASSIFIED

ANNEX III, Page 3 of 8
Exhibit 1 - Page 3 of 6

several thousands hectares. Thus it appears that there is a positive interest on the part of individual landowners in participation in this program.

In addition to individual landowners it was also established that several banks held substantial amounts of land which they would be interested in selling at reasonable prices under the program.

On the basis of the foregoing, it was concluded that 1) land is available in amounts substantially in excess of the number of sound cooperatives to use such land and the capacity of credit under the project to finance it and 2) no serious political opposition is likely to be raised by the landowner groups who have in the past so successfully resisted the government agrarian reform program. The latter conclusion is confirmed by the fact that no opposition to the project has been brought to bear during the past few months of project development. If SIPPTAL was going to move, it would have done so already.

2. Cooperatives

Not surprisingly, cooperative groups reacted enthusiastically to the proposed program.

As the program is scheduled to start with the members of USAID sponsored rice cooperatives, informal interviews were held with officials of the nine cooperatives under the program. The main conclusion of these interviews is that the membership regards the inability to purchase land as the major obstacle to further improvement of their economic well being and growth of cooperatives into viable permanent organizations. On the other hand, the officials of the two cooperatives that have purchased land regard this purchase as the major achievement of the organization.

It was pointed out by members of the cooperatives that when the purchase of land is not feasible, it is difficult to attract members notwithstanding the advantages in terms of purchase of inputs and marketing facilities that the cooperatives can provide at present.

The proposed credit terms and anticipated land prices were explored and considered satisfactory.

UNCLASSIFIED

UNCLASSIFIED

ANNEX III, Page 4 of 8
Exhibit 1 - Page 4 of 6

It might be noted that the Mission relied heavily in its analysis on its own personnel and CLUSA contractors for its evaluation of the project from the viewpoint of cooperative buyers.

3. Private Ecuadorean Banks

Private banks were canvassed primarily with a view to determining the availability of production credit for guaranty under the program as originally conceived. Six private banks in Guayaquil, Babahoyo and Quito were interviewed. These banks indicated a range of reactions from lack of immediate interest to refusal to participate in production credit financing under the program. Generally speaking, the private banks have established credit lines with the larger farmers and were unwilling to become involved in cooperative financing until such time as the financial reliability of the cooperatives was established. It was in part on the basis of these interviews that the Mission concluded that the original plan calling for guaranty of agricultural credit rather than direct generation of the credits as proposed for this loan would be impossible.

The Association of private Banks was approached also. It indicated that it found the project desirable for Ecuador but that the operation should be handled by the BNF.

4. Foreign Banks

The Mission conducted extended discussions with the managers of the First National City Bank and the Bank of America which maintain branches in Ecuador. Both of these banks indicated a positive interest in the program at the outset. However, during the spring the GOE passed legislation requiring substantial amounts of housing bonds to be purchased by the banks. In consequence, both banks indicated that it would be impossible for them to consider further participation in this project at the present time.

5. Banco Nacional de Fomento and Cooperative Bank

Discussions with the Cooperative Bank indicated its willingness to support the program although the Bank was of the view that in light of its limited resources, even assuming it receives the proposed loan from USAID it would not be desirable for the Bank to undertake the program at the present time, a view with which the Mission concurred.

UNCLASSIFIED

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ANNEX III, Page 5 of 8
Exhibit 1 - Page 5 of 6

The BNF indicated strong interest in the program. It further has demonstrated this through its cooperation with the Mission in preparation of this paper and its representations to the Ministry concerning its interest in handling the project. Apparently BNF is the appropriate institution to handle the operation.

6. GOE Officials

Interviews were conducted with Government officials at all levels in the Ministry of Agriculture, the National Planning Board, the National Rice Commission, and other organizations. A generally positive reaction was obtained at all levels. One persistent cloud on this attitude was the view expressed by many lower level government officials concerning the desirability and necessity that IERAC be the administrating organization. Generally speaking, these views were expressed by persons previously associated with IERAC. When the IERAC question was put to the Ministry of Agriculture, he agreed that it would not be desirable at the present time to consider IERAC as the administrating organization and subsequently no further serious objections were advanced on this basis. The Mission considers the response of officials interviewed to have been highly favorable.

On the basis of the foregoing review, the Mission concluded that the land sale guaranty operation as presented in the IRR was entirely feasible and indeed would be limited primarily by the capacity to form sound cooperatives. The guaranty of production credit was eliminated from the program and direct generation of production credit substituted as there simply did not appear to be significant resources available within the economy to carry out this element of the program. Finally, the attitude of all concerned was generally positive with the exception of the pressures previously noted for the involvement of IERAC. It is clear that there will be no immediate danger of interference. With respect to the future, the Mission itself would be favorably inclined toward development of IERAC participation in the operation provided that the organization can be resuscitated. The likelihood is that if significant improvements in the organizations status are not carried out,

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pressures to involve IERAC will not be particularly meaningful. Conversely, if the organization is substantially improved the Mission would consider it desirable to involve IERAC. The Mission's conclusion on this point is that this problem is well in hand.

CIUSA/USAID/E AGRICULTURAL COOPERATIVE DEVELOPMENT
PRCGPAM

Lewis Townsend
Agricultural Coops. Advisor

Gustavo Riofrío
Rice Project Director

Administrative Assistant
Education R. Leon
Extensionist G. Velastegui

Coordinator of Legal, Education and Public Relations Matters
P. Maldonado

Secretaries
M. González-Rubio
I. Proenza

EXTENSION TEAM

1. Land tenure solutions.
3. Supply of inputs.
5. Supply of credit.
6. Marketing plans.
7. Cooperative extension.
 - a. Organization.
 - b. Legalization.
 - d. Basic Education.
 - e. Administration & management

EXTENSIONISTS

Daule Valdivieso	Milagro - Yaguachi Benítez	Vinces Armendariz
Babahoyo Falconí	Sanborondón Salazar	
Ass't	Secretary	

ACCOUNTING-AUDITING TEAM

- c. Accounting and auditing.

ACCOUNTANTS

Zones Daule Milagro Babahoyo	Zones Yaguachi Vinces Babahoyo
Layana	Mosquera

PRODUCTION TEAM

4. Production improvements.
 - a. Modern techniques.
 - b. Use of inputs.

AGRONOMISTS

Zones Milagro Yaguachi Babahoyo	Zones Daule Vinces Babahoyo
Montesdeoca (R.C.)	Salgado (M.A.)

INFRASTRUCTURE TEAM

2. Development.
 - a. Topographical plans.
 - b. Loans (application)
 - c. Supervision of construction.

AGRONOMIST

Moncayo

Topographer López	Topographer Verdesoto
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 ANNEZ III - Page 7 of 8
 Exhibit 3 - Page 1 of 2

<u>Legalized Cooperative</u>	<u>Location</u>	<u>Extension Zone</u>	<u>Legalization Date</u>	<u>Number Members</u>	<u>Coop Bank Members (X)</u>	<u>Paid Capital & Reserves</u>	<u>1959 Earnings To Date</u>	<u>Total Social Cap. (Assets)</u>	<u>Land Owned Hac.</u>
1. Yaguachi	Yaguachi	Yaguachi	June/67	15	X	5,250.87	(718.30)	12,751.23	
2. Jujan	Jujan	Yaguachi	Nov./67	13		100,742.00	10,291.57	497,928.67	561
3. La Unión	Duile	Duile	May/68	14	"	24,177.80	19.00	210,213.20	
4. Narcisca de J.	Nobol	Duile	Aug./68	15		1,720.00		4,511.00	
5. Juan Montalvo	Babahoyo	Babahoyo	May/68	20	X	1,108.00	11,500.00	159,951.00	225
6. El Roblecito	Ricaurte	Babahoyo	May/68	11	X	143,268.35	(25,966.22)	1,215,078.93	360
7. Las Mercedes	Babahoyo	Babahoyo	1961	55	X	50,834.29	6,390.30	98,267.60	300*
8. La Carmela	B. Capos	Milagro	June/68	44		16,713.50	17,256.75	333,374.54	567*
9. San Juan	P. Viejo	Babahoyo	May/69	23	X	?	?	?	
TOTALS				265		308,986.81	19,735.09	2,562,239.87	

Pre-Coops

1. Cañaverl	Caracal	Babahoyo		25					
2. Pueblo Nuevo	F. Cordero	Babahoyo		25					
3. Rosa Elvira	Taura	Milagro		27					
4. Huancavilca	Milagro	Milagro		26					
5. Ecuador	La Beldaca	Yaguachi		25					
6. Villa Mercedes	Yaguachi	Yaguachi		25					
7. Legua de los Indios		Vinces		26					
				<u>272</u>					

Total members of cooperatives and pre-coops

537

Additional groups under study: Mananica, Colinas, Laurel, Ventanas, Jiguel.

*Land in possession of cooperatives under negotiation with owners.

UNCLASSIFIED
 AMEX 111 - Page 2 of 2
 Exhibit 2 - Page 2 of 2

LENDING PROCEDURES OF THE DIVISION OF SUPERVISED CREDIT

Guarantees

Short and medium-term loans should be guaranteed by crop liens, preferably on the products financed by the loan; long-term loans must be guaranteed by a mortgage. The relation between current value of the guarantees with that of the loan should be one to one. Where the Bank considers it necessary, additional collateral may be requested of one borrower.

Loans to cooperatives should be guaranteed with the assets of the borrower cooperative. If the value of such goods is not sufficient, pledges or mortgages should be taken from the borrower cooperative members. The amount of loan should in no case exceed 70% of the value of the guarantee.

Requirements for obtaining Supervised Agricultural Credit

The Bank requires that an applicant must meet the following requirements in order to qualify for a supervised credit loan:

- a) To be legally capable and of full age; b) to be a farmer with sufficient experience to administer his farm; c) to own a family type farm with definite or provisional title duly legalized and registered; d) to exploit directly the farm and to live permanently in it or in a town nearby; e) to be a farmer as a main occupation; f) to be capable of fulfilling its obligations concerning planning, effective administration of the farm and making timely payments of the loan.

Likewise, it requires that production and marketing cooperatives in order to be qualified for this type of loans meet the following:

- a) To be legally constituted and composed of small farmers who meet the same conditions required individually; b) to present a feasibility study of the project needing financing in which the technical and financing elements of the enterprise are described, the results to be obtained and the possibilities of repaying the loan; c) the cooperative should agree to a financial auditing by an authorized representative of the Bank.

UNCLASSIFIED

ANNEX IV, Page 2 of 12
Exhibit 1 - Page 2 of 3

The recommendations made after the auditing in regard to the administration of the loan are mandatory to the cooperative.

Procedures for the loan application and collection

Any applicant initiates his contact with the Bank by visiting with the Branch Manager, who determines the eligibility of the applicant. Once the Manager approves, the application goes to the credit division where it is registered and the reports concerning the solvency of the applicant and his guarantor are made by the Bank. From there on, it goes to the manager's office who decides either to accept or reject the loan application. After that it goes to the legal and auditing departments where the corresponding reports are prepared. Included in this phase is the evaluation of the land and of the guarantees, and checking all matters related to investments. These reports are passed on to the analyst of the credit division who determines the approval or rejection and the conditions of the loan. If the case merits approval by the manager, he gives a final decision or sends the application to the main office attaching his own report when the lending operation must be decided by the general manager or the Board of Directors of the Bank.

With the determination by the competent authority, the appropriate entries are made in the records, then it goes to the legal section to prepare the details of the guarantees needed in the transaction. Once all steps are finalized, the manager and the borrower proceed to the signing of the documents.

The loan is not made effective until it is included in the accounts. After fulfillment of this requirement disbursements start in accordance with the provisions of the respective agreement.

The General Manager decides on original loans exceeding the operating quotas assigned to the branch manager, as well as on those financed out of the AID funds. The Board of Directors decides on the cases of applications submitted by members of the board or his relatives, when waiving interests payments, or applications submitted by enterprises in which the members of the Board have some participation as shareholders or administrators and those that may be financed by issuing security mortgages.

After a medium or long-term loan has been granted, additional loans may be authorized to the same borrower in the following cases:
a) when because of unforeseen events a larger investment is required

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than that authorized by the original loan; b) if there is a substantial increase in the cost of labor, seeds, fertilizers, insecticides, machinery and other elements that change substantially the investment plan; c) in the event that a substantial or unforeseen increase in the cost of agricultural or livestock production occurs justifying an additional investment in the cultivation or livestock enterprise; d) when other reason exists that justify such a decision, providing the administration and planning of the farm demonstrates capacity of repayment of the original and of the additional loans.

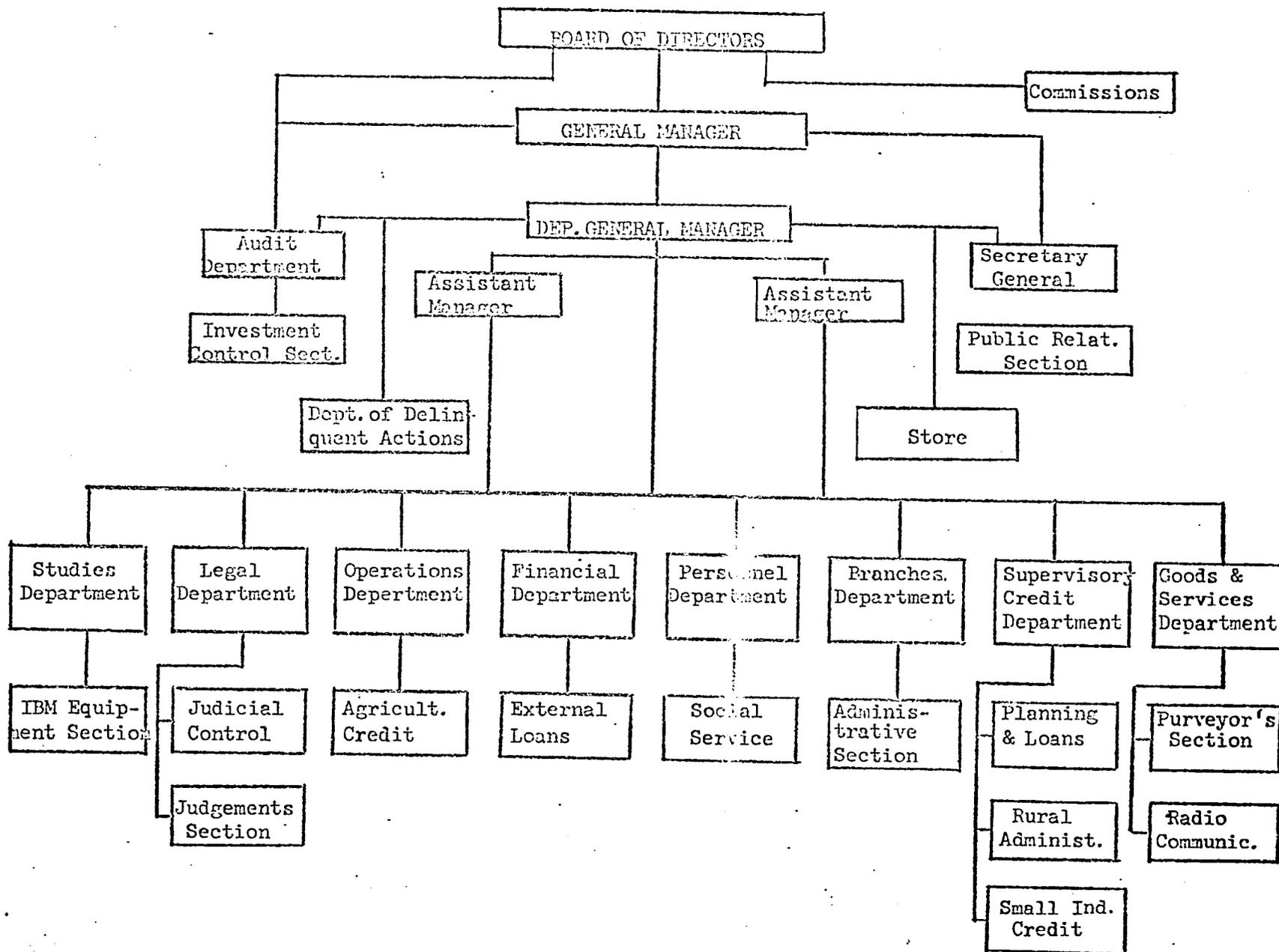
Loan Supervision

The bank has set forth regulations concerning supervision of its loans. In practice, inspections are made when an application has been presented by borrowers who still have pending operations with the Bank, or when the disbursements in accordance with the agreement required prior inspection or in case of gross irregularities by the borrowers. This procedure of the bank is required due to the limited number of inspectors, who have to cover great distances in remote places without adequate services, roads or adequate funding which reduces the possibility of making frequent visits to farms. The Bank is looking into this matter with a view to increasing the number of supervisors.

The functions of the supervisors are 1) to see that crops are sent to the stipulated destinations in the investment plans or administration plans of the farm; 2) to assure that at the end of the farming year that progress has been made; 3) to review and evaluate financial data; and 4) to program new plans for the farms for the coming year.

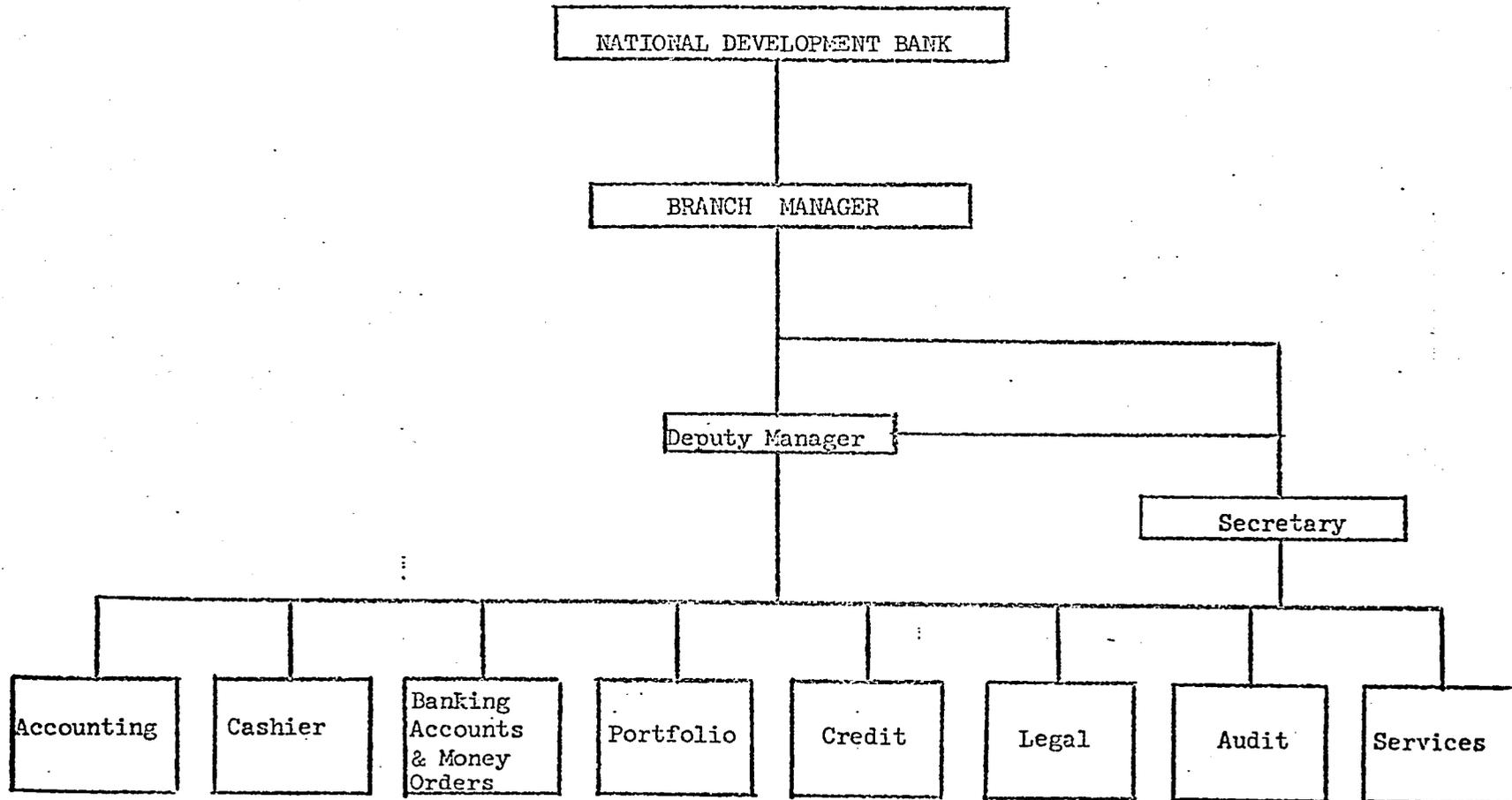
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ORGANIZATIONAL CHART - NATIONAL DEVELOPMENT BANK



ORGANIZATIONAL CHART OF A BRANCH OF THE

NATIONAL DEVELOPMENT BANK



CURRICULA VITAE

1. Name LUIS ERNESTO BORJA MURILLO,
General Manager

Age 57 years

Education Political Science (New York
University)
Agrarian Economics (New School)

Experience with the National
Development Bank Mortgage Bank of Ecuador:
Statistics Assistant, Statistics
Chief, 1936/1943

National Development Bank:
Assistant Manager for Administration:
General Assistant Manager: I-14-45
to XII-31-46; Representative
Director, to the National Economic
Council; Deputy Director to the
President; Director-President
III-1-49 to VII-30-52; General
Manager: IX-11-62 to date.

Administrative Experience Personnel Director of the Flota Mer-
cante Gran Colombiana in New York
from September 1952 to August 1962.

2. Name ANGEL AUGUSTO DONGILIO DEL
POZO, Assistant General Manager

Age 58 years

Education Lawyer

Experience with the National
Development Bank Mortgage Bank of Ecuador: Delegate
from Guaranda, 1943 - 1944.

Guaranda Branch: Manager VIII-8-44
to VIII-27-48

Experience with the Private
Banking Institutions

National Development Bank:
Assistant General Manager:
IX-28-67 to date.

Administrative experience

Central Bank of Ecuador

"24 de Mayo" School, Quito,
Teacher, 1936-1938; Vice-
Principal "Pedro Carbo"
School, Guaranda, 1938 to 1944

Central University, Quito:
Teacher of the Faculty of Law,
1953 to date

3. Name

ALFONSO RENEE BENALCAZAR
RUALES, Director of the Department
of Supervised Credit

Age

40 years

Education

Economist
Agriculture Economics, U. S. A.

Experience with the National
Development Bank

Quito: Chief, Studies, Section,
Technical Department; advisor
to the Supervised Credit Department;
Director of the Supervised Credit
Department, II-15-60 to IX-22-61;
X-15-65 to date

4. Name

JAIME REINALDO BURBANO RUALES,
Advisor to the General Manager

Age

53 years

Education

Engineer Agronomist
Agricultural Credit: U. S. Department
of Agriculture, 1942-1943
Agrarian Economics

Entrance date	June 12, 1945 to March 11, 1947; July 3, 1951
Experience with the National Development Bank	Quito, Regional Advisor to the Sierra. Agriculture Inspector, VI-12-45 to III-11-47; Chief of the Agriculture Extension Department, VII-3-51 to XII-31-55; Deputy Chief of the Technical Department, I-1-57 to XII-31-59; Deputy Director of the Technical Department, I-1-60 to II-17-63; Director, Technical Department II-18-63 to VI-5-63; Director, Studies Department, VI-6-63 to VII-31-65; Director of the Supervised Credit Department, VII-1-65 to IX-20-65; Advisor to the Supervised Credit Department, IX-21-65 to VI-25-67; Assistant to the Manager: VI-26-67 to date
Administrative Experience	Food and Agriculture Organization of the United Nations - Economist from 1947 to 1951
5. Name	OTTO EMILIO ANDRADE STAHL-SCHMIDT, Director, Financial Department
Age	45 years
Education	Economist International Law and Economic Sciences, Technical Teaching-BID-CEMLA-Mexico
Experience with the National Development Bank	Technical Assistant, Agronomist, Agriculture Specialist, Economist, Chief of the Industrial Section, Deputy Director of the Technical Department, Deputy Director of the Studies Department; Director of the Financial Department, from V-31-55 to date

Experience with private
banking institutions

Banco de Préstamos: Quito.
Banking Accounts Assistant,
July 1945 to September 1946.

Administrative Experience

Caja del Seguro. Quito. General
Assistant for Credit, X-46 to VI-55.

Casa "López" Quito. General
Assistant for Credit, XI-44 to VI-55.

Empresa Editora "Cosmos".
Reporter. V-44 to IX-44.

BNF PLAN FOR IMPROVING DELINQUENT ACCOUNTS *

In order to expedite the process of improving its portfolio, the BNF has proposed to the IDB a plan whose principal aspects are now being executed. This plan can be summarized as follows.

- a) It will be supervised by a new Department of Delinquent Accounts, currently operating as a section,** and will be executed with the active participation of the branch managers and inspectors. The functions of the new department will be chiefly the following:
 - i) to supervise administrative or extralegal steps for collection of delinquent loans and to oversee, with the advisory services of the Legal Department, legal collection measures taken by the institution; ii) to verify that operations of renewal, consolidation, replacement and others decided upon by the Board of Directors or General Manager are carried out within the terms set forth in the BNF credit manual; iii) to establish a register of undesirable clients or those temporarily prohibited from operating with the bank; iv) to ensure that two or more branches do not grant loans to the same client; v) to ensure that the prohibition against operating with delinquent debtors is enforced, and vi) to maintain a register of debtors whose obligations have been written off. In order to carry out these new functions, the department will be divided into three sections: one to supervise legal recovery procedures; another to supervise extralegal collection operations and a third responsible for preparing and keeping up to date the various registers of clients.
- b) In each of the branches in the most important cities, such as Quito, Guayaquil, Manabí, Cuenca, etc., portfolio recovery sections will be established under the Department of Delinquent Accounts, with one chief, two special inspectors and a number of administrative officers. The work of these sections will be coordinated with the Department of Delinquent Accounts and will supplement the efforts of the branch managers and their permanent inspectors.
- c) Special investigations will be carried out through the Department of Delinquent Accounts on the factors that have contributed

* Source: IDB, Loan to the Banco Nacional de Fomento, Agricultural and Industrial Credit Program, February 19, 1969.

** The Board of Directors of the BNF has already approved the plan for collection of delinquent accounts and has agreed that the portfolio recovery section should become a department. To this end, a project for amendment of the institution's bylaws is being prepared and will be submitted soon to the Banking Authority of Ecuador for approval.

to the success or delinquency of the different types of credit, by geographic area, allocation, term, etc. This department will bear responsibility for recommending, on the basis of the results of such investigations, the changes deemed advisable in the credit manuals, administrative standards and collection procedures of the institution.

- d) For credits still to fall due, the BNF has established a system of notices with the first sent 10 days prior to maturity, the second on the date of maturity, a third eight days after that date and a fourth 15 days after maturity. Within 30 days after expiration of a loan term, a BNF inspector will visit the debtor to arrange some type of settlement. If, after the inspector's visit, no satisfactory settlement formula is reached, legal steps will be taken for collection. If a settlement is arranged but the commitment is not carried through, collection will also be made through legal means.

The BNF proposed to the IDB Management that any loan that should become delinquent in the future would be collected legally within not more than 30 days after the date of the respective maturity. The BNF has agreed that, within the period stated in its bylaws (not to exceed 90 days), when any installment of amortization or interest is not made on a credit financed with the resources of a Bank loan, the legal action necessary for its recovery will be undertaken, except in duly justified cases.

- e) Credits that were more than six months overdue on the date of inspection of the plan on which no legal action has been taken will be collected legally and this process will be halted only if a means of settlement with the defendant is reached.
- f) By Resolution 517, dated June 5, 1968, the Monetary Board of Ecuador authorized an increase in the interest rate charged by the BNF on delinquent loans from 10% to 12%, so that the pressure of this financial penalty would force clients to pay off their delinquent obligations with the bank.
- g) The BNF has proposed to achieve in the next five years a delinquent portfolio balance representing not more than 15%, through a 1% deduction in the first year, 2% the second year, 3% the third year,

*

3.7% the fourth and the remainder in the fifth year . As of the close of 1967, the amount of the overdue portfolio represented 27.2% of the total amount of loans in effect and, as of June 30, 1968, this ratio had declined by 3.1% to 24.1%. It must be borne in mind, however, that as of June 30, 1968, credits granted by the former Development Credit System maturing prior to December 31, 1962, totaling S/. 39.4 million (US\$2.2 million) were written off, accounting for almost all of the improvement noted in the first half of this year.

* It should be noted that in May 1967 the political constitution enacted by the Constituent Assembly of Ecuador abolished as an admissible legal system for the collection of credits of various institutions, including the BNF, what is known as "compulsory jurisdiction". After examining the legality of the action taken by the Constituent Assembly, the Supreme Court of Ecuador declared that in order to reintroduce compulsory jurisdiction a constitutional amendment would be required. The Government of Ecuador has agreed to accept as a condition of the guarantee contracts for the proposed loan support of the BNF and other credit institutions in seeking the necessary constitutional amendment and thus re-establishing compulsory jurisdiction. It is considered, however, that this legal procedure is not an essential condition for attainment by the BNF of a suitable level of collection and it is therefore recommended that no such clause be included in the guarantee contract.

THE COOPERATIVE MOVEMENT IN ECUADOR AND ITS RELATION WITH USAID

1. Introduction

The Ecuadorean cooperative movement is of great interest to USAID because it has proved to be a successful device for mobilizing small savings, redistributing income to lower and middle income groups and bringing additional agricultural lands into production. As such, it has proven its value as a vehicle of AID objectives in Ecuador and will continue to receive strong support from the Mission. As this project will utilize the vehicle of cooperatives, background on the cooperative movement in Ecuador and the relation of USAID to the movement is of importance.

2. The History and Nature of the Cooperative Movement in Ecuador

The first cooperative in Ecuador was organized in 1919 and the first Cooperative Law was passed in 1939 by which time 17 cooperatives had come into existence. The growth rate increased to approximately twenty yearly, and the number of cooperatives reached 482 by the end of 1960. With the beginning of technical assistance on the part of the USAID and others and the promulgation of the Agrarian Reform Law in 1963, the growth rate has sharply increased to more than 150 new cooperatives yearly. As of February 28, 1969 there were 1,812 cooperatives legalized and registered in the National Directorate of Cooperatives of the Ministry of Social Welfare.

It should be recognized that most of these 1812 cooperatives are not affectively functioning organizations as many were formed to gain tax advantages, to obtain land under the Agrarian Reform Law or perhaps to further some individual's political ambitions. Perhaps 500 cooperatives are sound organizations in cooperative terms. The "real" cooperatives of small farmers, artisans and the urban middle class have required inputs of technical assistance from advisory agencies such as USAID, OAS, Government of Israel, CEDOC (Catholic Labor Unions) and private organizations supported by international organizations such as MISEREOR. Many of these cooperatives are members of the Cooperative Bank, whose membership

now totals 187 cooperatives.

Realizing the need to increase and improve the effectiveness of technical support to cooperatives, the National Directorate of Cooperatives with support from most of the cooperative technical assistance agencies is presently planning a nation-wide census of cooperatives to determine their actual status so as better to program effective use of technical assistance. Also, the USAID Mission has invited a CLUSA Programming Team to visit Ecuador to assist the Mission in analyzing technical assistance and plan effective programs.

Notwithstanding the requirements for improvement in many cooperatives significant achievements have been made where technical assistance and financing has been available. These areas of success and the involvement of USAID in achieving this result are described in the following paragraphs not only to record what has been done but also to suggest the potential which can be tapped with the help of further AID support.

3. Credit Unions

By far the most important group of cooperatives in Ecuador are the credit unions whose formation began in 1963 through technical assistance received from a grant-financed USAID/CUNA contract and from the Peace Corps. The National Federation of Credit Unions now comprises 220 cooperatives, 136 of which are affiliated with the Cooperative Bank. The 220 cooperatives in the Federation have a combined membership of more than 45,000. Multiplying this figure by 5 as rough average of family size, it can be seen that the credit union movement now involves 225,000 people, or close to 4% of the country's population.

Although the initial emphasis of the credit union program was on lending for consumption purposes, the emphasis now is on production credit, particularly for agriculture. Since 1965, the National Federation of Credit Unions has sponsored a Program of directed agricultural production credit. This program now involves 26 credit unions and an estimated 4,000 farmers. Of all loans granted by Federation-affiliated credit unions in 1968, an estimated 30% were

for agricultural purposes.

The total capital of the Federation-affiliated cooperatives amounted to S/104,837,000 (US\$ 5,766,600) at the end of 1968, up 60% from the end of 1967. Of this amount S/72,282,000 (US\$ 3,975,900) represented savings by credit union members (up 63% from the previous year). Most of the remainder was accounted for by credit union borrowing from the Cooperative Bank. As of December 31, 1968, savings in credit unions represented an amount equal to 7% of the savings in commercial banks. In 1968, 89% of the Bank's loans were to credit unions a percentage that is expected to decline in the future as increasing numbers of agricultural production and marketing cooperatives join the Bank.

4. Coffee Cooperatives

A USAID financed CLUSA administered program was initiated in 1966 to improve the economic status of small coffee growers by organizing them into coffee marketing cooperatives so as to eliminate the middlemen in the export marketing process. There are now 50 coffee marketing cooperatives with 5,000 members. They are grouped into five regional unions of cooperatives and a National Federation of Coffee Cooperatives. One of the regional unions now owns a coffee processing plant and another is negotiating for the construction of a modern plant. The others rent or contract processing plants but are developing plans for construction of their own processing facilities.

Cooperative marketing arrangements have helped individual members' income rise by at least \$4 per bag since the program began in 1966. Total exports by the coffee cooperatives in 1968 were valued at US\$ 2,500,000 and exports of US\$ 4,500,000 are expected in 1969. For the 1968-69 coffee year, the cooperatives have secured 17% of the country's total coffee export quota. This is equivalent to approximately 110,000 sacks or more than twice the amount received in 1967-1968, when the cooperatives received 10% of the lower country quota figure of 500,000 sacks. As the program is now well

established, CIUSA support of the program has been reduced to a minimum since January, 1968 (US\$ 10,200 in FY 1969) and is expected to terminate completely by June, 1969.

5. Rice Cooperatives

While phasing out of the coffee cooperatives program, CIUSA/Ecuador began in late 1967 to devote its attention to rice cooperatives. Although the original intention of the program was to organize marketing cooperatives similar to the coffee cooperatives, a study of the position of the small rice growers in Ecuador--who grow perhaps as much as 75% of the country's rice--led to the conclusion that new methods of production would have to be explained along with marketing arrangements. It was also recognized, though, that the willingness of the small rice farmer to adopt new methods of production would be limited unless he was assured more secure tenancy arrangements or, even better, land ownership.

It has been found that there are good prospects for small rice farmers to purchase land. Many landowners in the Cuyapas River Basin are willing to sell their land at prices that are favorable to small farmers in comparison with the rentals they are now paying. A major obstacle to land sales to small farmers has been the lack of an effective mechanism for effecting land sales in light of the traditional distrust by owners to extensions of land purchase credit to campesinos. To meet this need, USAID/Ecuador is proposing this loan to establish a pilot project for a guarantee system for land sales and for production credit to small farmers buying land.

To date 9 rice production/marketing cooperatives, comprising 285 rice farmers with an average of 7 hectares per member have been legalized under the CIUSA/Ecuador program and 7 other pre-cooperatives are participating in the program. Two of these have been able to purchase land with a 10% cash down payment, the remainder to be paid over a five-year period. That these cooperatives have been able to secure financing for their land purchases is considered highly significant of the growing regard for cooperatives in their areas.

In addition to the services of the CIUSA/Ecuador team, there have been several other technical assistance inputs into the rice cooperatives program. Both the National Rice Commission and the Ministry of Agriculture have made available agricultural extensionists to assist with the program. A USAID/Ecuador extension advisor has got up 35 rice demonstration plots and 13 fertilizer trials. Several Peace Corps Volunteers are also working with the program.

Progress to date, while encouraging, should be considered modest. In some cases, anticipated results have not been achieved. In two of three cooperatively-farmed "capitalization plots" of 15-20 hectares yields expected from the adoption of new techniques and use of improved seed were not achieved largely because of the inability of the farmers to assimilate fully the new techniques. Another problem has been adverse weather. Drought conditions have limited the demonstration plots and have also reduced yields. Nevertheless, the farmers who participated in these projects have learned much from their experience, and increased yields can be expected in the future.

Despite these difficulties, there are still ample grounds for optimism regarding the future of the program. Initial expectations were too optimistic in view of the low socio-economic and education levels of the great majority of small rice farmers. Taking this problem into account--as well as adverse weather conditions--progress has been significant. The land purchases, the ability of several cooperatives to obtain for the first time commercial loans instead of much higher interest loans by loan sharks, and a demonstrated willingness to adopt new methods of production are indications that the program will soon begin to achieve significant results.

6. Sierra Agricultural Cooperatives

The CIUSA program is at present studying how technical assistance inputs through existing organizations can assist agricultural cooperatives in the Sierra to improve their programs.

7. Peace Corps Participation

In the early stages of the development of the Credit Union Program the need for continual education and assistance in administration was evident. Consequently, the Honduran 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 arrived in January 1964 and assisted mainly in the organization of new cooperatives. The second and third groups which arrived in late 1964 and mid-1966 worked mainly in improving the quality of the cooperative operations. Of the fourth group of 25 volunteers which arrived in September 1968, 15 devote their time to improving credit union operations while 10 are working specifically with small group of farmers participating in the production credit program.

To date more than 100 Peace Corps Volunteers have worked in the credit union program. In addition, 8 volunteers are working under informal arrangements with the Rice Cooperative Program or with the new Sierra agricultural cooperative program. The effectiveness of the Peace Corps Volunteers working in the rice areas has been disappointing, with some notable exceptions. The reasons for this ineffectiveness have not yet been fully analyzed, but a resolution of the difficulties is strongly to be hoped for, as the Peace Corps represents a potentially valuable input to the program. One obvious problem has been that no Peace Corps group has been trained specifically for agricultural cooperatives, but plans are being made to undertake such a program in 1970.

One concludes from the foregoing that as the quality of technical assistance improves, the cooperative movement will show further gains. Limitations on progress are not wholly attributable to the cooperative membership.

8. Summary

Of the 187 cooperatives now members of the Cooperative Bank, 136 are credit unions, only 31 are agricultural (including 5 banana

UNCLASSIFIED

ANNEX V - Page 7 of 7

cooperatives), and the remaining 20 are of various other categories. However, as the USAID/CIUSA Agricultural cooperatives Program strengthens and grows the number of agricultural cooperatives is expected to increase rapidly. Access to credit on reasonable terms from the Cooperative Bank will be a powerful stimulus to further improvements in the economic position of these low-income farmers. The proposed project is expected to provide a great impetus to further growth of the Cooperative Movement in Ecuador.

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PER HECTARE COSTS OF SUBSISTENCE RICE FARMING

UNDER TRADITIONAL METHODS OF CULTIVATION

(Costs in Sucres)

Operations	Use of Vehicles & Machinery		Manpower				Materials		Total Cost	Cash Outlays 1/	
	Unit	Cost	Total		Hired Labor		Quantity	Cost			
			Days	Cost	Days	Cost					
1. Clearing			10	200	5	100			200	100	
2. Burning			1	20	1	20			20		
3. Clearing			3	60	3	60			60		
4. Hand Seeding			10	200	5	100			350	250	
5. Bird Control - I			3	75	1.5	35	1qq.	150	75	40	
6. Herbicides			2	50	1	25			170	145	
7. Fertilizer Applic.			2	40	1	20	1gal.	120	180	160	
8. Weeding			20	400	10	200	2qq.	140	400	200	
9. Pesticides			4	80	2	40			210	170	
10. Bird Control .. II			2.5	65	1	25	2kg.	130	65	40	
11. Harvesting			25	375	13	195			400	205	
12. Transport	\$/ 6/qq.	120						25	120	120	
13. Interest 2/									110	110	
14. Contingencies 3/									80	80	
15. Amortization of Land Purchase									360	360	
Totals		<u>120</u>	<u>82.5</u>	<u>1,565</u>	<u>43.5</u>	<u>820</u>	<u>39</u>	<u>745</u>	<u>565</u>	<u>2,800</u>	<u>1,980</u>

1/ Excludes the value of family-labor inputs.

2/ Eight percent of the cash outlays for items 1-12 (rounded to the nearest ten sucres)

3/ Five percent of the cash outlays for items 1-13 (rounded to the nearest ten sucres)

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SUBSISTENCE RICE FARMING UNDER TRADITIONAL METHODS

OF PRODUCTION: PER-HECTARE COSTS, REVENUES, AND NET INCOME

(Based on an average yield of 20qq. of polished rice per hectare; one crop annually)

		<u>Alternative Price Assumptions (per qq.)</u>		
		<u>S/ 110</u>	<u>S/ 135</u>	<u>S/ 160</u>
A. Including Imputed costs of Family Labor				
Revenues		S/ 2,200	S/ 2,700	S/ 3,200
Costs		<u>2,800</u>	<u>2,800</u>	<u>2,800</u>
Net Income		- S/ 600	- S/ 100	S/ 400
B. Excluding Imputed costs of Family Labor				
Revenues		S/ 2,200	S/ 2,700	S/ 3,200
Costs		<u>1,980</u>	<u>1,980</u>	<u>1,980</u>
Net Income		S/ 220	S/ 720	S/ 1,220

PER-HECTARE COSTS OF COMMERCIAL RICE FARMING
UNDER IRRIGATED AND MECHANIZED METHODS OF PRODUCTION

(Costs in Sucres)

Operations	Use of Vehicles & Machinery		Manpower				Materials		Total Cost	Cash Outlays 1/	
	Unit	Cost	Total		Family Labor		Hired Labor				
			Days	Cost	Days	Cost	Days	Cost			
1. Clearing	1 hr.	100							100	100	
2. Soil Preparation	7 hrs.	475							475	475	
3. Seeding)								2qq.	400	400	
4. Fertilizer) Application)	1 hr.	100	4	80	4	80		3qq. P	220		
								2qq. K	95		
5. Herbicides			2	60	2	60		8qq. N	560	1,055	975
6. Hand Weeding			10	200	5	100	5	2gal.	440	500	440
7. Pesticides-I & II			4	120	2	60	2	2 kg.	130	200	100
8. Irrigation		500	5	100	5	100				250	190
9. Cleaning of Irrig. Dikes & Canals			3	60	3	60				600	500
10. Bird Control			10	200	5	100	5			60	
11. Harvesting	1.7 hrs.	500								200	100
12. Transport	\$/ 4/qq.	280								500	500
13. Interest 2/										280	280
14. Contingencies 3/										370	370
15. Amortization of Infrastructure										250	250
16. Amortization of Land Purchase										750	750
Totals		<u>1,955</u>	<u>38</u>	<u>820</u>	<u>26</u>	<u>560</u>	<u>12</u>	<u>260</u>	<u>1,845</u>	<u>6,350</u>	<u>5,790</u>

- 1/ Excludes the value of family labor-inputs.
2/ Eight percent of the cash outlays for items 1-12 (rounded to the nearest ten sucres)
3/ Five percent of the cash outlays for items 1-13 (rounded to the nearest ten sucres)

COMMERCIAL RICE FARMING UNDER SEMI-MECHANIZED METHODS

OF PRODUCTION: PER HECTARE COSTS, REVENUES, AND NET INCOME

(Based on an average yield of 40 qq. of polished rice per hectare; one crop annually)

	Alternative Price Assumptions (per qq.)			
	<u>S/ 110</u>	<u>S/ 130</u>	<u>S/ 155</u>	<u>S/ 180</u>
A. Including Imputed costs of Family Labor				
Revenues	S/ 4,400	S/ 5,200	S/ 6,200	S/ 7,200
Costs	<u>4,520</u>	<u>4,520</u>	<u>4,520</u>	<u>4,520</u>
Net Income	- 120	S/ 680	S/ 1,680	S/ 2,680
B. Excluding Imputed costs of Family Labor				
Revenues	S/ 4,400	S/ 5,200	S/ 6,200	S/ 7,200
Costs	<u>4,060</u>	<u>4,060</u>	<u>4,060</u>	<u>4,060</u>
Net Income	S/ 340	S/ 1,140	S/ 2,140	S/ 3,140

PER-HECTARE COSTS OF COMMERCIAL RICE FARMING
UNDER SEMI-MECHANIZED METHODS OF PRODUCTION

(Costs in Sucres)

Operations	Use of Vehicles & Machinery		Manpower						Materials		Total Cost	Cash Outlays 1/	
	Unit	Cost	Total		Family Labor		Hired Labor		Quantity	Cost			
			Days	Cost	Days	Cost	Days	Cost					
1. Clearing	1 hr.	100										100	100
2. Land Preparation	5.75hrs.	400										400	400
3. Seeding)												400	400
4. Fertilizer Applic.)	1 hr.	80	2	40	2	40				2qq.	400	400	400
5. Herbicides			2	60	1	30	1	30		2qq. 10-30-10	220	620	580
6. Weeding			14	280	7	140	7	140		4qq. Am. Sulf.	280	500	470
7. Pesticides-I&II			4	120	2	60	2	60		2gal.	440	280	140
8. Bird Control - I&II			10	200	5	100	5	100		2kg.	130	250	190
9. Harvesting			40	720	5	90	35	630			50	200	100
10. Transport	\$/ 5/qq.	200										770	680
11. Interest 2/												200	200
12. Contingencies 3/												260	260
13. Amortization of Land Purchase												180	180
Totals		<u>780</u>	<u>72</u>	<u>1,420</u>	<u>22</u>	<u>460</u>	<u>50</u>	<u>960</u>		<u>1,520</u>		<u>4,520</u>	<u>4,060</u>

1/ Excludes the value of family-labor inputs.

2/ Eight percent of the cash outlays for items 1-10 (rounded to the nearest ten sucres)

3/ Five percent of the cash outlays for items 1-11 (rounded to the nearest ten sucres)

COMMERCIAL RICE FARMING UNDER IRRIGATED AND MECHANIZED METHODS

OF PRODUCTION: PER-HECTARE COSTS, REVENUES, AND NET INCOME

(Based on an average yield of 70qq. of polished rice per hectare per crop; two crops annually)

	<u>Alternative Price Assumptions (per qq.)</u>		
	<u>S/ 130</u>	<u>S/ 155</u>	<u>S/ 180</u>
A. Including Imputed costs of Family Labor			
Revenues per crop	S/ 9,100	S/ 10,850	S/ 12,600
Costs per crop	<u>6,350</u>	<u>6,350</u>	<u>6,350</u>
Net Income per crop	S/ 2,750	S/ 4,500	S/ 6,250
B. Excluding Imputed Costs of Family Labor			
Revenues per crop	S/ 9,100	S/ 10,850	S/ 12,600
Costs per crop	<u>5,790</u>	<u>5,790</u>	<u>5,790</u>
Net Income per crop	S/ 3,310	S/ 5,060	S/ 6,810

AGRARIAN REFORM IN ECUADOR

Agrarian reform has ordinarily been considered an effort requiring expropriation of lands and massive government intervention in operations. The novelty of the approach taken in this project necessarily raises the question of why the traditional approach to land reform is not desirable. The answer in the case of Ecuador is rooted in the history of the GOE agrarian reform effort and its current political and administrative implications. To provide this background, we reproduce here an analysis written by Dr. Liss Lekis who evaluated the operations of AID under contract with the Mission in 1967 and 1968.

"Recognition of a pressing need for change in the structure of agrarian society and land ownership is relatively new in Ecuador. During the presidential elections of 1956, only one candidate spoke out for the need for agrarian reform. He was defeated. By 1960, however, the picture had changed, and during the campaign preceding the elections, every candidate loudly supported the concept of agrarian reform, although from several quite different points of view. Everyone appeared to agree that something should be done, and immediately, but there was little agreement as to what. Dr. Velasco Ibarra, elected President of Ecuador in 1960, immediately named a commission to study the problems of agrarian reform and prepare a draft of a law to submit to Congress. During the sessions of Congress in 1960, however, members were too occupied in attacking the previous regime to pass the law submitted. By 1961 hopes for passage of the law were frustrated by an antagonism between President Velasco and Congress which was resolved only when Velasco was forced out of office and replaced by Dr. Carlos Julio Arosemena. Various programs were presented to Dr. Arosemena, but no action was taken on any. Under heavy political pressure, Dr. Arosemena finally announced that a Law of Agrarian Reform would be established by Executive Decree previous to the session of Congress scheduled for August, 1963.

A Decree was prepared and was ready for the President's signature, but the coup carried out by the military in July, 1963, completely changed the prospects once more. The Military Junta that took power gave the unwillingness of the government of Arosemena to enact the necessary reforms as one of the reasons for this overthrow, and it was with the sponsorship of the Military dictatorship that the Law of Agrarian Reform was passed in July, 1964.

In general, there are two opposing points of view regarding agrarian reform. One represents the thesis upheld by the traditional forces

mainly made up of landlords. As could be expected, this theory is opposed to agrarian reform, or at least to a form which would result in a drastic reduction of the large land holdings. This group favors colonization as a solution to all the problems of land tenancy in Ecuador. Customary arguments to this effect include, 1) if large parts of well cultivated land are expropriated, production will immediately drop, 2) only a minority of rural inhabitants will benefit from agrarian reform at the expense of the great mass of urban dwellers who will have to pay for rural development and also suffer from higher food prices, 3) capital will no longer remain in the country and the index of investment will drop, and 4) colonization, not expropriation, should be given preference in any program because of its fewer political and economic disadvantages.

The other point of view is recognized as being "liberal". The progressive reason that the redistribution of lands will increase production, will improve local markets, will accelerate national growth, and generally improve the standard of living of the rural sector. In brief, this group claims that the land must produce all of which it is capable with the results of such production being divided equally among the factors of production.

Although these two groups are most vocal in their arguments, there is a third group, more to the center politically than either of the other two which takes the stand that expropriation of well cultivated lands would be a costly error resulting in a withdrawal of investment capital following by chaos. They reason that agrarian reform should refer only to the expropriation of lands left uncultivated in a program which would include improving facilities of agricultural credit and extension.

Unfortunately, the final Law of Agrarian Reform which was passed and turned over to IERAC (Instituto Ecuatoriano de Reforma Agraria y Colonizacion) for implementation and administration was influenced by all of these divergent and incompatible viewpoints and was, thus, satisfactory to no one.

Aims and Philosophy of IERAC 1964-1966

The implementation of agrarian reform, according to its interpretation by the first Board of Directors of IERAC, was planned around the achievement of both long and short range goals.

1. Long Range Goals:

a) Political. To change the power structure within the country and obtain a true democracy by levelling the present unequal social structure.

b) Social. To achieve social reform through social mobility aimed at destroying the rigid social stratification characteristic of Ecuador. It was considered that this process could only be carried out in an atmosphere of peace and tranquility that would promote the development of true democracy.

c) Economic. To develop a society in which economic development could be achieved. (This was not considered a possibility within the present structure.)

2. Short Range Goals:

a) To correct the present defects in the agrarian structure so as to transform society and thus prepare the country for political, social and economic development.

b) To change the base of society which at present is built upon exploited and underprivileged masses. Contemporary society was considered to have three primary defects:

- 1) Defects in the tenancy of the land,
- 2) Defects in the labor market,
- 3) Defects in the distribution of the land due to the prevalence of latifundia and minifundia.

As a result of these basic defects, other unfavorable factors effecting the prosperity and welfare of the country developed:

1. Low productivity of land and man,
2. Illiteracy,
3. Lack of industrial development,
4. Malnutrition,
5. Low index of economic growth.

To correct these conditions which came about as the result of and not the cause of the basic defects, it was considered essential that the entire structure of society be changed, a process which the XERAC Director felt deserved first priority in any effective reform program.

The term "precarious tenancy," was used to describe the conditions under which 260,000 people worked the land in the Sierra and included not only the huasipungueros, but six or seven other types of tenancy including share croppers, renters and all others dependent upon the good will of the landlord.

It was felt that if these form of tenancy and types of people could be eliminated or changed into something different, the basic faults of society listed above would also be eliminated.. It was not thought sufficient to change only one or two of the precarious tenancy forms; all elements of possible exploitation had to be removed.

The Directors of IERAC recognized the fallacy held by many critics of agrarian reform, that faults of tenancy and distribution of land could be corrected by simply expropriating the land and dividing it up. It was felt on the contrary that this action would achieve nothing so long as the present social institutions remained. Emphasis was placed on changing the status of the inhabitants rather than the distribution of the acreage, thus making the base of the problem human rather than one of land alone.

Under the Law of Agrarian Reform IERAC was justified in intervening in land holdings only for specific reasons:

1. For defect in tenancy,
2. For defect in land use,
3. For defects in land distribution (lands over a maximum size).

Although priority was given the reasons for intervention in the order listed, the Board of Directors in general felt that defective land distribution should rank above land use because of the greater ease in effecting corrections. Although it is easy to determine when land owned is greater than a maximum set by law, or when it is idle and uncultivated, it is not easy to determine to what extent cultivated land is badly cultivated. If there is any cultivation at all, there is always a point of disagreement as to whether the use of the land is bad, - or sufficiently bad to allow intervention and/or expropriated by IERAC.

In order to find land for persons suffering from any of the forms of exploitation the first consideration was the distribution of the land, and IERAC considered it essential to eventually expropriate large land holdings in order to achieve "integration" of the campesino.

Before expropriating private property as allowed under the Law of Agrarian Reform, however, full use was planned for the state owned haciendas operated by Asistencia Social (Public Welfare) which were scheduled to be turned over the IERAC for redistribution and resettlement. Although IERAC and Asistencia Social are both agencies of the GOE, they are both "autonomous," and the largest part of the annual budget of Asistencia Social for the haciendas, an arrangement which, in a sense, requires the government to repurchase its own property through IERAC.

The haciendas of Asistencia Social are, in general, operating under unfavorable conditions. All produce incomes far below their potential due to faulty rental contracts, poor choice of renters and a lack of technical efficiency which progressively destroying the value of the land. On the other hand, Asistencia Social renters receive a high income in proportion to their investment because of their indiscriminate exploitation of soils, a factor of not much concern to them because of the usual short term of the rental (eight years.) Living conditions and salaries among hacienda workers and huasipungueros previous to the establishment of IERAC were little, if any, higher than elsewhere in the Sierra, despite the fact that Asistencia Social is the official government welfare agency.

Neither the total extent (133,000 hectares), however, nor the potentially productive area (56,000 hectares) of the 77 haciendas of Asistencia Social were large enough to justify the hope that expropriation could end there. Even the complete redistribution of these land can have relatively little impact upon the 254,000 families living in conditions of "precarious tenancy." It was hoped, however, that a well planned and efficiency executed redistribution of these lands would serve as a model to give impetus to a gradual but decisive agrarian reform.

Actual redistribution of expropriate land was planned to be handled by awarding the land titles to cooperatives to be organized in all areas where the program was to be carried out. Opponents of agrarian reform used this feature of the plan as justification for accusing IERAC of being Communist dominated. IERAC insisted the reason for granting one title to a group of people was to reduce the costs of the program and benefit more individuals. It was also claimed that individual titles were not appropriate for huasipungueros as one of the primary objectives of the program was to form these people into a group or society, a goal most easily be accomplished through joint cultivation of the land. It was also pointed out that it would hardly be logical to expect people with a background of generations of submission to the patron, and with no opportunity to develop initiative and secure adequate educations, to change overnight into capable land managers. It was felt that through communal farming,

the huasipungueros could be more easily trained in modern farm methods, could learn cooperative management, could secure credit through their cooperative, and could eventually from their own agricultural corporations or companies, an achievement regarded as impossible with individual ownership.

The advantages of the cooperatives or agricultural associations (collective farming) include the benefits of cooperative marketing and purchasing, transforming the areas too small for individual holdings into collective farms of adequate size.

Faith in the efficiency of collective farming and cooperative action is based on the success of the Israeli models, and several of the personnel at IERAC had training in Israel. For those who claimed the system proposed by IERAC was based on Communism, it was answered that farm titles are made to the cooperative; they are not held as the property of the State.

A low rate of land utilization is a primary characteristic of latifundia just as over cultivation is of minifundia, but by pooling the human and material resources of a group provided with technical assistance and agricultural credit, it was hoped both conditions could be avoided.

IERAC's plans for collective farming did not eliminate private holdings in areas where this type of ownership is economically feasible as in colonization area, nor was colonization discouraged. Considering the realities in the Sierra, however, of too many people and too little land, cooperative holdings offer one of the few possible solutions to both the over-population and the under-production of the Sierra.

Even the collective farm with intense cultivation and increased production, however, cannot answer indefinitely the problem of a population rapidly outstripping its available material resources and food supply.

The new structure of society as envisioned by the original Board of Directors of IERAC would consist of three types of agriculturists:

- 1) Agricultural laborers: employed for salary and not owning land;
- 2) Empresas: large agricultural enterprises made up of groups of associates including some small, independent land owners;
- 3) Cooperative workers made up of former huasipungueros and others who received redistributed lands from the State (IERAC). These, because of communal ownership and collective farming would be in a position to compete effectively with the large empresas noted above.

Provided that agrarian reform could achieve these aims, Ecuador would then be provided with a society capable of making progress. The workers in a cooperative would be in a position to compete with the empresas on an equal basis, something that as individuals they could never do.

In addition to the cooperative type of organization, there would also be some "mixed type" tenancies consisting of individuals holding personal titles to parcels of land, but sharing other land, such as pasture, in common. IERAC admitted the need of empresas both for production and as sources of employment for the group of agricultural laborers. It was estimated that at best, land ownership could only be provided in the Sierra for 54,000 of the 254,000 families in need. With the withdrawal of the former group, however, from the labor market, it was thought that demand for labor should rise, and salaries and standards of living would automatically go up.

The catch in the above planning is that each step toward economic and social improvement depends upon the implementation of previous steps difficult to control. If industrial development does not increase at a rate much higher than that of the past few years, there will be no jobs for rural migrants to urban areas and if rural education is not improved, even a greatly increased industrial sector will not provide work for an illiterate and untrained labor force with nothing to recommend it except need. On paper, the theory looks infallible. That is, 1) the reorganization of agriculture into empresas and prosperous cooperatives would produce service industries and other occupations to serve the needs of a developed agricultural community (mechanics, stores, etc.), 2) increased income to cooperative members would result in greater industrial development to meet the new demand. The steps needed, however, to transform an uneducated subsistence farmer into a producer and a consumer are liable to be complicated, time consuming and costly.

After its reorganization, (from the Instituto de Colonizacion), IERAC set first priority on the abolishment of the status of huasipunguero. The Law of Agrarian Reform specific the liquidation of this form of tenancy within twenty months after its passage, and to a large extent, this provision has been carried out, the hacendado having been required to compensate huasipunguero according to the number of years of his service. Up to ten years service was rewarded with the ownership of the huasipungo (the small plot of land worked). For service beyond ten years the huasipunguero was entitled to cash compensation for days and hours worked, but only very rarely were records available to indicate the amount of compensation he should have received. Huasipungueros with less than ten years service were required to pay the difference between the value of

their service for the number of years they had worked and the ten years required to gain possession of the plot of land, where most had lived all their lives as had their parents and grandparents.

The average size of land awarded for ten years of service to the hacienda was approximately 2.8 hectares, rarely large enough to use the labor of a family, or productive enough to support its members even at a subsistence level. After liquidation of the huasipunguero status, the landowner (patron) no longer felt a paternal obligation to employ all those living on his property even at an average salary of S/6 -S/10 per day. He now can pick and choose his labor force, thus leaving many ex-huasipungue-ros far worse off than they were before when they could depend to some extent on the paternalistic attitude of many traditional landowners who might employ 200 to do the work of ten. IERAC is often accused of having caused this situation, whereas, in fact, they were only carrying out the requirements of the law which shortsightedly demanded "freeing" the huasipungue-ros from their state of peonage without considering what was to become of them after that.

A year and a half after the founding of the agrarian reform program the Military Junta fell and was replaced by representatives of the obligarchy, the bitterest opponents of agrarian reform. Immediately the budget of IERAC was cut to the point that over half its employees (most working in extension) had to be discharged, and the program reduced to a fraction of the original plans. The first Board of Directors of IERAC had recognized the need for education, extension, credit, and technical assistance if any from land distribution was to be effective in the Sierra. They also recognized a harder fact - that there were not a sufficient number of available productive or potentially productive acres to provide for 250,000 families even on a subsistence level. One answer to the problem lay in more intensive cultivation requiring research and above all, extension to inform the ex-huasipunguero or an owner of minifundia of new methods, new types of seeds, or other means by which he could increase the yield per acre of his land plot. Following the cut in the IERAC budget, (which has never been made up) extension on any large scale was impossible, as was agricultural credit, two of the basic assumptions of the original plan of action.

Colonization

The answer of the large land owner to the demand for agrarian reform was usually "colonization". The recent history of Latin America presents innumerable examples of colonization plans, most of them total failures, sometimes due to lack of funding, lack of resources, or lack of land productivity, but primarily to a poor choice of colonists and a failure

to anticipate the problems that would arise. There are two points of view regarding the best methods to make colonization work. The traditional point of view claims that colonization cannot be successful without ample advance planning in order to provide all the necessities of life and a basic culture, i.e., a rural school, a store, an agricultural extension agency, easy transport to market, etc., and insists that colonization plans provide all these items. The other viewpoint stresses the desirability of a plan similar to the Homestead Plan in the United States. That is, a claim could be made to empty, uncultivated lands owned by the State. If after five years of occupation, a house has been built, crops planted and success more or less assured, a clear title to the property would be awarded. The law in Ecuador does give squatters certain claims to property occupied over a period of time, and many renters or agricultural laborers who might have a subsequent claim to the land (SIC).

The Agrarian Reform and Colonization Law gives IERAC administrative responsibility over all state lands and all lands that revert to the State for whatever legal cause, including those left uncultivated for ten consecutive years. There being relatively few state owned lands in the Sierra, colonization was restricted to areas between the Sierra and the Coast, and the sparsely populated almost unknown Oriente. The area selected for the implementation of the first colonization plan was Santo Domingo de los Colorados, the site of the first unsuccessful Pilot Plan of Colonization.

Occupying this area were thousands of families living on land to which they held no legal title. IERAC undertook a program of legalization of titles for land squatters who had occupied the land for a minimum number of years, a situation known in Ecuador as "spontaneous colonization". The second responsibility of IERAC in the colonization program was the development of new lands for resettlement of excess population from other areas, a function that obviously required land survey, access roads, extension agricultural credit, and most of all, funds.

Experience thus far with colonization shows clearly that the problem of excess population in the Sierra will not be solved by colonization projects on the Pacific slopes. Most of the settlers of the area come from the Coastal provinces, and, although there is a significant seasonal migration from the Sierra to the Coast, it is composed mostly of males who work as agricultural laborers four or five months a year. If they remain, they leave a destitute family in the Sierra and are often accused of being a primary cause of delinquency and crime on the Coast.

Until the fall of the Military Junta and the subsequent cutting of IERAC funds, considerable progress had been made in the construction of access roads, in the building of an extension service, construction of rural schools and legalization of titles. In collaboration with the Banco de Fomento and using an IDB loan, an initial plan of supervised agricultural credit was worked out and implemented to the benefit of some 1000 colonists in the Santo Domingo area. Colonization projects were also planned and started on the east slopes of the Andes toward the Oriente which showed greater promise of attracting population from the Sierra.

During the first eighteen months of the IERAC program (1964-1966) 18,877 land titles were delivered to squatters with another 12,099 in process; in the colonization program (new settlers) 7,512 titles to 265,880 hectares were delivered and 8,068 were in process for an additional 254,620 hectares. In the Agrarian Reform program 132,761 hectares of land were distributed with 220,417 in process.

Achievements and Activities of IERAC

A. Agrarian Reform:

The first project of IERAC involved the "freeing" of the huasipungueros from their status of peonage. From the foundation of IERAC in 1964 to September, 1967 15,344 families made up of 76,720 individuals were relieved of their "precarious tenancy" and given legal possession of 46,500 hectares, an average of 3.0 hectares per family. In this process IERAC acted in conformity with requirements of the Law of Agrarian Reform which aimed at liquidating all forms of precarious tenancy by 1968. An additional 8,821 families benefitted to the extent of 36,727 hectares made possible by processes of expropriations (haciendas of Asistencia Social) and reversions of property.

From 1965-68 IERAC intervened in the distribution of private properties of 16,396 hectares at the request of the owners which are now occupied legally by 669 families.

Progress in reaching goals set for settlement of ex-huasipungueros on former haciendas of Asistencia Social was also indicated.

1) San Vicente de Pusir (Carchi): Through September 1967, 502 families received titles to pieces of land on the hacienda. Of this number, 154 are organized in four cooperatives controlling 3,600 hectares of land. Lack of funds, however, have so far presented completion of the anticipated works of infrastructure. Although cut down to a fraction of the original plan, a Community Center was built with the collaboration of the Mision Andina, studies were completed for four other such Centers on the hacienda; topographic measurements were taken of 5,000 hectares; a silo with a capacity of 120 metric tons was built; and some agricultural credit plan extension service made possible a 50% increase in production. With the cooperation of the Andean Mission, 30 housing units were improved and a school built, and with the assistance of the Ministry of Agriculture, a demonstration farm of 30 hectares was added. See Section on PL 480 Loans which notes a diversion of USAID funds destined for agricultural credit. (not reproduced in this Annex).

2) Hacienda Pasillo (Pichincha/Cotopaxi); The project emphasized works of infrastructure as a means of increase production and raise the standard of living of the ex-huasipungueros. During the first year of this project IERAC administered the hacienda. During the second year 80% of the cultivated land was turned over to the two cooperatives. During this time an intensive program of agricultural extension and cooperative promotion was carried on to prepare the former huasipungueros to take over both cultivation and administration. Two cooperatives were organized, Cooperativa Atahualpa with 228 members, and Cooperativa Simon Bolivar with about 30 members which received 1,779 and 221 hectares respectively.¹ The planning for the construction of a Community Center was completed. Within the cooperative organization a carpenter's shop, a barber, dressmaker and others are operated by members of the community. With the aid of the cooperative members, offices, laundries and communal baths were built and a cooperative store established. Credits to the campesinos consisted of machinery and animals, cattle, horses and hogs.

^{1/} Atahualpa members are all ex-juasipungueros. Coop. Simon Bolivar members are mestizos, former employees of the hacienda who do not want to belong to cooperative made up of "indigenas". This conflict between Indians and the slightly better educated mestizo who rejects the Indian culture and who has collaborated in the exploitation of a social group beneath his own is common everywhere in the Sierra.

- 3) Tenguel (Guayas). In 1964 IERAC bought the hacienda Tenguel from the United Fruit Co. for the sum of \$/ 3,940,000, and has since attempted to solve the many socio-economic problems of the heterogenous group of inhabitants. Emphasis was placed on cooperative development and through September 1967, 12 cooperatives with 580 members were organized and received 7,390 hectares of land out of a total of 16,000 on the hacienda. The first pilot plan of Agrarian Military Conscription was carried out; on this property with a company made up of 100 conscripts, all natives of the area. This plan (CAME) attempts to give military training to campesinos simultaneously with agricultural education and instruction in cooperative organization.
- 4) Guantug (Canar); The project is made up of five haciendas with a total extension of 30,000 hectares. Intervention was initiated at the beginning of 1967, and by the end of the year 9,252 hectares had been delivered to 322 families in seven cooperatives. Thirty families of ex-huasipungueros also received 600 hectares. The remainder is planned for distribution to families who have migrated to Canar for lack of agricultural work and reasons of demographic pressures. The beneficiaries of the project have cooperated in completing works such as access roads and wells. Each family will receive five hectares of agricultural land and thirty hectares of pasture which, in this area is considered a "family size farm".
- 5) Zula (Chimborazo): The property, formerly belonging to the Church consists of six sections with a total of about 16,000 hectares. Beneficiaries will be 237 families of ex-huasipungueros and other landless groups living in the area. The parcelization of the agricultural sector has begun and is estimated to be completed about the middle of 1968. Each family will receive eight hectares of agricultural land and ninety of pasture which is the family size unit in this area.
- 6) Hospital Catazo (adjacent to Zula): The 1,603 hectares of the property will be turned over to 57 families in 1968. Emphasis is planned to be given to cooperative organization and the efficient use of irrigation.
- 7) Colta Monjas (Chimborazo): The area of 3,300 hectares will benefit six groups of campesinos. Since intervention in 1966, 650 hectares of agricultural land have been distributed to 170 beneficiaries. Three hundred fifty hectares are destined for a reforestation project and another 2,700 will be used for communal pasture.

In order to solve the problem of minifundia in the Sierra, future plans of IERAC include programs of:

1) Social integration - Emphasis will be given to education, hygiene, sanitation etc. to awaken the campesino to a consciousness of his problems and those of the Nation. To achieve this goal the cooperation of agencies such as the Ministries of Education, Agriculture, Prevision Social, and Health, the Misión Andina, OIT, and FAO were regarded as essential.

2) Economic integration - Means by which human and material resources can best be used to increase agricultural production, raise the rural standard of living, and improve the economy of the country are the goals of this phase of the program.

In 1968 a regional development plan is to be effected in the area around Cayambe (Heda. Pesillo) in which IERAC plans to place 1000 families on seven haciendas of Asistencia Social with an area of 10,000 hectares. It is hoped that the project will have a national impact which will facilitate similar programs in the future.

B. Colonization

The area of concentration chosen for the first colonization project was Santo Domingo de los Colorados, a center of migration from both Coast and the Sierra. The conomic prospects of this region have been greatly enhanced with the construction of roads to Guayaquil and Quito and those currently under construction linking Santo Domingo-Chone-Bahía and Santo Domingo-Esmeraldas. To develop the area, however, required financing for access roads, surveying and subdividing lots, development of all types of infrastructure, and building of schools as well as aiding in the organization of marketing and production cooperatives, and planning and implementing a program of supervised agricultural credit.

The International Development Bank authorized a loan of \$2,600,000 to IERAC in February, 1964 to aid in the financing of the plan for spontaneous colonization in Santo Domingo. Funds were to be used to complete construction of access roads, install three community centers, build and equip 20 schools, provide agricultural and housing credit and a broad extension program to an area of about 17000 km² occupied in 1964 by 1,600 families.

A report of the activities of IERAC published in El Comercio, January 4, 1968 claimed that from the foundation of the institution in 1964 until September, 1967, 230,820 hectares of land had been surveyed and legalized in favor of 6,400 families. From January to September 1967, 1,008 families received titles to 39,600 hectares of land. It was pointed out that the cut in funds made in 1966 was reflected in the deaccelerated rate of the legalization of land and titles program. The report also noted that the original project of assistance to spontaneous colonization in Santo Domingo contemplated settling 1,600 families on 170,000 hectares. Despite financial problems, however, the project developing the colonization plan in Santo Domingo, 194.5 kilometers of access roads were built, 14.5 more than were included in the original plan, and thirty four schools were completed, 14 more than had been projected. Agricultural credit anticipated to be S/. 25,640,900 exceeded that figure by S/ 1,552,840 for a total of S/. 27,193,740 (\$1,495,805). 1/

Much, however, remains to be done.

Plans were also made for colonization in other areas in addition to Santo Domingo.

1) Valley of the Upono River: This project is considered "in progress" with the financial participation of the IDB and the cooperation of the Centro de Reconversion del Austro in Cuenca and aimed at settling 15,000 families on 268,000 hectares of underdeveloped land in the Oriente.

2) Valley of the Nangaritzza River: This project is still in an advanced "being studied" stage, but was planned for the settlement of 1,500 families on 100,000 hectares. It was hoped that the work on the project could begin in 1968.

3) Being studies:

- a) Valle de Arapicos, Chiguaza, Yacuiipa (Oriente) 200,000 hectares.
- b) Zona Coca, Aguarico, 500,000 has. (Oriente)
- c) Carretera Puerto Ila/Bahia, 150,000 hectares (Coast)
- d) Triangle between Guayllabamba and Blanco Rivers 100,000 hectares.

1/ See "Families Receiving Agricultural Credit", in Analysis of Recommendations on the Agrarian Reform Program in Ecuador. USAID/1966

C. Centro de Investigaciones y Enseñanza en Reforma Agraria

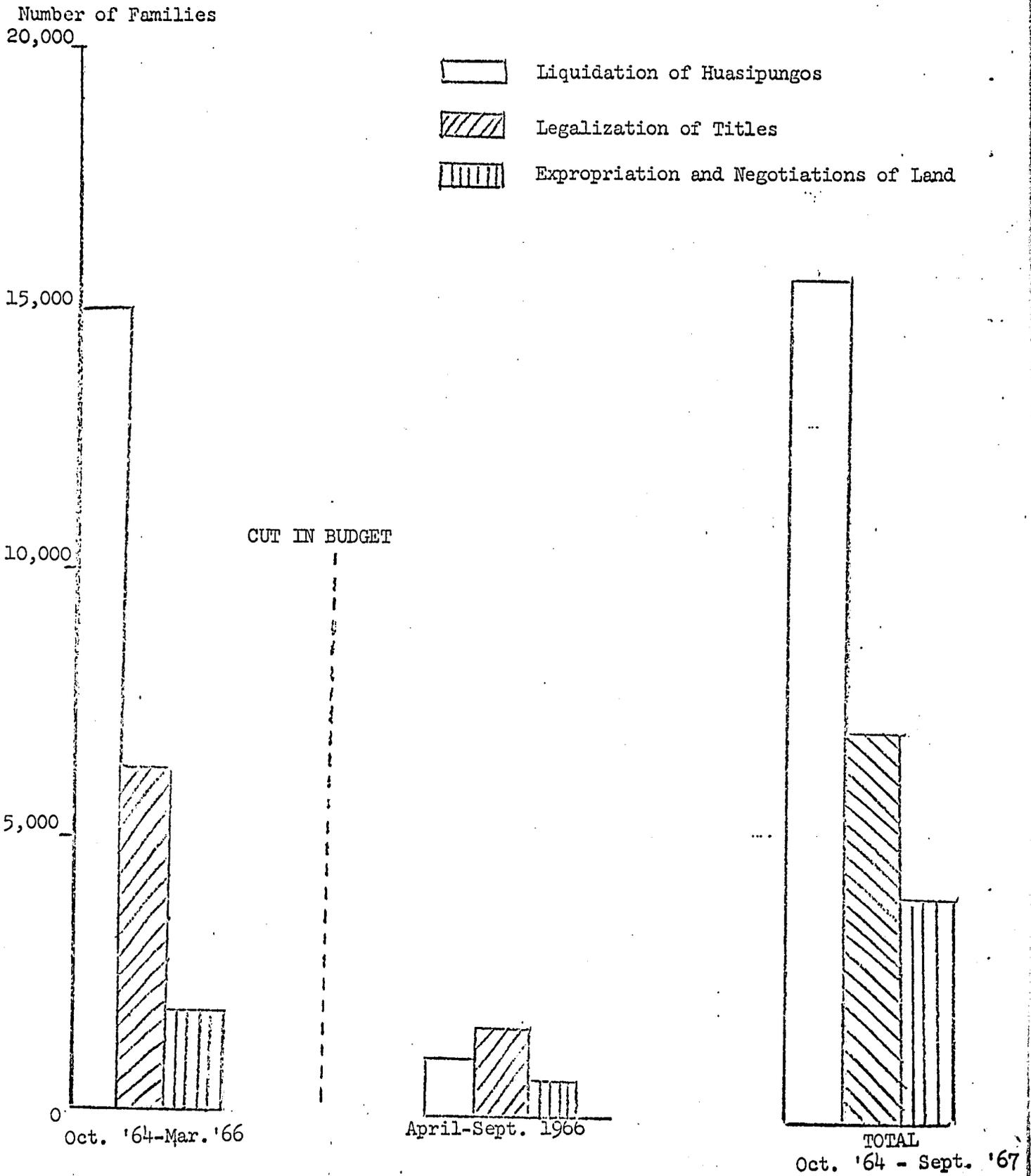
The Center was founded in December, 1966 to train executives and technicians working in the field of agrarian reform. In its first year of operation, six courses, having an average duration of three weeks, were given to 291 participants in five cities in Ecuador. In cooperation with IERAC, the Institute organizes six other courses in various zones of the country which were attended by 167 persons. \$165,000 in PL 480 funds were used in the development of the Center, the activities of which, however, have been restricted because of political pressure, with emphasis at present being given to "rural development" rather than the hated (by the oligarchy) agrarian reform.

As a means to explain the need for agrarian reform and colonization to all sectors of the public, IERAC published 16 books or pamphlets during 1967.

V. Problems and Criticism of IERAC

IERAC's principal problem from the beginning was lack of financing as provided by the Law of Agrarian Reform. In 1965, the first year of operation, IERAC was assigned 15.9 million sucres from the national budget or about 1/2 of what had been approved and anticipated. This was supplemented with 4.6 million sucres as IERAC's share of taxes, 10.6 million earned income from haciendas administered by the institution, and 2.3 million from other Ministries with which agreements has been signed. In addition IERAC used 10.4 million from the IDB loan for colonization and 6.1 million of USAID PL 480 funds, a total for 1965 of 49.9 million or about equal to the \$ 50,000,000 annual figure set in the law. With the fall of the Military Junta, however, in March, 1966 IERAC was the first agency to have its funds drastically cut, and since then has never received sufficient income to carry out the plans and projects made so optimistically in 1964 (see Graph).

IERAC PROJECTS BY NUMBER OF FAMILIES BENEFITED



At the time of the USAID evaluation of IERCA in September 1966, the agency was struggling to meet its program commitments with limited funds. The accomplishments of the program in its first eighteen months, however, and the dedication of its director and personnel were remarkable, and continued USAID support to IERAC, at least in the form of PL 480 funds, was recommended. Only a few weeks after the evaluation was completed, the government changed, and in the light of the new political situation, the Director of IERAC resigned. His assistant, who succeeded him as Director, was forced out after a very short time, and the purpose and direction that had characterized IERAC became weaker and weaker as opposition to the program of agrarian reform strengthened.

Publicity regularly appears in the press announcing IERAC's "granting of titles" or "legalizing land tenancy," but as compared with the first year's accomplishments, these seem small and stopgap.

In January, 1968 a statement was published as the result of a conference of Ecuadorean sociologists, which claimed that agrarian reform had been a fraud and a deception, because in its three years of operation only 3% of the properties larger than 500 hectares in size had been affected, and concluded that, therefore, latifundia remained intact with little change.

The report noted further that even though the degrading status of "precaria" and peonage as exemplified by the huasipunguero had legally been abolished, the relationship of man to the land has not improved. Instead, additional social and economic problems had been created, the most serious being the inability of the ex-huasipunguero to survive on the produce of his plot of land and the extreme difficulty of finding outside employment.

The only authentic reform that could be noted after three years was in the resettlement of the ex-huasipungueros and other marginal farmers on haciendas expropriated from Asistencia Social, and even on these, the complementary programs and works planned could not be financed.

Some superficial changes have been made which, although not satisfying even minimum aspiration for moderate reform, have avoided the basic problem of the need for a dramatic structural social change. The adherents of agrarian reform claim that "real" reform must include, 1) the expropriation of unused, badly cultivated, or oversized land holdings, and 2) the provision of complementary resources to achieve a

genuine land revolution not to be confused with rural development, colonization or agricultural improvement. It is argued that this revolution must be massive, rapid, and radical, capable of destroying simultaneously latifundia and the class of latifundistas, and breaking the vicious circle that props up the present decadent agricultural structure and political power.

Only with a revolution of this kind is it thought possible to end the conditions of latifundia and minifundia which have produced fatal consequences in the form of, 1) economic stagnation, 2) social rigidity perpetuating class divisions, and 3) illiteracy, unemployment, malnutrition, and misery.

Technical assistance is admitted to be essential to a successful change in land tenancy and social structure, but agricultural credit, housing, education and infrastructure as well as campesino organization must also be provided for agrarian reform to succeed.

The claim of the Sierra landowners that there is not sufficient land in the Sierra left to implement agrarian reform is countered by pointing out the number of hectares of uncultivated or badly used land characteristic of the large haciendas, the number of properties exceeding in size any reasonable limits, and the number of hectares owned by the State, the Church, banks and schools, or, that is, belonging to institutions which have nothing to do with developing agriculture.

Liberals claim that the State has the obligation to take the necessary steps to end an unjust and irrational situation as do the governing classes upon whom the ultimate solution depends, if the consequences of a crushing process are to be avoided.

Attention is often called to the minimum effectivity of IERAC, by pointing out the limited number of changes effected in three years.

Lands Expropriated or Intervened by IERAC, 1964-1967

Owner	Number of Holdings	Size	Number of Families Benefited
State	13	52,912	3,410
Church	2	68,000	1,660
Private	24	106,773	6,722
TOTAL	39	227,685	11,792

Of these 39 properties,

22 out of 24 held privately were over 500 hectares in size,

2 out of 2 church properties were over 500 hectares in size,

9 out of 13 State owned properties were over 500 hectares in size.

Thirty-three properties out of a total of 1,369 over 500 hectares in size were expropriated or intervened representing only 2.4% of all properties of that size. This, it is stated, is not agrarian reform.

Not only the sociologists have attacked the agrarian reform program. A statement published in El Comercio January 6, 1968, and attributed to the Christian Democratic Party, commented:

"It is a fact that while the problems multiply and it becomes more vital to integrate the minifundias and destroy the latifundias, the advisors of the Ministry of Agriculture (IERAC) occupy themselves with transforming agrarian reform into colonization toward the Coast and the Oriente in violation of the aim of the Development Plan which placed a priority on remedying the underdevelopment of the inter-Andean Sierra."

Other published criticism come from the Camara de Agricultura (representing the large landowners). 1/

1/ El Comercio, November 25, 1967

"The prolific programs of agricultural education detailed in the General Development Plan have not been carried out, (By IERAC)"....."and the majority of landowners have NEVER received a visit from a technician nor had the benefit of his advice."

Many more examples could be cited, but it is sufficient to say that during its lifetime, IERAC has been battered by criticisms of all kinds from all directions. Primarily, however, operation of the institution have been threatened from two directions, first from the large land holders who, although they hesitate to condemn the concept of land reform, refuse to apply it to themselves and accuse IERAC of being "Communitistic" in its program. Secondly, IERAC is under attack from extremist groups led by the Communists who claim the organization is a "tool of the oligarchy and the latifundistas." It can hardly be both.

Since his selection as interim-President, President Arosemena has consistently avoided the issue of agrarian reform, preferring to follow the line of the oligarchy and talk about "spontaneous colonization" instead. On March 12, however, the President met with the Directors of IERAC, and surprisingly accused them of impeding agrarian reform, basing his statements on claims presented to him by the member of the Board representing the Federation of Indians, a Communist dominated group. The complaints were little more than a resume of the same recurrent problems, and there seemed little point in taking them to the President for his personal intervention, particularly as they could have been discussed in regular Board meetings.

In President Arosemena's statement to the press, he expressed his opposition to anything which hinders just land distribution, explaining that his party supports agrarian reform as an "imperative of civilization both for social justice and to avoid social upheavals," thus reversing many of his statements made in the past.

The same day that President Arosemena made his accusations against the management of IERAC, a new IDB loan to IERAC in the amount of \$3,000,000 was announced which was specified to "finance the program of resettlement on Haciendas San Vicente de Pusir, Pasillo, and Tenguel. Actually, IDB representatives informed USAID that this statement was in error and that none of the funds would go to Tenguel which has received a private loan, and that IDB money would be used to expropriate and develop other Asistencia haciendas as well as continue work on the old projects.

Following the President's accusations, there ensued a chain of charges and counter charges involving most of the personnel of IERAC, the Director of the Department of Agrarian Reform, who had been singled out for Presidential criticism, defending himself in the columns of the newspapers three separate times.

The Comercio, in an editorial a few days later, criticized the IERAC Directors of "buck passing" and trying to sidestep agrarian reform, and termed them "indifferent and lacking in dynamism," accusing them of having paralyzed the program.

Despite the Agrarian Reform Director's defense of himself and his policies in the face of President Arosemena's criticism, the Board of Directors of IERAC announced on April 17, 1968 that he had been removed from his position along with the Program Director, both of whom blamed their dismissal on the President's failure to support agrarian reform, and the machinations of the Federation of Indians (FEI) Representative on the Board, an effective squeeze carried out by the extreme leftists and the conservative landowners, groups which, although acting from different motives, are determined to paralyze and destroy the agrarian reform movement.

On May 30, 1968, the organization of employees of IERAC made a direct appeal to the President that the members of the Board of Directors be requested to resign, asking at the same time for an official evaluation of IERAC and the stabilization of the economic situation of the institution. The Director of IERAC was accused of negligence and of having allowed the assets of IERAC to be attached as the result of a legal battle over the price of an expropriated hacienda. The petition added that "agrarian reform has been paralyzed since the present executives were appointed to office." In the IERAC Board meeting which followed, the FEI representative was quick to side with the employees, saying that "IERAC must be an institution dedicated to social transformation and renovation rather than a bureaucratic and political apparatus."

By June 4, 1968 the resignations of the Director was accepted and the resignation of the Director of the Department of Colonization was announced by the press, which, combined with the earlier departures of the Director of the Department of Agrarian Reform and the Program Director left IERAC practically without a Board of Directors. (It is said, however, that the

UNCLASSIFIED

ANNEX VII, Page 22 of 22

Director of Colonization refused to resign and his pictures are still appearing in newspapers as Board member). One of the few who survived the power struggle of the last few months, however, was the Communist representative of FEI who now finds himself in an extremely strong position.

Since the completion of Dr. Lekis' report the situation of IERAC has continued to deteriorate. In order to avoid taking a stand on politically sensitive issues, various members of the Board of Directors refused to attend official sessions. Lack of financial support brought most field activities to a complete standstill. With all these uncertainties, the better trained and more effective personnel have left the Institute, causing further demoralization.

One current plan calls for the incorporation of IERAC into the Ministry of Agriculture. However, as of this date no definite action has been taken. Judging by the past, even after a firm decision is made it will be months before financing and staff is available.

When and if IERAC in its present or future incarnation shows signs of being able to handle its responsibilities AID's position vis-a-vis that organization should be reevaluated. In this connection, the involvement of IERAC in the proposed project might be considered. For now, the facts suggest that the proposed project should be carried on independently.

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DRAFT LOAN AUTHORIZATION

Provided from: Alliance for Progress Loan Funds
ECUADOR: Land Sale Guaranty

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 (the "Loan") pursuant to Part I Chapter 2, Title VI, Alliance for Progress, to the Government of Ecuador ("Borrower") of not to exceed three million six hundred thousand United States dollars (\$3,600,000) to assist in financing the sale of agricultural land to campesinos and the extension of production credit thereto, the Loan to be subject to the following terms and conditions:

1. Interest and Terms of Repayment: Borrower shall repay the Loan to the Agency for International Development ("A.I.D.") in United States dollars within forty (40) years from the first disbursement under the Loan, including a grace period of not to exceed ten (10) years. The Borrower shall pay to A.I.D. in United States dollars on the disbursed balance on the Loan interest of two (2) percent per annum during the grace period and three (3) percent per annum thereafter.
2. Other Terms and Conditions:
 - (a) Equipment, materials and services financed under the Loan shall have their origin in and be procured from the United States of America or Ecuador. Shipping financed under the Loan shall be procured from the United States, and marine insurance financed under the Loan shall be placed in the United States with a company authorized to do a marine insurance business in any state of the United States.
 - (b) United States dollars utilized under the Loan to finance local currency shall be made available to Borrower or its designee through Special Letters of Credit and shall be used only for procurement in the United States of equipment, materials and services.

- (c) This authorization will terminate six months after the date of approval if by that time the Borrower has not signed a loan agreement reflecting the project substantially as described in the Capital Assistance Paper.
- (d) The Loan shall be subject to such other terms and conditions as A.I.D. may deem advisable.

Depp

Deputy U.S. Coordinator

(Date)