

5190094

5190094-②

CAPITAL AMBASSADOR

5190094

Proposed and Recommended
For the Review of the
Development Bank Committee

EL SALVADOR: RURAL UNION DEVELOPMENT (FEDECACES)

By David
Development

ROOM 1538 EB

AID-ILG/P-890

LA/SP

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

UNCLASSIFIED

AID-DLC/P-890
May 15, 1970

MEMORANDUM FOR THE DEVELOPMENT LOAN COMMITTEE

SUBJECT: El Salvador: Credit Union Development (FEDECACES)

Attached for your review are the recommendations for authorization of a loan in an amount not to exceed \$2,000,000 to the Federacion de Cooperativas de Ahorro y Credito de El Salvador, "Fedecaces," to assist in financing local currency costs of subloans by Fedecaces to member credit unions and thereby to assist in the development of a self-sustaining private cooperative federation.

Please advise us as early as possible but in no event later than close of business on Tuesday, May 26, 1970, if you have a basic policy issue arising out of this proposal.

Rachel C. Rogers
Secretary
Development Loan Committee

Attachments:

Summary and Recommendations
Project Analysis
ANNEXES I-IV

UNCLASSIFIED

UNCLASSIFIED

AID-DLC/P-890

EL SALVADOR

May 15, 1970

CREDIT UNION DEVELOPMENT (FEDECACES)

<u>Table of Contents</u>	<u>Page</u>
SUMMARY AND RECOMMENDATIONS	i
SECTION I - NATURE OF THE PROJECT	1
A. DESCRIPTION OF ACTIVITIES	1
1. Project Definition	1
2. A. I. D. Financing	2
3. Operation of Fedecaces	3
B. BACKGROUND OF PROJECT	8
1. The Cooperative Movement in El Salvador	8
2. Genesis of the Project	10
3. Other Sources of Funds	10
C. PROJECT JUSTIFICATION/RATIONALE	11
1. Relationship to CASP	11
2. Relationship to ES ¹ Credit System	11
3. Contribution to ES ¹ Economic Development	14
4. Debt Service Capacity of ES	15
5. Impact on U. S. Economy	15
6. Title IX - Building of Democratic Institutions	15
7. Consistency with CIAP Reviews	16
8. Certification of USAID Director	16
SECTION II - PROJECT ANALYSIS	17
A. Borrower	17
B. Economic and Social Evaluation	18
1. Demand	18
2. Economic Impact	18
3. Social Evaluation	19
C. Financial Analysis	20
1. Fedecaces Operating Situation	20
2. Comparative Balances	20
3. Loans Made by Fedecaces	21

UNCLASSIFIED

UNCLASSIFIED

4. A.I.D.'s Contribution to Fedecaces	22
5. Terms of the Loan	24
6. Justification of Loan Terms	24
7. Alternative Sources of Funds	25
8. Prospects of Repayment	25
SECTION III - LOAN ADMINISTRATION	26
Implementation Plan	26
Conditions and Covenants	27
Two-step Option	31
SECTION IV - ISSUES	32
<u>ANNEXES</u>	
ANNEX I	
EXHIBIT	
A. CAEC Approval of IRR	
B. USAID Director's Certification	
ANNEX II - PROJECT DETAIL	
EXHIBIT	
A. Borrower's Application	
B. Survey of Fedecaces Credit Union System	
C. Map - Locations of Fedecaces Credit Unions	
D. Financial Data	
E. EXIM, IDB, and IBRD letters expressing no interest.	
F. Letter of Support to Fedecaces by GOES.	
G. Letters from Central Bank on line of credit.	
H. Salvadoran Agricultural Credit System	
ANNEX III - STATUTORY CRITERIA	
ANNEX IV - LOAN AUTHORIZATION (Draft)	

UNCLASSIFIED

UNCLASSIFIED

SUPPLEMENTS (See Official Files)

1. Law of Cooperatives and Law creating Salvadoran Institute for Cooperative Development (English and Spanish)
2. Statutes of Fedecaces (Spanish)
3. Model Statutes for Salvadoran Credit Union (Spanish).
4. Analysis of Fedecaces (Spanish)
5. Survey of Credit Union Demand (Spanish)
6. Credit Regulations of Fedecaces (Spanish)

UNCLASSIFIED

**EL SALVADOR
CREDIT UNION DEVELOPMENT**

SUMMARY AND RECOMMENDATIONS

1. **BORROWER:** The Federación de Cooperativas de Ahorro y Crédito de El Salvador (FEDECACES) is a private non-profit national federation of 78 affiliated credit unions with a total membership of over 10,000. It is chartered by the Ministry of Interior, and operates under the Commercial Code of El Salvador. (The first cooperatives law was passed in November, 1969 and Fedecaces will be governed thereby when the law becomes operative.) The offices of Fedecaces are located in San Salvador and the member credit unions are located in urban and rural areas throughout El Salvador. An acceptable application dated February 16, 1970, has been received from Borrower. (Annex II, Exhibit A)

2. **REPAYMENT PROSPECTS:** The loan will not be guaranteed. It will be backed by the full faith and integrity of Fedecaces, the 78-member credit unions and the present membership of 10,000 Salvadorans. This moral obligation will be formalized through resolutions passed by the respective governing bodies of Fedecaces and the member credit unions. Credit union lending cumulatively amounted to \$244 million dollars in the credit unions in 12 Latin American countries as of December 31, 1969. Spot checks in several Latin American countries indicate a delinquency rate within 5 percent and a write-off rate within 1 percent, the latter amply covered by established reserves. The A.I.D. loan will be drawn down by Fedecaces on the ratio of 1½ to 1, A.I.D. loan paid-in share capital in Fedecaces and member credit unions, providing a reasonably good debt-equity ratio in the total system. The net worth of Fedecaces was \$53,200 (equivalent) on 31 December 1969. A forced capitalization plan requires that 10 percent of all sub-loans be invested in share capital of Fedecaces thereby rapidly increasing the equity of the Borrower to a projected \$1 million by 1975. Maintenance of value risk will be covered by Fedecaces by establishing a reserve of up to \$100,000 equivalent or 5% of the A.I.D. loan. The m.o.v. reserve will be created by reserving an amount equivalent to one-half of one percent of outstanding sub-loan balances at the end of each calendar year (from all sources of funds) until the total of such reserves reaches \$100,000 equivalent. Convertibility of local currency to dollars is assured under the Law of International Transfers. The required authorization of the Ministry of Economy and the subsequent registration of the A.I.D. loan with the Central Bank to assure convertibility would be a condition precedent to any disbursement of A.I.D. loan funds.

2. **LOAN:** The proposed loan is not to exceed \$2,000,000, all or virtually all for local currency expenditures. It will be repaid in dollars over a 25-year term, including a grace period of seven years. Interest during the grace period will be two percent (2%) per annum and three percent (3%) thereafter. The "two-step" procedure will be offered to the GOES on an optional basis, with the condition that GOES guarantee repayment of the loan.

4. Total Contributions or Loan Funds in Total System (Fedecaces plus Credit Unions)

	<u>1970</u>	<u>%</u>	<u>1973</u>	<u>%</u>
A.I.D.	\$ 0	0.0	\$ 2,000.0	35.3
Fedecaces	\$ 32.0	3.7	\$ 212.5	3.8
Credit Unions	\$ 617.2	71.4	\$ 2,228.0	39.3
BCR	\$ 200.0	23.1	\$ 1,225.8	21.6
Other	\$ 15.9	1.8	-	0.0
	\$ 865.1	100.0	\$ 5,666.3	100.0

The above growth in contributions by the various parties reflects the catalytic effect of the A.I.D. loan over the three year disbursement period, 1971-3. Due to this accelerated growth, caused essentially by the A.I.D. loan plus T.A. inputs, it is expected that Fedecaces will be able to achieve a self-sustaining level by 1975. (see Annex II-D for financial data).

5. DESCRIPTION OF THE PROJECT: The proposed loan would assist in financing sub-loans from Fedecaces to the member credit unions, for the following purposes:
- (a) Relending for fixed and working capital loans to small farmers, artisans, small industries and small commercial enterprises.
 - (b) Relending for personal loans to refinance usurer debts, purchase household and personal effects, purchase medical-dental services, pay for educational expenses and other personal expenses.
 - (c) To finance improvements in the offices, office equipment and management of the credit unions themselves.
- A. I. D. loan funds will be made available to the "Borrower" on a pari passu basis of $1\frac{1}{2}$ to 1; i. e. one and a half units of loan funds to one unit of paid in share capital in Fedecaces and member credit unions.
6. PURPOSE: This loan project pursues several objectives and will:

UNCLASSIFIED

(a) Address the aims of Title IX of the FAA by involving large numbers of persons in the development, organization and administration of free voluntary private associations. EX

(b) Provide seed-capital to accelerate the development and reorientation of an existing private federation of credit unions and assist it to become self-sustaining. XXXX

(c) Make credit available to thousands of people who have no access to credit under present conditions, with particular emphasis on the rural area.

(d) Establish a system for the formation of capital not presently being marshalled which in time could significantly add to and complement present credit resources.

7. OTHER SOURCES OF FUNDS: By communications dated December 2, 1969, January 6, 1970 and December 11, 1969, the World Bank, the IDB and the Export-Import Bank respectively indicated no interest in financing this loan. (See Annex II, Exhibit E). In substance these international agencies are not interested in providing concessional local currency seed-capital loans for credit union development in El Salvador and/or such financing is not in accord with their objectives. //

In general other external free world sources would not be interested in providing the required financing for the same reasons as stated above plus the additional fact that such financing would not meet the risk or income criteria of private banking. In 1969 Borrower secured lines of credit, at 9% interest per annum, in kind, from commercial houses in the amount of approximately \$60,000. In October of 1969 the Central Bank of El Salvador approved a one-year line of credit in the amount of \$200,000 at 2% per annum which is legally tied to relending for "Productive Purposes"; i. e. for loans to small agricultural and industrial enterprises. The Central Bank has indicated that it would be willing to expand this line of credit once the Fedecaces system demonstrates its ability to effectively use such credits. (See Annex II, Exhibit G, letters from Central Bank.) //

In addition to the domestic resources available to Fedecaces an AID concessional loan is needed to provide the volume, flexibility and margins required to fulfill the purposes set forth in 6 above. Section II-D of the CAP provides the supporting financial analyses and rationale.

8. STATUTORY CRITERIA: All statutory criteria have been met as shown in Annex III.
9. VIEWS OF MISSION: The Mission strongly supports credit union development as an important vehicle for achieving mission objectives related to the political socio-economic development of low income groups in El Salvador, especially in the rural area. The credit union movement has been promoted and assisted by USAID since 1964. The system has been delivering extremely limited amounts of credit to people who ordinarily do not have access to financing on reasonable terms from other sources. As a Title IX activity the credit union movement contributes effectively to the development of free democratic institutions. Therefore the Mission considers this loan a priority element in support of USG objectives in El Salvador and recommends approval of the proposed loan.
10. VIEWS OF THE GOES: The National Planning Council, the President of El Salvador, the President of the Central Bank and other agencies of the GOES have expressed their support of the Fedecaces system and assign a high priority to the continued expansion of the system. See Annex II, Exhibit F for views of the GOES.
11. ISSUES: All issues have been satisfactorily resolved during intensive review but local cost financing. All of the loan proceeds, with the possible exception of dollar technical assistance contracts in the maximum amount of \$100,000, would be used for local currency financing to provide small sub-sub-loans of an average \$200. It is estimated that Fedecaces and its member credit unions will disburse approximately \$12.1 million equivalent in sub-loans (from new capital sources and rollover funds) during the three-year disbursement period of the loan, and that 7% of these disbursements (\$840,000) equivalent will be used for off-the-shelf purchases of U. S. goods. This represents the equivalent of 42% of the \$2.0 million A. J. D. loan. Within less than ten years from the time the A. J. D. loan is operational, it is estimated that off-the-shelf purchases of U. S. goods caused by the project will exceed the amount of the loan. This will produce a positive effect on the U. S. balance of payments in the medium run. There are no U. S. G. owned local currency funds available for this loan project.

12. Loan Administration: All disbursements would be for local cost expenditures with minor exceptions. U.S. Dollars will be converted to local currency made available to the Borrower by a method acceptable to A.I.D. and Borrower.

Dollar expenditures, if any, would be made by a method agreed upon in writing by A. I. D. and Borrower; i. e. reimbursement, direct payment, letter of commitment; letter of credit, or other mutually acceptable method.

Procurement would be managed by the sub-sub-borrower, the very small entrepreneur, who would generally buy small quantities of commodities off the shelf.

13. RECOMMENDATIONS: On the basis of Intensive Review of the Project the Capital Assistance Committee concludes that the project is technically, economically and financially justified, it is recommended that a loan to Fedecaces for an amount not to exceed \$2,000,000 be authorized subject to the following terms and conditions:

(a) All loan funds will be authorized for local currency expenditures.

(b) Repayment will be over a twenty-five year period, including a seven year grace period. Interest during the grace period will be two per cent (2%) per annum and three per cent (3%) per annum thereafter.

(c) The GOES will be offered the two-step procedure as an option, on the condition that the GOES guarantees the full amount of the A.I.D. loan.

(d) Interest and principal payments will be made in U.S. dollars.

(e) Prior to any disbursements, FEDECACES and its member credit unions will individually pass resolutions, in form and substance satisfactory to AID, backing this loan with the full faith and integrity of the credit union system and attesting to the moral obligation to repay the loan.

(f) Source and origin of procurement would be largely El Salvador in off the shelf items, although some external procurement is conceivable and will be limited to the United States or independent countries of the Western Hemisphere south of the United States (except Cuba).

(g) Prior to any disbursement of loan funds Fedecaces will assure the convertibility of local currency to U. S. dollars and set up a reserve for the maintenance of the value of dollar loan funds in form and substance satisfactory to A. L. D.

(h) A. L. D. loan funds will be made available on a pari passu basis of one and a half ($1\frac{1}{2}$) of loan funds to one (1) of paid in share capital in Fedecaces and its member credit unions.

(i) Borrower will covenant that it and A. L. D. would carry out progress reviews as deemed appropriate by either party and that Borrower will take remedial action as appropriate.

(j) The loan authorization will include a statement to the effect that the loan will be subject to such other terms and conditions as A. L. D. may deem advisable.

PROJECT COMMITTEE:

Capital Resources Development Officers	:K. Davidson, AID/W LA/DR :T. T. Foley, USAID/ES
Financial Analyst	:A. Castro, CUNA/LARO
Credit Union Consultant	:P. Pérez G., CUNA
Credit Union Specialist	:N. Alvarez, CUNA
Special Advisor	:T. Dickey, PCV/ES
Program Officer	:R. Witherell, USAID/ES
Economist	:J. Ferch, U. S. Embassy/ES
Counsel	:Kent Knowles, ROCAP/G

Drafting Officers: Davidson/Foley

May 15, 1970

SECTION I. NATURE OF THE PROJECTA. DESCRIPTION OF ACTIVITIES1. Project Definition

The Borrower (Fedecaces) is a Federation with 78 affiliated credit unions having a total membership of over 10,000. Fedecaces is located in San Salvador and its members are located throughout the country as shown by the map in Annex II, Exhibit C. By assisting the system to consolidate its growth to date, provide for future expansion and develop a self-sustaining organization, the project will pursue several purposes.

Project activities will involve thousands of people, voluntarily associated in credit unions, in the democratic processes of organizing and managing these private enterprises. Overall individual political socio-economic development will be enhanced and some movement from the rigid traditional paternalistic patron framework of dependency towards a more independent, democratic and individually responsible framework can be expected.

Thousands of people will have access to credit. Credit union services will provide escape from usurer's rates, which in a few cases run as high as 20% per day, make better and more effective use of available personal resources, and a relatively better standard of living will be achieved.

The system will also assist in the formation of additional capital by bringing the small savings of thousands of people together, as well as providing a channel for other domestic and foreign capital. Fedecaces will complement the present banking system and the savings and loan system. Its deposits will be held in banks and it will use various banking services. In addition it will build credit worthy applicants for the other systems.

Specifically over the three-year project period Fedecaces has set up the following estimated goals:

Membership: from 10,000 to 30,000

Credit Unions: from 78 to 137 (including branch offices).

Loan Portfolio: from \$250,000 to \$3,438,000

Share Capital (1) from \$4,700 to \$350,000

Note (1): With the forced capitalization system the Credit Unions will be increasing their shares in Fedecaces in relation to their borrowings from Fedecaces.

In order to carry out the project Fedecaces will expand its subloans to affiliated credit unions who in turn will expand their sub-sub-loans to credit union members, in the following categories:

Project 12/2/73

a. General Purpose Loans to: Consolidate debts; provide small commercial loans, pay for medical-dental services; pay for educational expenses; purchase household or personal effects, improve housing; etc.

b. Productive Loans. For fixed and working capital needs of very small entrepreneurs, small farmers, sharecroppers artisans, cottage industries, and small industry.

c. Administrative Improvement Loans. A portion of the A. L. D. loan will be used to establish a revolving fund for this type of sub-loan, based on studies which prove financial feasibility. They will be used to finance full time professional staff, office equipment and office furnishing.

Fedecaces is experienced in these areas of lending and no unusual operating problems are foreseen. An estimate of loan use is shown in the table below:

<u>Type Loan</u>	<u>1970</u>	<u>1971</u>	<u>1972</u>	<u>1973</u>	<u>1974</u>
General Purpose	6%	36%	44%	39%	38%
Productive	78%	52%	48%	52%	55%
Management	16%	12%	8%	9%	7%
	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

In addition Fedecaces will expand its services to affiliates in all areas of credit union activities.

2. A. L. D. Financing

The total project will cost \$7,733,500 virtually all in local currency, of which A. L. D. will contribute up to 2,311,500, as shown in the table below:

	71	72	73
A.I.D. Loan	949.8	1,050.2	(1)
A.I.D. Grants	50.0	30.0	30.0
Share Capital	342.1	671.4	922.6
Other Sources	515.0	1,079.3	1,891.6
	<u>1,856.9</u>	<u>2,830.9</u>	<u>2,844.2</u>

(1) There may be a disbursement flow over into 1973 and to provide for this contingency, the loan has a 3-year drawdown estimate.

A. L. D. loan funds will be made available on a pari passu basis with share capital purchases in the federation and any affiliated credit union, at the ratio of $1\frac{1}{2}$ loan funds to 1 share capital. Other sources would include loans from the Central Bank and other financial institutions and lines of credit from commercial houses. The Central Bank authorized a \$100,000 line of credit to the Borrower in October, 1969 for carrying over and intends to expand this amount (see letters in Annex H, Exhibit G). The Banco Hipotecario has authorized a \$100,000 line of credit for the teaching profession's credit union and would expand it by the same amount when needed. Commercial banks have provided lines of credit to Fedecaces and others. If interest rates are high they will be used if necessary. It is also expected that the Supervised Agricultural Credit Agency - ABCA (Association of Rural Welfare), the Fund for Economic Development and Livestock (MEGA) and Land (META) will support programs they wish to use the credit union system to complete their own credit delivery systems. Coordination of this type of activity is being pursued by Fedecaces.

No problems are foreseen in the maintenance of paid-in share capital since projections are based on past experience and further motivation is provided in that the use of A. L. D. loan funds is tied to increasing paid-in share capital. Although the Borrower will have no control over the contributions from "Other Sources" there have been sufficient expressions of support for Fedecaces that no difficulty is anticipated in securing additional resources to channel into the system.

3. Operations of Fedecaces

Sub-loans are made to affiliated credit unions to meet the demand (see credit survey, Annex H, Exhibit H) for loans for general purpose loans, working capital loans and other loans.

UNCLASSIFIED

loans of the members. Loans to improve credit union administration are also made. The terms of the sub-loans vary depending on the cost of the funds used, the objective of the sub-loan, the management capabilities of the credit union, and the feasibility of the sub-project. Generally, interest rates range from 6% to 10% per year to the sub-borrower and repayments are scheduled for 1 to 5 years.

These substantial spreads are required in order that FEDECACES provide technical and other services at the credit union level, meet administrative costs, build customary reserves and pursue self-sufficiency.

To date about 40% of lending in the system has been applied to "productive loans;" i.e., working capital loans to very small enterprises. 60% of lending has been for general purpose loans, mostly of the personal type. During the course of the project it is anticipated that these percentages can be reversed with 60% going to productive and management activities and 40% to general purpose loans. Lower interest rates or differential discounting will be used to stimulate productive or administrative loans.

Sub-loan ceilings are a matter of regulation (see Supplement 6, Credit Regulation of Fedecaces). Feeder loan individual sub-loans are limited to amounts not to exceed 10% of Fedecaces operating capital earmarked for lending or five times the net worth of the sub-borrower.

The general policy of Fedecaces to date has emphasized the establishment of rural credit unions in order to create a base for the federation. The project will assist in realigning policy and shaping objectives. Loan emphasis will be placed on: (1) reaching rural areas; (2) providing loans for productive rather than general purpose purposes; (3) credit union administration; and reaching a self-sustaining position. In view of the limited supply of financial services available, Fedecaces does not duplicate available services nor does it compete with existing credit systems.

UNCLASSIFIED

First priority is given to establishing credit unions in locations which have no financial institution whatever. Secondly, credit unions are promoted where their services are complementary to existing financial services. And finally they are promoted in places where existing services are not accessible to all that need them.

To carry out its policy Fedecaces performs a number of services and functions, briefly described below:

a. Management Seminars

Fedecaces offers courses on local, zonal and national levels in all aspects of cooperativism. Tuition is charged for all courses to defray expenses.

b. Technical Assistance

To help the credit unions improve their operations technical assistance is offered in the following aspects of cooperative administration: accounting, auditing, office organization, budgeting, projections, organization of promotional campaigns, loss prevention, bad debt control, financial counseling for members, agricultural technical assistance for members with production credit, general administration for the Boards of Directors, organization of new services by the credit unions.

c. Supervised Agricultural Production Program

This program provides agricultural production supervision and intensive cooperative management development in conjunction with the necessary financing. The object of this program is to provide the small farmers who have associated in credit unions, with the credit necessary to purchase modern agricultural inputs, and the technical education and supervision needed.

d. Legal Assistance

The Legal Advisor of Fedecaces is available to the member credit unions for assistance in loan collections, and for groups in the organizational stage, assistance in the process of chartering and the legalization of their By-Laws.

e. Publications and Supplies

The Publications and Supplies Department prints and supplies

accounting forms and educational materials, offers a printing service to the cooperatives for Annual Reports, bulletins, etc., and sells at reduced prices some office supplies and equipment.

f. Savings, Loan Insurance and Bonding

Through an agreement with CUNA MUTUAL Insurance Society, Fedecaces offers life insurance on individual members savings and loans. This insurance pays for loans outstanding and pays to the beneficiary an amount equal to the deceased persons savings. In May of 1970 it is hoped that the Federation, through CUMIS, will be offering a bonding service for local managers and leaders.

g. Central Accounting

Presently in the planning stages is the service of Centralization of Funds and Accounting. This service will utilize presently unused reserves, allow a rapid transfer of unused funds within the affiliated credit unions, and improve the liquidity and solvency of the credit unions and the Federation. This service should be operational by the end of 1971.

h. Financing

The Fedecaces began making loans to its member cooperatives in October, 1967, with a maximum amount of \$400 per loan. These loans were made from the capital of Fedecaces. In April, 1968, the amount was raised to \$800 per loan and in October, 1968, it was raised to \$2,000 due to an AID grant for use in financing the needs of its members. Loan uses are described on page 2 in the same section.

Sub-lending procedures are well developed and follow these steps:

a. Loan Papers. Fedecaces requires the following documentation:

1. A properly executed application on Fedecaces forms.
2. A copy of the credit union charter and By-Laws.
3. Balance sheets and Profit and Loss statements for the last three years and a Trial Balance of the latest month.
4. A loan delinquency report.

5. A copy of the Loan Regulations of the Credit Union.

6. A certified copy of the minutes of the meeting, signed by the Secretary of the Board of Directors, whereby the Board is authorized to apply for the loan and the names of the representatives who can sign and act for the credit union in matters related to the loan.

7. A plan for the use of the loan.

b. Loan Evaluation. The loan papers are studied and analyzed by a loan officer of Fedecaces. A report is prepared which contains an analysis of the administration, the operations of the credit union, the capacity to pay and the recommendations and conditions necessary for the protection of Fedecaces interests.

c. Approval. The Manager is authorized to approve loans up to \$800 and to authorize certain other special types of loans. All other sub-loan applications are approved by the Credit Committee of Fedecaces. ✓

d. Disbursement. Once the loan contract is signed by the applicant, the disbursement is made by check and delivered to a representative of the sub-borrower or it is delivered by mail.

e. Loan Control and Evaluation. Subsequent to disbursement of the sub-loan periodic visits are made by extension agents and auditors of Fedecaces who verify the use of the sub-loan, evaluate the results and arrange for technical assistance as needed.

There are 2 delinquent loans of 18 loans outstanding, amounting to \$410 of a total loan portfolio of \$29,854.

Both loans are considered collectible. The delinquency rate amounts to about 1.4% but Fedecaces loan volume is too small at this point to draw valid conclusions on delinquency. The project committee believes that a 5% delinquency rate and up to 1% for bad debts are valid estimates.

Operating practices of the affiliated credit unions (sub-borrowers) closely follow the pattern of Fedecaces and do not need to be repeated here. A model for credit union By-Laws is available as Supplement No. 3. Other sources of comparative information are found in Supplements 1, 4 and 6.

In carrying out its functions Fedecaces has reached a level of activities that sets a norm of visiting each credit union at least once a month and sponsoring one seminar per week. It also makes at least three spot check visits and one full audit of each affiliated credit union each year.

B. BACKGROUND OF PROJECT

1. The Cooperative Movement in El Salvador

The first chartered cooperatives appeared in El Salvador in 1914. These were generally multi-purpose production cooperatives that lived short lives. The largest in the country is the Cotton Producers cooperative, created by governmental decree in 1940. This cooperative controls all of the cotton production, marketing and acreage allotments are channeled through it. The government has entrusted the job of cooperative development and promotion to the Ministry of Agriculture, the Ministry of Labor, the Ministry of Education, the National Supervised Agricultural Credit Agency (ABC), and the Community Development agency. In the private sector the Salvadoran Coffee Company promotes the organization of cooperatives of small coffee producers, the Catholic Church develops and services credit and production cooperatives among small farmers through its Federation of Cooperatives and the El Salvador Credit Union Federation (FEDECACES) organizes and serves urban and rural credit unions.

In 1943 the Government of El Salvador created a "Rural Credit System" which uses quasi-cooperative local organizations controlled by an autonomous governmental Federation.

At the beginning of 1969 there were 258 cooperatives, not all of which were chartered.

Classified according to type there were:

<u>Type of Cooperative</u>	<u>No.</u>	<u>%</u>	<u>No. of Members</u>	<u>%</u>
Credit Unions	131	50.78	11,341	37.29
Savings and Consumer	17	6.59	1,694	5.57
Artisan	7	2.71	331	1.09
Agricultural	59	22.87	6,671	21.93
Multiple Services	34	13.17	1,080	3.55
Production and Marketing	6	2.33	9,097	29.91
Transportation	4	1.55	201	.66
	<u>258</u>	<u>100.00</u>	<u>30,415</u>	<u>100.00</u>

Until recently the cooperatives in El Salvador functioned under the Salvadoran Commercial Code. In November of 1969, the Legislative Assembly of El Salvador passed its first "Law of Cooperative Associations" and at the same time created the "Salvadoran Institute for Cooperative Development". (See Supplement 1) The new law provides the following advantages:

1. The government recognizes cooperatives as positive instruments of social and economic development for the country.
2. It clearly defines the activity of cooperatives and sets specific norms for their constitution, administration and supervision thus avoiding dangerous deviations from the cooperative system.
3. It facilitates the legal process of chartering.
4. It establishes clear norms for the integration of cooperatives into the Federations and for Federations into Confederations.

The Salvadoran Institute for Cooperative Development will be the specialized official institution charged with promoting, coordinating, and supervising the organization of all cooperative activities in the country. The government will channel all the efforts of its Ministries in cooperative work through the Institute. The Board of Directors of the Institute will consist of ten persons, five of which will be named by the government and five by the cooperative movement of El Salvador.

2. Genesis of the Project

The USAID/El Salvador has been providing technical assistance to the credit union movement since 1964. That year ROCAP and CUNA International initiated a program of credit union organization and development utilizing modern concepts adapted to local conditions. A cooperative technician was contracted to be the CUNA/AID Project Director and a staff of local fieldmen were hired to organize and develop the credit unions. By 1966 56 credit unions were formed representing a total of 4,241 members, \$63,736 of paid in capital and a cumulative total of \$151,610 in loans. The Credit Union Federation was formed by these credit unions and chartered in June of 1966.

Affiliated credit unions now number 78 with a total membership of over 10,000 and paid in share capital is about \$425,000. CUNA provides two contract technicians under USAID contract who work directly with FEDECACES and the member credit unions. The project also enjoys the back up services of the CUNA/LARO team based in Panamá. Without AID assistance it is doubtful that the credit union movement would be this far advanced. The Fedecaces system is under constant study by USAID and CUNA and the last published study in depth was done in 1968, and is represented by Supplement 4, "Analysis of the Federation of Credit Unions of El Salvador".

In view of the sustained growth of the Borrower, the USAID forwarded an IRR to AID/W which was approved by Cable State 203276 dated December 5, 1969. (See Annex I-A). All of the issues raised in the IRR and response have been resolved in the opinion of the Project Committee. Section IV, "Issues" provides related information.

FEDECACES formal application is dated February 16, 1970 and is shown as Annex II-A, "Borrower's Application".

3. Other Sources of Funds

Other international agencies have shown no interest in financing the project and the negative response of the Export-Import Bank, the World Bank and the IDB are shown in Annex II, Exhibit E. The project cannot meet commercial banking criteria at this time so that source of funds cannot be tapped. Local development funds are available to some extent at the present time, but not on the terms required. They are foreseen as a substantial resource in the future.

C. PROJECT JUSTIFICATION/RATIONALE

1. Relationship to CASP.

El Salvador's latest CASP submission sets as a course of action to "promote the continued development of..... credit unions, cooperatives..... pursuant to Title IX of the FAA." In addition to furthering Title IX objectives, this project will also assist in the "Improvement of Agricultural Productivity" a primary CASP objective.

2. Relationship to El Salvador's Credit System

Fedecaces will complement the present credit system by providing services which are not presently available wholly and partially and serving people who do not presently have access to credit. An in depth study of agricultural credit institutions was jointly made by the National Planning Office, with assistance from the Ministry of Economy, the Banco Hipotecario and the Inter-American Development Bank. A summary of the study is attached as Annex II, Exhibit H, "Agricultural Credit Institutions". Evaluations of all sources of credit in El Salvador are made; institutional, non-institutional and special. Included in the study are sources of funds, major beneficiaries, loan uses and shortcomings of each source. Major shortcomings are outlined below:

a. Institutional Sources of Credit

1. An overwhelming proportion of credit is for working capital.
2. Credit for expansion and modernization of productive capacity is below requirements.
3. Terms of loans do not meet the needs.
4. An overwhelming proportion of credit goes to finance traditional export crops - coffee, cotton, sugar.
5. Food crops are starved for funds.
6. Most institutions follow too conservative an approach and minimize risks, thus favoring the large, affluent borrowers who have credit standing and collateral to pledge.

7. An over emphasis on real estate as collateral and the reluctance to accept crops or livestock as security. This excludes many competent small and medium size farmers. Quite often the credit is not used for the purpose for which it was borrowed.

8. Shortage of overall financial resources, poorly distributed in favor of traditional exports and large landowners, forces the medium, small and very small farmers to borrow from private non-institutional sources at much higher cost.

9. Shortage of qualified agricultural technicians and absence of agricultural research and feasibility studies upon which to base loans.

10. Slow processing of loan papers and excessive centralization of decision making.

11. The credit delivery system, is not extensive enough and many areas do not enjoy credit services.

b. Non-Institutional Sources of Credit

1. Credit is almost always short term and for operating capital only.

2. Interest charges are relatively high, amounting to $3\frac{1}{2}\%$ more than commercial bank rates.

3. Credit extended is often part of a sales contract, binding the producer to sell at a fixed price below the market price.

4. Credit is insufficient to meet the needs of the medium, small and very small farmers.

c. Special Agricultural Credit Programs

(Land Improvement - META), Cattle Improvement (MEGA), Swine Improvement (MEPO) and the Central Bank's Economic Development Fund (FDE).

1. Shortage of qualified technical personnel.

2. Lack of effective control over use of funds.

3. The practice of permitting the financial intermediaries

to apply their own criteria for lending, which often conflicts with the purpose of the loan program.

4. Poor coordination and understanding between the technical and financial aspects of projects.
5. Lack of required project development.
6. Poor planning and follow-up on investment projects.
7. Lack of coordination between government agencies and programs.

It would be pretentious to think that the FEDECACES system will correct the above shortcomings, but it can assist towards correcting some of them. It is expected that FEDECACES will:

1. Provide credit to small and very small farmers.
2. Tailor loans to fit the needs.
3. Not make loans for traditional export crops; coffee, cotton, and sugar.
4. Lend without real estate collateral and will accept crops, livestock or a personal note as security.
5. Control end use of loan funds.
6. Address the shortage of overall credit resources by bringing ever increasing amounts of new capital into the credit system of the country.
7. Process loans rapidly in a decentralized way through its member credit unions.
8. Extend services to areas not presently served.
9. Provide a credit source as an alternative to the usurer and other high cost sources of credit.
10. Be able to channel funds from special sources such as META, MEGA, FDE, and ABC through its affiliated credit union members.
11. Arrange for the provision of necessary technical assistance.

3. Contribution to El Salvador's Economic Development

Although the conflict with Honduras set back El Salvador's economy, through hard work of its entrepreneurs and the good fortune of rising coffee prices the country appears to be approaching its pre-conflict growth rate of approximately 4% GDP. This recovery has occasioned shifts in traditional sales and investment patterns; import substitution and export promotion activity have increased. Private investment has resumed with caution as entrepreneurs assess the future of the markets of El Salvador and Central America.

While economic growth is still sluggish at 4%, population growth maintains a high rate of 3.6%, virtually excluding any per capita income gain. Complicating the issue is the fact that almost 50% of the population is under 15 and no significant reduction in the growth rate is foreseen for the near future.

The GOES appears to be taking an increased interest in economic and social development as reflected by an expanded public sector investment program. The government has recommended a substantially increased 1970 investment budget to the national assembly, to be financed by a sales tax not yet approved.

The influx of refugees from Honduras has exacerbated almost all of El Salvador's socio/economic problems, but has not created any acute problems. The GOES is re-locating the refugees and is assisting them to find employment. By these measures the GOES shortly hopes to fully integrate the refugees into the life of the country.

In the future the economy can be expected to accelerate modestly, if exports continue to increase and coffee prices remain reasonably high. Should this occur import controls may be gradually reduced. Private investment would increase, with emphasis on the domestic market, and the world market. A more cautious investment approach to the Central American markets, as it undergoes restructuring, appears likely.

Future GOES investment programs are expected to concentrate on public works construction, export promotion, land reform, agricultural and rural development and educational reform. The problem of financing these programs will probably constitute a continuing source of public debate.

The loan to FEDECACFS is not expected to have great impact on the major economic issues such as private investment, export promotion, import substitution, tax revenues and the development of the CACM. However, the credit union system will serve thousands of people in the rural sector, assisting them to achieve higher agricultural productivity and income. Refugees would have access to credit through the system and might be assisted in their resettlement process.

The present loan will provide "seed capital" to strengthen the system. It is too early to project the economic impact of the program. Optimistically viewed, in the future it could develop into a third financial system of significant importance, and also serve as one vehicle for the overall development of people in the lower income groups, especially in the rural areas.

4. Debt Service Capacity

Debt burden of GOES is relatively low in comparison to other Latin American countries of similar economic conditions. The present loan should not represent much of an additional burden.

5. Impact on the U. S. Economy

The loan will not have an adverse effect on the U. S. economy due to competition with U. S. enterprise. During the disbursement period (1971-3) total project purchases are estimated at \$12.1 million dollars, of which 7% or \$840,000 is estimated to be of U. S. source/origin from off-the-shelf purchases. Within 5 to 7 years project purchases of U. S. source/origin will equal the amount of the loan. In the long run the loan is expected to make a contribution to the U. S. economy.

6. Title IX - The Building of Democratic Institutions.

Title IX provides that "emphasis shall be placed on assuring maximum participation through encouragement of private voluntary organizations and strengthened local government institutions." Credit union development directly addresses Title IX objectives. Thousands of people participate and become deeply involved in building cooperative enterprises and thereby participate in the process. It constitutes a practical laboratory for personal development by:

1. Providing opportunities for decision making, growth of responsibility and development of social skills.
2. Demonstrating the right of majority rule and the protection of the rights of the individual.
3. Changing individual motivation and attitudes, and developing responsible leadership.

7. Consistency with the CIAP Reviews

Although the CIAP has not made specific reference to cooperative and/or credit union development in El Salvador, it is the conclusion of the project committee that this loan addresses the CIAP findings and recommendations for the social and economic development of El Salvador.

8. Certification of D/USAID

The USAID Director certified on March 4, 1970 that in his opinion FEDECACES has demonstrated the necessary capabilities to carry out this loan project. Refer to Annex I, Exhibit B, for the actual certification.

SECTION II - PROJECT ANALYSIS

A. BORROWER

FEDECACES is a private non-profit national federation, chartered by the Ministry of the Interior and regulated under the Commercial Law of the country. Its members are 100 affiliated credit unions. Each credit union sends its representatives to the zonal and general assemblies (annual meetings, the General Assembly being the maximum authority of the Federation. The General Assembly elects the officers of the Federation which include seven members of the Board of Directors, three members of the Supervisory committee and three members of the Credit Committee. The Board of Directors names three of its members to an Executive Committee which serves between meetings of the Board of Directors.

The Fedecaces manager is named by the Board of Directors and is in charge of operations, which are carried out through three divisions. Personnel of Fedecaces numbers 20 and 6 Police Constables, Volunteers and 2 contract employees from CUNA provide advice and assistance to the federation and its members. The organizational organization chart gives a graphic picture of Fedecaces (See Annex II, Exhibit A).

The project will be carried out by Fedecaces through sub-loans to its member credit unions, with needed advice and assistance. The credit unions in turn will make loans to their members.

Management of the project is exercised at the federation and credit union levels. Seven years, 1964 through 1970, inclusive, will have been spent in building the system, largely through AID technical assistance. The management is considered adequate to administer the project, assuming continued management advisory services by CUNA through 1973 as planned. Training programmed local and foreign, will be a continuing feature of A. I. D. assistance for key personnel of the system. The Federation carries out an average of one training seminar per week on some phase of credit union activities and on the job training is accomplished by visits carried out daily. A continued up-grading of personnel at all levels is planned and programmed. Section III-D, Conditions and Covenants includes recommendations which will be included in the loan agreement to help assure satisfactory management.

Additional details on the organization and administration of the Borrower are found in Annex II-A and its supplements.

The relationship of Fedecases with other public and private organizations is shown in Annex D-A. At present these are largely informal relationships, and most of them are directed to operating to enhance cooperation.

B. ECONOMIC AND SOCIAL EVALUATION

During the course of its review Fedecases made a survey of the credit needs of its member credit unions covering the twelve months. The results indicate that there are 870/ units of credit unions amounting to the credit unions which cannot be supported for lack of funds in an amount of \$206,000. It also shows an estimated need of \$5,000,000 during the next 12 months for the following categories:

	%	Amount
Capital Deficiency	2.3%	\$1.7
Fixed Capital	3.2%	2.4
Fixed Capital	0.3%	1.6
Working Capital	1.2%	0.9
	<u>7.0%</u>	<u>5.6</u>

The program was explained to the project committee. The major source of reference to the projected use of \$950,000 in 1973, under the one year term conditions precedent to the program. A review of the survey is included in Annex D-B, and the actual survey responses are attached to the report.

The intangible benefits deriving from consideration of the objectives of this loan - development of cooperative organizations and their human resources - are difficult to quantify. A test for measuring the economic impact of the program will be the growth factor of the free credit union in the region and its economic productivity effect on the economy of the region as a result of the program.

The program will involve the loan of funds and sub-lending of funds, the project will involve the relationship of the affiliated free credit

unions from the present 10, 000 to 30, 000 by the end of 1973. This addition of 20, 000 low-income families will benefit an additional 100, 000 people (at an average of five people per family).

Family monetary incomes of prospective credit union members is estimated to be \$712 equivalent per year in 1970. With the assistance resulting from the project, it is estimated that the family income of affiliated members will rise to \$863 equivalent per year by the end of 1973, an increase of \$151 per family, or 21.2%.

This produces a productivity increase of \$3,020,000 per year for the 20, 000 newly added members. These added productivity benefits would exceed the amount of the AID loan.

This magnitude of productivity increase will be significant to the 100, 000 low income and marginal family members, who are striving toward middle class stature. Many of these will eventually become a part of the potential national tax base of the country.

3. Social Evaluation

The underlying purpose of this project is the personal development of 30, 000 people by involving them in the organization and administration of a credit union system. They will be voluntarily associated in grass-roots private democratic organizations. Through such participation it is expected that the objectives of Title IX of the F. A. A. will be served.

It is likewise expected that by educating the membership to a responsible use of credit and an appreciation of savings that many social benefits will accrue. Loans for improved housing, personal effects, education, and better health will be extended to ever increasing numbers of people. By eliminating usurer debts and providing credit on individually designed terms a more effective use can be made of available family income.

The system offers the small and very small entrepreneur a source of credit, technical assistance and personal education. This will improve the productivity of thousands of people and their standard of living and quality of life.

In summary it offers hope to many of improving their lot and satisfying some of their minimum aspirations.

The mere fact of voluntarily associating with others to make decisions to improve the group as a whole and for self-improvement

constitutes social development. To arrive at the decision to join a credit union implies the assumption of personal responsibility to contribute to the group as well as to enjoy the benefits.

C. FINANCIAL ANALYSIS

1. Fedecaces Operating Situation

Since its inception, Fedecaces has shown annual operating losses (See Annex II Exhibit D-1) as would be expected during the pilot period in which the framework of a national credit union system is being established. These operating losses have been offset by A. I. D. grant subsidies to Fedecaces (Annex II Exhibit D-2). During 1966-1969, Fedecaces' net operating loss represented 86.9% of its net operating expenses. As Fedecaces gained experience and benefited by the technical assistance provided by A. I. D. grants, this ratio began to turn downward, being 98% in 1966, 99% in 1967, 74% in 1968, and 83% in 1969. (1969 showed higher technical assistance costs as lending program was expanded).

The cumulative net loss during 1966-1969 amounted to \$174,100. Virtually all of the net losses incurred during this period were for the expenses of creation and improvement of affiliated credit unions. Fedecaces sub-lending activities only became an important part of its operations in 1969.

From 1970 through 1974 Fedecaces expects to produce operating revenues through substantially expanded sub-lending activities, to the point that A. I. D. grant subsidies will no longer be needed. Fedecaces net losses are projected to decrease from \$124,500 in 1970 (a year in which A. I. D. loan funds are not expected to be available for substantial expansion of Fedecaces' sub-lending program) to \$99,400 in 1971, and \$34,800 in 1972. In 1973 Fedecaces projects a net gain from operations of \$42,600.

2. Comparative Balances 1966-1969

Fedecaces began operations in May 1966, as successor to the AID/CUNA cooperative development program, which began in late 1964. As of December 31, 1969, Fedecaces' assets totalled \$81,400 (equivalent), against liabilities of \$28,200, and capital and reserves of \$53,200 (of which paid-in capital was \$4,700, reserves \$5,500, and a carryover of A. I. D. granted funds for sub-lending of \$43,000). Loans outstanding amounted to \$47,800. Comparative balance sheets for the period 1966-1969 are

shown in Annex II D-3.

Throughout its four years of operations, Fedecaces has maintained a satisfactory working capital ratio and its cash position has been satisfactory.

Fedecaces' working capital ratio did not become a significant datum for financial analysis until it dedicated a larger part of its program to sub-lending in 1969 as an effort toward approaching self-sufficiency. In 1969 Fedecaces' working capital ratio (current assets to current liabilities) was 2.4 - 1.0, and net working capital amounted to \$40,200. It is anticipated that Fedecaces will maintain a satisfactory working capital ratio averaging about three to one during the years 1970-1974.

During 1966-1969 Fedecaces has operated primarily on its own funds derived from affiliated credit union savings and A. L. D. grants. Thus, the ratio of net worth to total liabilities is not significant to that period of its operations. Starting in 1970, Fedecaces will incur short-term (Central Bank credits) liabilities, and in 1971 long-term liabilities (A. L. D. loan drawdowns).

From a cold capital risk viewpoint, Fedecaces' net worth to total liabilities during the period 1970-1974 may not be favorable enough for it to safely incur additional long-term indebtedness unless it is of a concessional type. A covenant will be included in the loan agreement to require A. L. D.'s prior approval of Fedecaces' incurrence of any additional medium or long-term indebtedness during the life of the loan.

3. Loans made by Fedecaces 1966-1969.

During 1966-1969 Fedecaces made 26 loans aggregating \$72,747 (equivalent). By function, these loans were distributed as follows:

<u>Function</u>	<u>Amount</u>	<u>Percent</u>
General Purpose	\$28,400	39%
Productive	43,366	60
Management	981	1
Total	<u>\$72,747</u>	<u>100%</u>

With the assistance of the A. L. D. Regional auditor, an audit being performed on Fedecaces during intensive review has revealed that Fedecaces has complied in all material respects with A. L. D. grant agreements and covenants.

An informal project committee examination of Fedecaces accounts during February 1970 indicated that Fedecaces delinquencies on sub-loans made from A. L. D. grant funds were about 1.4% and it had not suffered any losses from bad debts. Fedecaces small reserves for bad debts appear to be adequate for at least the short-term future.

The projected expansion of Fedecaces' lending program, caused by the A. I. D. loan and funded from both A. L. D. and local sources, will undoubtedly be subject to a higher delinquency rate than has been incurred during Fedecaces' short lending experience to date. It is anticipated that adequate reserves for the contingency will be established by Fedecaces as a result of the recommendations which will be made by A. I. D. grant funded technicians who will assist Fedecaces in expanding its system.

Fedecaces' annual lending activities increased from \$1,700 during 1966 to \$54,000 during 1969. The projected cash flow for the period 1970-1974 estimated Fedecaces loans to sub-borrowers at \$234,400 for 1970, \$1,286,000 for 1971, \$2,957,900 for 1972, \$3,433,700 for 1973, and \$4,306,000 for 1974. See Annex II D-6.

4. A. I. D.'s Contribution to Fedecaces Capital and Operations

A.I.D. has made substantial technical assistance contributions to FEDECACES and anticipates phasing out by the end of 1973 as shown in the following table.

A.I.D. Technical Assistance Grants to FEDECACES
(in thousands of U.S. \$ equivalents)

<u>Year</u>	<u>Total</u>
1966 (Actual)	\$ 68.2
1967 "	58.7
1968 "	74.1
1969 "	167.0
1970 (Programmed)	158.5
1971 "	50.0
1972 "	30.0
1973 "	30.0
1974 "	<u>NONE</u>
	\$636.5

5. Financial Plan

Estimated contributions of loan funds to the project over the estimated 3-year disbursement period are equivalent to \$5,666,300 broken down as follows by source of funds:

Total Contributions of Loan Funds in Total System (Fedecaces plus Credit Unions)

	<u>1970</u>	<u>%</u>	<u>1973</u>	<u>%</u>
A.I.D.	\$ 0	0.0	\$ 2,000.0	35.3
Fedecaces	\$ 32.0	3.7	\$ 212.5	3.8
Credit Unions	\$ 617.2	71.4	\$ 2,228.0	39.3
BCR	\$ 200.0	23.1	\$ 1,225.8	21.6
Other	<u>\$ 15.9</u>	<u>1.8</u>	<u>-</u>	<u>0.0</u>
	<u>\$ 865.1</u>	<u>100.0</u>	<u>\$ 5,666.3</u>	<u>100.0</u>

The above growth in contributions by the various parties reflects the catalytic effect of the A.I.D. loan over the three year disbursement period, 1971-3. Due to this accelerated growth, caused essentially by the A.I.D. loan plus T.A. inputs, it is expected that Fedecaces will be able to achieve a self-sustaining level by 1975. (see ANNEX II-D for financial data).

As seen from the foregoing table, domestic resources are to account for 64.7% of the loan program and 35.3% will come from the ID loan. AID grants are in addition to the above.

5. Terms of the Loan

The terms recommended for the proposed loan of \$2.0 million are a 25-year amortization period for Borrower, including a 7-year grace period on repayment of principal, and an interest rate of 2% during grace period and 3% thereafter. The two-step procedure will be optional. If GOES elects to accept payment in colones from Borrower, it will make dollar payments to A. I. D. over a period of 40 years, including a 10-year grace period at an interest rate of 2% during its grace period and 3% thereafter and will also guarantee repayment.

6. Justification of Loan Terms

The project committee believes that the terms recommended are essential to Fedecaces' development financing needs, and

are in conformity with current A.I.D. practice. The financial analysis of Borrower (Statement of Operations, comparative balance sheets, and projected cash flow) indicates that Fedecaces will be solvent financially and can reasonably be expected to assimilate the amount of funds being requested. The loan also will make an important contribution to achieving an improved level of income for thousands of Salvadorans, and to some degree, strengthen the country's balance of payments position.

7. Availability of Alternative Sources of Funds.

The loan committee, after considering the numerous efforts of Fedecaces to obtain credits from other lenders, is convinced that A.I.D. is the lender of last resort for the concessional-term funds which Fedecaces requires. IBRD, IDB and Eximbank have respectively indicated no interest in this loan. (See Annex II - Exhibit E).

8. Prospects of Repayment.

The loan will not be guaranteed. Given the important Title IX purposes of this loan it is believed desirable to keep government influence and/or paternalism to a minimum. Therefore, the USAID has not pressed Fedecaces or the GOES for a government guarantee.

The loan will be backed by the full faith and integrity of Fedecaces the 78 member credit unions and the 10,000 credit union members. This moral obligation will be formalized through resolutions passed by the respective board of directors of Fedecaces and each credit union. It is important to the development of the credit union movement that each member understand his moral obligation to repay the AID loan just as he would a loan from his credit union.

The delinquency and charge off rates for 12,000 federal credit unions in the United States on \$7 billion in loans are characteristically low, 3.0% and 0.25% respectively. Although statistical rates are not yet available for Latin America it is estimated by spot checks that they are within 5% and 1% for delinquency and charge offs on \$244 million of cumulative credit union lending in 12 Latin American countries.

The total system (Fedecaces and credit unions combined) backing the AID loan will have a minimum debt-equity ratio of 3 to 2 because the AID loan will be drawn down on a $1\frac{1}{2}$ to 1 relationship with paid in share capital to the system. Fedecaces alone has a debt-equity ratio projected as follows: 1970, 2 to 1; 1971, 7 to 1; 1972, 9 to 1; 1973, 6 to 1; 1974, 5 to 1; 1975, 4 to 1. The rapid growth of Fedecaces equity will be achieved by a forced capitalization plan which requires that 10% of all Fedecaces subloans be used to purchase share capital of Fedecaces.

Convertibility of local currency to U.S. dollars will be assured under the Law of International Transfers. The maintenance of value risk will be assumed by Fedecaces which will build up a m.o.v. reserve to an amount equal to 5% of the outstanding balance of the AID loan. A bad debt reserve of 1.5% of all outstanding loans (including those financed by A.I.D., plus those from local sources) will be set up by Fedecaces. This, plus the approximate 2% reserve maintained at the affiliated credit union level, provides a 3.5% bad debt reserve for the system. Fedecaces management will be assisted by AID/CUNA technicians through 1973, thus assuring an in-house monitoring of all of its activities.

Obviously, an unguaranteed loan to a new and developing credit union federation is not a gilt edged investment. After all projections, policies, organization and operations have been analyzed the loan is a calculated bet on the people who will carry out the project and the future of the host country economy.

All things considered, the Project Committee believes that A.I.D. will have reasonable protection as lender and concludes that prospects for repayment are reasonably good.

SECTION III - LOAN ADMINISTRATION

The Federation of Savings and Loan Cooperatives (Fedecaces) will have the primary responsibility for implementation of the loan. The convertibility aspect of the loan, will be guaranteed by Fedecaces' registry of the loan with the Central Bank. The credit risk will be assumed by Fedecaces, backed by its member credit unions, as explained immediately above on page 25, paragraph 8. In addition, a maintenance of value reserve will be established. The primary responsibility for fulfilling A.I.D.'s part of the implementation function rests with USAID/El Salvador, assisted by LARO/CUNA technicians, and by ROCAP and AID/W personnel, as appropriate.

The Loan Agreement and basic Implementation Letter No. 1 will state the conditions which must be fulfilled by Borrower prior to any disbursement of A. I. D. funds. USAID/El Salvador and LARO/CUNA personnel, assisted by ROCAP and AID/W personnel, as may be required, will ensure that loan procedures considered acceptable as conditions precedent and the covenants contained in the Loan Agreement are in fact being followed, and that Fedecaces' institutional and sub-lending activities are progressing satisfactorily.

On the assumption that the Loan Agreement will be executed by September 30, 1970, the following schedule of implementation target dates appears realistic:

FY 1970

April 1970	Agreement authorized
June 1970	Draft Agreement and IL No. 1 Submitted to Fedecaces

FY 1971

Sept. 1970	Fedecaces and A. I. D. execute agreement
Dec. 1970	Conditions Precedent to first disbursement met, Fedecaces arrangements for continued line of credit from Central Bank completed.

Jan. 1971	Commitments made and first disbursement made.
<u>FY 1972</u>	
August 1971	\$750,000 disbursed.
December 1971	Additional share capital paid in to credit union system and total of \$1.0 million disbursed.
April 1972	Additional share capital paid in to credit union system total of \$1.5 million disbursed.
Dec. 1972	Loan fully committed.
March 1973	Loan fully disbursed.

The Loan Committee foresees no unusual problems in implementing this loan. Fedecaces has established a framework of free affiliated credit unions upon which to build an expanded system, suitable technical services are now being performed and are expected to be continued by LARO/CUNA, and the Mission has obtained Fedecaces' agreement to take such steps as may be necessary to successfully implement this loan. All standard A.I.D. procedures for procurement and disbursements will apply.

Conditions and Covenants

In addition to the usual conditions and covenants, the Loan Committee recommends that the Loan Agreement contain the following requirements:

1. Conditions Precedent to any Disbursement
 - (a) Evidence of registration of the loan with the GOES to assure availability of United States dollars for payment of interest, repayment of principal, or other payment obligations,
 - (b) Evidence that, except as A. I. D. and Borrower shall otherwise agree in writing, Borrower and its member credit unions have a net worth (share capital, reserves,

undistributed earnings, and donations) amounting to not less than the equivalent of five hundred thousand United States dollars (\$500,000).

- (c) Borrower will provide evidence in form and substance satisfactory to A.I.D. attesting that this loan will be backed by the full faith and integrity of Fedecaces and its member credit unions.

2. Conditions Precedent to Disbursement of more than \$750,000 (equivalent):

- (a) Evidence that, except as A.I.D. and Borrower shall otherwise agree, Borrower and its affiliated credit unions have increased their share capital by at least \$100,000 equivalent from the base established in III.1.(b).

3. Additional Covenants and Warranties:

In addition to the standard covenants, the Loan Agreement shall contain covenants to the effect that, unless A. I. D. otherwise agrees in writing,

- (a) Borrower shall agree to incur no additional medium or long-term indebtedness or to dispose of real property without prior A. I. D. approval in writing.
- (b) Borrower shall agree to expand its rural credit unions, within two years from the effective date of the loan, to the point where the rural credit unions' proportion of Borrower's and its member unions' paid-in share capital is at least thirty (30%) of the total value of such paid-in share capital,
- (c) Borrower shall agree that earnings on the interest spread between the rate charged in the A.I.D. loan and that charge on sub-loans of Borrower as well as the rollover funds from the A.I.D. loan shall remain in the credit union program of Borrower.
- (d) Prior A. I. D. approval shall be obtained with respect to the technical and economic feasibility of any project financed under this loan in an amount exceeding fifty thousand United States dollars equivalent (\$50,000),

- (e) No equity investments shall be made in whole or in part from A. I. D. loan funds without prior approval of A. I. D. in writing,
- (f) No contractual commitment for professional services financed under the loan shall be made by Borrower or its member unions until A. I. D. shall have given its approval of the contractor and the contract,
- (g) Sub-loans to eligible sub-borrowers from Borrower shall be made for varying periods but in no case for less than one (1) year nor for more than fifteen (15) years, including various grace periods whose duration shall be determined by Borrower; however, loans of longer duration may be allowed in exceptional cases with prior A.I.D. approval.
- (h) It is understood and agreed that of the two million United States dollars (\$2, 000, 000) equivalent loaned to Borrower by A. I. D. , not to exceed one hundred thousand United States dollars (\$100, 000) or its equivalent may be used for technical assistance contracts.
- (i) Borrower will covenant that it and A. I. D. will carry out progress reviews of the project as deemed appropriate by either party and that Borrower will take remedial action as appropriate.
- (j) Borrower shall accrue out of net income a reserve against bad debts, and other losses of not less than 1. 5% of outstanding loans and an administrative maintenance of value reserve of not less than 0. 5% per year computed on the balance of all outstanding sub-loans, cumulative until such reserve is equal to 5% of the AID loan, at which percentage level it will be maintained. In the event that a devaluation of Salvadoran colones should occur, and the m. o. v. reserve is depleted, the m. o. v. reserve will be revised, in a manner satisfactory to A. I. D. , so that the reserve is rebuilt to the point that it equals at least 5% of the then outstanding balance of the A. I. D. loan.

This reserve is not available for payment of dividends by Borrower but may be loaned, invested, or otherwise used by Borrower in any manner consistent with the provisions of the Loan Agreement.

- (k) Borrower will exert its best efforts to encourage a wide distribution of equity participation in Borrower, with special emphasis in increasing the proportion of its rural credit unions equity position.
- (l) Borrower and its member credit unions shall not without prior approval of A.I.P. declare or distribute any cash dividend on, or make any distribution on account of, any class of stock of Borrower now or hereafter outstanding, exceeding 10% annually of paid-in capital during the term of the loan, except distribution in excess of 10% is matched by a cash prepayment of this loan.
- (m) Borrower shall require any sub-borrower of more than \$25,000 equivalent in any bill made available, satisfactory to Borrower.
- (n) Borrower shall make, and review with A.I.P., an annual operating plan and budget, including the amount of income and expense, and use of loan funds.
- (o) Borrower will include in all financial statements a statement that the sub-borrower (directly or indirectly) owns a share of capital of Borrower and is liable for the full loan.

4. Covenant Concerning Dividend Payouts

- (a) It is understood and agreed that A.I.P. loan funds will be made available on a non-recourse basis of one and one-half (1 1/2) of A.I.P. funds of the local share capital of Borrower and its member credit unions.
- (b) The local currency required to meet the local needs incurred under the loan will be provided as required by the USDO (RDO) following the amount determined by State/Treasury for other purchases and needs for U.S.G. needs.

31
UNCLASSIFIED

Special Option

The Act will provide that the Government of El Salvador may elect the two-step repayment procedure. If the procedure is elected, the COME will accept payments from the borrower and will make payments in dollars under the following terms:

A. Interest on the principal balance of the loan at the rate of two percent (2%) per annum during a grace period not to exceed ten (10) years ("Government Grace Period"), and three (3) percent per annum thereafter.

The principal in United States dollars, within forty (40) years, including the Government Grace Period.

total amount of the

will also guarantee repayment of the loan if the two-

SECTION IV - ISSUES

All issues have been satisfactorily resolved; as noted below.

<u>Issue</u>	<u>Loan Committe Comment</u>
1. Capability of system to manage self-help housing, grain storage and marketing systems.	1. Beyond capabilities at this time. Dropped as a major activity.
2. Provision of reasonable debt: equity ratio by Borrower	2. Intensive review indicates ratio of 4 debt: 1 equity which is considered satisfactory and attainable within 5 years.
3. Legislative requirements.	3. New Cooperative Law passed December 9, 1969.
4. GOES Guaranty	4. Not considered essential. Loan to be backed by total system. See Sec. II-C-8.
5. Duplication of existing services by expanding Fedecaces role in rural areas.	5. No issue. Fedecaces provides other needed services and/or operates where no other institution has representation. Needs far beyond available services of all agencies.
6. Technical assistance requirements.	6. See Section II-A A. L. D. grant phase out 1971-73. Loan operations will provide thereafter.
7. Financial viability.	7. Project considered financially viable with AID concessional interest rates and diminishing T.A. input through 1973. See Sec. II-C.

- | | |
|--|---|
| 8. Local currency requirements | 8. See Section II-C for justification. |
| 9. Fedecaces management capability to carry out project. | 9. See Part Two - Sec II-A; appraisal of management factor and supporting measures. |
| 10. Convertibility of funds for loan servicing. | 10. No problems foreseen. Easily managed by registering loan under International Transfer Law. See Sec. II-C-8. |
| 11. Guaranty operations. | 11. To be undertaken at a later date. |

T E L E G R A M

FROM: SECSTATE WASH DC
TO: AMEMBASSY SAN SALVADOR
SUBJECT: FEDECACES CREDIT UNION IRR

THE CAEC APPROVED FEDECACES IRR SUBJECT TO THE FOLLOWING:

1. Clarification of loan activities. Assuming purpose help FEDECACES achieve self-sustaining financial status with expanded role as central agency, self-help housing and perhaps grain storage and marketing systems would appear beyond capabilities of credit unions or FEDECACES in early stage development.
2. If FEDECACES to assume central agency role for system AID loan assistance requires reasonable debt-equity ratio or in lieu thereof viable financial plan for achieving this, Financial outline presented in IRR requires amplification and explanation in view guaranty program and other financial and technical requirements.
3. Any legislation, GOES approvals and/or support required by FEDECACES to expand role should be secured during intensive review or set forth as condition precedent disbursements. AID/W concurs with Mission re new cooperatives law as being basic to viability of credit union system. Since GOES guarantee of AID loan is required suggest USAID secure assessment to this effect prior initiation intensive review.
4. Among other things review should clearly define the need for expanding FEDECACES role in rural area within context of existing institutional structure and services, especially related to ABC, Caja de Crédito and similar rural based credit institutions.

ANNEX I
Exhibit A

Page 2 of 2

5. Credit union development 1966-69 impressive, especially in urban area. Review should address TA requirements to sustain growth during life of loan and thereafter and indicate whether inputs to be loan or grant funded.
6. Financial analysis should justify money cost margins between AID, FEDECACES, credit unions and ultimate users and projections should establish financial viability. Since latter basic to loan authorization suggest USAID undertake financial analysis immediately following assessment GOES willingness act as guarantor AID loan and probability achievement workable cooperatives law.
7. Re paras 2 and 6 AID/W could arrange for financial analyst TDY through CUNA/AID/LARO contract. Cable USAID concurrence, timing, appropriation and allotment numbers.

RICHARDSON

UNCLASSIFIED

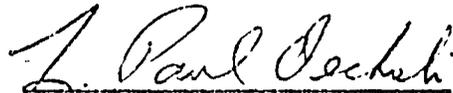
ANNEX I
Exhibit B, Page 1 of 1

CREDIT UNION DEVELOPMENT

CERTIFICATION PURSUANT TO SECTION 611(e)
OF THE FOREIGN ASSISTANCE ACT OF 1961
AS AMENDED

I, L. Paul Oechsli, the principal officer of the Agency for International Development in El Salvador, having taken into account among other things, the maintenance and utilization of projects in El Salvador previously financed or assisted by the United States, do hereby certify that in my judgement El Salvador has both the financial capacity and the human resources capability to effectively maintain and utilize the capital assistance project, "Credit Union Development" (Fedecaces).

The capital assistance paper certifies that the statutory criteria as applied to El Salvador have been met. Discussion in the capital assistance paper clearly has demonstrated the capability of El Salvador and the Borrower effectively to maintain and utilize the project. Basically, El Salvador has shown reasonable effectiveness in maintaining and utilizing projects financed or assisted by the United States.


L. Paul Oechsli, Director

Date: March 4, 1970

UNCLASSIFIED

FEDECAECS

PROJECT DETAILS

Exhibit A - Application letters from Fedecaces to USAID dated February 16 and 24, 1970 with following items:

- 1 - Basic data on Fedecaces
- 2 - Organizational Structure of Fedecaces
- 3 - Charter Members of Fedecaces
- 4 - Fedecaces Institutional Relationships

Exhibit B - Credit Survey of Credit Union System

Exhibit C - Map showing locations of affiliated Credit Unions

Exhibit D - Financial Statements and Projection

Exhibit E - Letters from IBRD, IDB and Export-Import Bank

Exhibit F - Letter of support to Fedecaces from National Planning Office

Exhibit G - Letter from Central Bank on line of credit to Fedecaces

Exhibit H - Salvadoran Agricultural Credit System

Supplements: (Not attached - see Official Files)

1. Law of Cooperatives and Law creating Salvadoran Institute for Cooperative Development (English and Spanish)
2. Statutes of Fedecaces (Spanish)
3. Model Statutes for Salvadoran Credit Union (Spanish)
4. Analysis of Fedecaces (Spanish)
5. Survey of Credit Union Demand (Spanish)
6. Credit Regulations of Fedecaces (Spanish)

FEDERACION DE COOPERATIVAS DE AHORRO
Y CREDITO DE EL SALVADOR

USAID SAN SALVADOR
ACTION TO *DOM*

F E D E C A I O N E S



Edificio LUZ 1er. Piso
Fuente Luminosa y 25 Av. Nte.
Apartado Postal 156
San Salvador, El Salvador. C A
TELS: 25-5103 25-5121 25-5123

UNCLASSIFIED
AID-DLC/P-890
ANNEX II
Exhibit A - Pg 1 of 9

16 de Febrero de 1970.

Mr.
L. Paul Oechsli, Director
USAID Mission to El Salvador
c/o Embajada Americana
Presente.

Estimado Mr. Oechsli:

Por este medio me permito informarle que nuestro Consejo de Administración en Sesión celebrada el día 11 de los corrientes, acordó gestionar ante esa Agencia la Asistencia Financiera necesaria para desarrollar el Programa de Asistencia Financiera y Técnica, que la Federación proporcionará a las Cooperativas afiliadas y a sus asociados.

El destino principal de los recursos que esa Agencia pueda proporcionar a la Federación, serán para créditos a la producción, al consumo, Contratos Gerenciales, equipo de Oficina, etc. La mecánica para la canalización de estos recursos ha sido ya establecida y aprobada por los Asesores de CUNA/AID.

La Federación está dispuesta a suministrar a esa Agencia en cualquier momento la información necesaria para demostrar la factibilidad en el uso de los recursos que se han puesto a su disposición, así como datos referentes a las experiencias que el campo crediticio ha tenido en el pasado.

De Usted con toda consideración,


LIC. RUBEN GODOFREDO RAMIREZ
Secretario/Consejo de Administración.

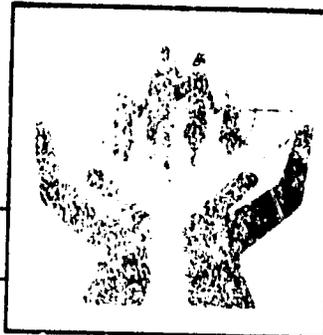
LEG/mef.

FEDERACION DE COOPERATIVAS DE AHORRO
Y CREDITO DE EL SALVADOR

USAID SAN SALVADOR
ACTION

CD

FEB 25 1970



Edificio LUZ 1er. Piso
Fuente Luminosa y 25 Av. Nte.
Apartado Postal 156
San Salvador, El Salvador, C. A.
TELS 25-5103 25-5121 25-5123

UNCLASSIFIED
ANNEX II
Exhibit A - Pg 2 of 4

February 24, 1970.

Mr. L. Paul Oechsli, Director
USAID Mission to El Salvador
c/o American Embassy
San Salvador.

Dear Mr. Oechsli:

Following our Board of Directors Secretary letter of February 1970, I am pleased to provide you with additional information on our proposed loan request.

During the past several years we have been working with advisors provided by your office with a view toward establishing a private non-profit self sustaining credit union system. Because of your technical assistance over the past five years we have been able to promote, organize and start up the operation of a Federation and almost 100 credit unions, 78 of which are presently affiliated with the Federation and have over 10,000 members. The net worth of the Federation and affiliated credit unions was about \$500,000.00 as of December 31, 1969. Credit union development has also benefited from the passage of a cooperatives law in December, 1969, which facilitate future growth.

At this time the Board of Directors and the management of FEDECACES feels that the credit union movement is at a critical point of development, because:

- a) We have a structure in place, carefully built over the past five years, with adequate pilot experience to be able to function satisfactorily;
- b) We are providing credit to lower income groups who have not had access to credit before but in very limited amounts. And more importantly thousands of people are participating in these voluntary private credit unions, which are practical laboratories for overall personal development;

c) We are anxious to extend our services to more people and involve many more thousands in this cooperative movements and at the same time move toward a self sustaining position.

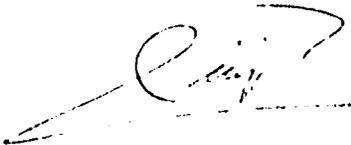
But to pursue our aims we are critically short of working capital at both the Federation and credit union levels. The Federations' volume of operations is far below the break even point and in order to operate under present conditions we need a subsidy. The individual credit unions lack volume and income and this prohibits their having professional full time management which could actively promote new members and services and further strengthen and extend the system.

In view of the above the Board of Directors authorized me to explore the possibility of an A.I.D. loan. This authorization is found in the Minutes of the Board's meeting of February 11, 1970. Therefore, I hereby apply to A.I.D. for a loan to assist in the development of the credit union system in El Salvador, at A.I.D.'s most concessional terms, in an estimated amount of \$2,000,000.00. A more precise loan figure will be forthcoming as our operational projections for 1971 - 3, (the proposed disbursement period,) are refined.

As attachments to this letter I am pleased to forward details about the Federation's organization, administration, legal basis, operations, financial statements and other details.

We will be happy to supply you with any other information you may need to help you evaluate our application.

Sincerely yours,



Dr. LUIS E. GUTIERREZ
Manager.

LEG/mef.

AID LOAN APPLICATION
(Attachment I to Fedecaces Letters)
of February 16, and 24, 1970

1. Borrower: "Federación de Cooperativas de Ahorro y Crédito de El Salvador" (FEDECACES)
2. Address: Edificio Luz
1a Diagonal y 25 Avenida Norte,
Apartado Postal #156
San Salvador, El Salvador, Central America
Tel. 25-3023, 25-3035, 25-3037
3. Present Financial Operations: Include limited short term loans to credit unions for agricultural operating capital sub-loans accompanied by technical assistance and two year loans to credit unions (limit \$2, 000) for Credit Union sub-lending. (See Supplement No. 6)
4. Legal Basis: Fedecaces is a juridical person authorized to function under the Ministry of Interior (See Supplement 2, By-laws, Official GOES Authorization)
5. The Federation is a cooperative that operates in the same manner as a Credit Union League in the U. S. and has the same basic philosophy and method of operation. In contrast with other credit institutions in El Salvador, the primary guarantee for the loans is the character of the member. The formation of capital through savings and the use of this capital to help meet the members credit needs is the basis of the credit union. The credit union can also act as an intermediary for the members in order to secure credit from sources to which the member does not have access.
6. FEDECACES has affiliated credit unions throughout the country of El Salvador (See Annex II-C)
7. The capital of the Federation consists of shares of \$20.00 each, which member credit unions own. As of December 31, 1969 the assets of the Federation amounted to \$31,400. As of the same date the Federation had accounts payable of \$20,860 and paid in capital of \$4,730 for a net worth of \$55,810.
8. Balance Sheets (See Annex II-D)
9. The organizational structure of Fedecaces (See Attachment 2)

UNCLASSIFIED

10. Credit Unions that Founded FEDECACES. (See Attachment 3)
11. Fedecaces Institutional Relationships. (See Attachment 4)
12. Biographic Data of Directors:

President: Efraín Romero Canahuati, 53, Salvadoran, Farmer, Administrator of the Tenancingo Cajas de Crédito (1943-1947) Accountant and Manager, Tenancingo Cajas de Crédito, (1948-Present), General studies on administration and cooperative accounting (1944), and loans and credit analysis (1944).

Secretary: Rubén Godofredo Ramírez, 36 Salvadoran, Secretary of National Circuit of Theaters, B. A., Faculty of Humanities, University of El Salvador, College studies in Humanities, also studies in Administration, analysis and human relations. Has been Director of various cooperatives.

Director: Gustavo Adolfo Caballero, 40, Salvadoran, High School, Inspector of Roads and Streets and Chief of Garbage Disposal Services - Santa Ana.

Director: Francisco Abraham Escobar, 36, Primary School Teacher, employee of Ministry of Education, has been both Director and teacher of various primary schools. Additional studies in cooperatives, nutrition and agriculture.

Director: Mauricio Salinas Sandoval, 35 Salvadoran, Agronomist, Has been agricultural administrator and is presently a consulting agronomist.

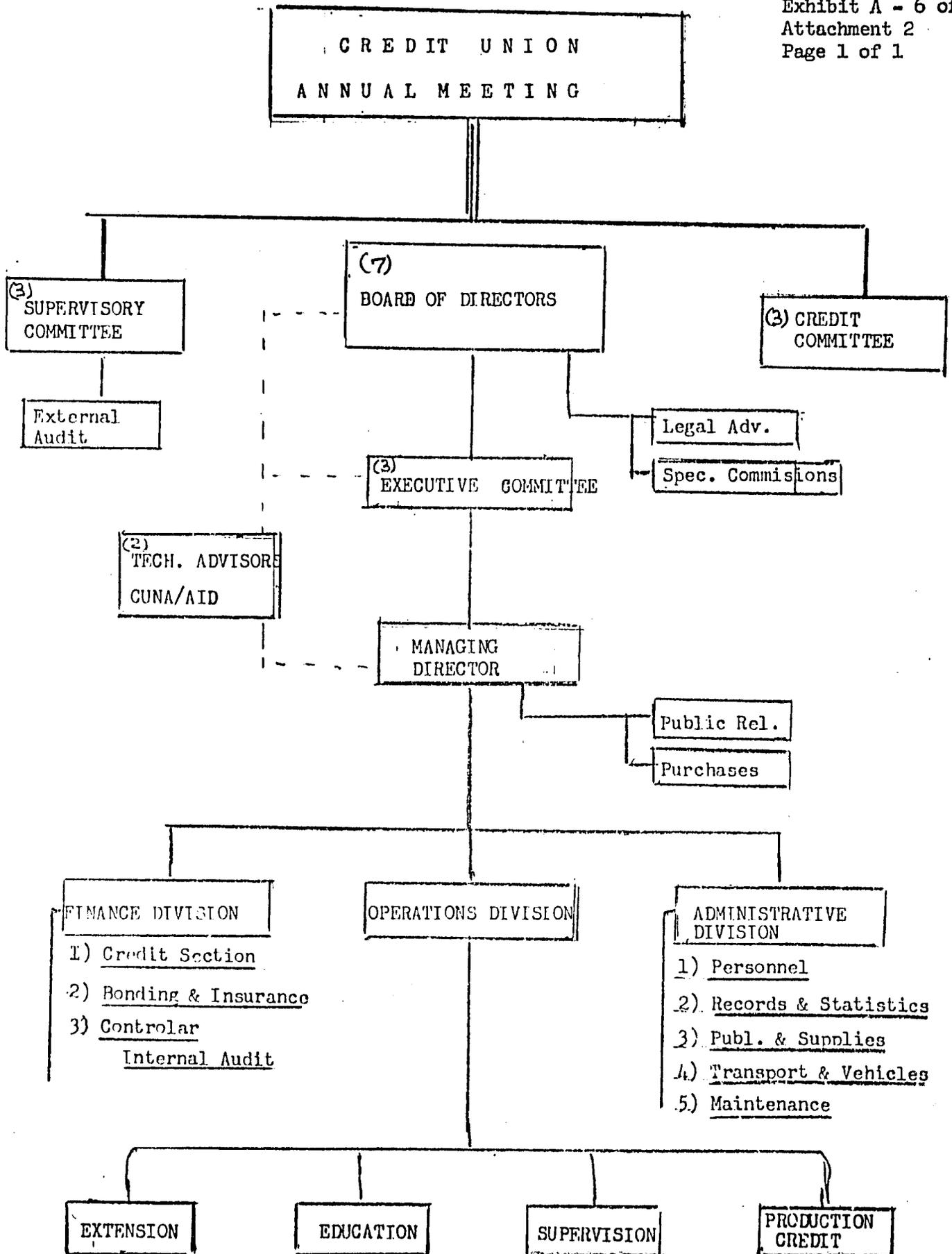
Director: Eufrasio Ferrufino Méndez, 38, Salvadoran, Primary School Teacher and Ass't Director of the Boys School of Santa Elena. Active in several cooperatives and civic associations.

13. Biographic Data: Manager
Luis E. Gutiérrez, 54, Salvadoran, Economist, B. A. and M. A. in Economics at McGill University, Canada and N. Y. U. respectively. 14 years in Foreign Service of El Salvador as vice consul, consul and consul general (1944-1958) Superintendent of Bank of El Salvador, Economic Consultant to INSAFI and Professor of Economics and Finance at the University of El Salvador. Serves 3 Boards of Directors of various organizations.

UNCLASSIFIED

FEDACE S ORGANIZATIONAL CHART

UNCLASSIFIED
ANNEX II
Exhibit A - 6 of 9
Attachment 2
Page 1 of 1



CHARTER MEMBERS OF FENEGACSE

- | | | |
|-----|--|--------|
| 1. | Ahorro y Crédito de Tenancingo | Rural |
| 2. | Magisterial de Iobasco | Rural |
| 3. | Comunal Agua Caliente | Rural |
| 4. | Comunal Tacuba | Rural |
| 5. | Magisterial de Tejutepeque | Rural |
| 6. | Comunal de San Juan Tepezontes | Rural |
| 7. | Magisterial Alberto Masferrer de Tejutla | Rural |
| 8. | Magisterial "22 de Junio" de Quetzaltepeque | Urbana |
| 9. | Magisterial Armeniense | Urbana |
| 10. | De Empleados Municipales de Santa Ana | Urbana |
| 11. | Comunal San Rafael, Santa Ana | Urbana |
| 12. | EE y TT Beneficio "LA MICA" | Urbana |
| 13. | Magisterial "Dr. J. Antonio Ruiz" San Sebastián | Urbana |
| 14. | Comunal de la Aldeíta | Rural |
| 15. | Empleados Educación Fundamental | Urbana |
| 16. | Pro-Reinvindicación Gremial Nueva S. S. | Urbana |
| 17. | Mercado No. 2 de Santa Ana | Urbana |
| 18. | Magisterial "Profesor J. A. Anaya Mantec" Jayaque | Urbana |
| 19. | Parroquial de Nueva Concepción | Rural |
| 20. | Comunal de Tapalhuaca | Rural |
| 21. | Comunal La Paz | Rural |
| 22. | De Empleados de A. L. D. | Urbana |
| 23. | "Alfonso Verduzco" de Aguilares | Rural |
| 24. | Comunal Colonia Posada - San Salvador | Urbana |
| 25. | San Rafael - Coatepeque | Rural |
| 26. | Comunal San Sebastián - Zacatecoluca | Urbana |
| 27. | Nuestra Señora de Lourdes - San Salvador | Urbana |
| 28. | Comunal San José Villanueva | Rural |
| 29. | Crédito Agrícola de Tejutla | Rural |
| 30. | Trabajadores "Fosforos Nueva San Salvador" | Urbana |
| 31. | Magisterial "12 de Octubre - Suchitlan" | Urbana |
| 32. | Magisterial "Franciso Gavidia" Dulce Nombre de María | Urbana |
| 33. | Magisterial Chalateca | Urbana |
| 34. | Comunal "La Reina" | Rural |
| 35. | La Constancia - Santa Ana | Urbana |
| 36. | Unidad de Salud - Santa Ana | Urbana |
| 37. | Comunal "Natividad" Santa Ana | Urbana |

UNCLASSIFIED

INDEX II

Exhibit A - Page 8 of 9

Attachment 3 - Page 2 of 2

38. ...
39. ...
40. ...
41. ...
42. ...
43. ...
44. ...
45. ...
46. ...
47. ...
48. ...
49. ...

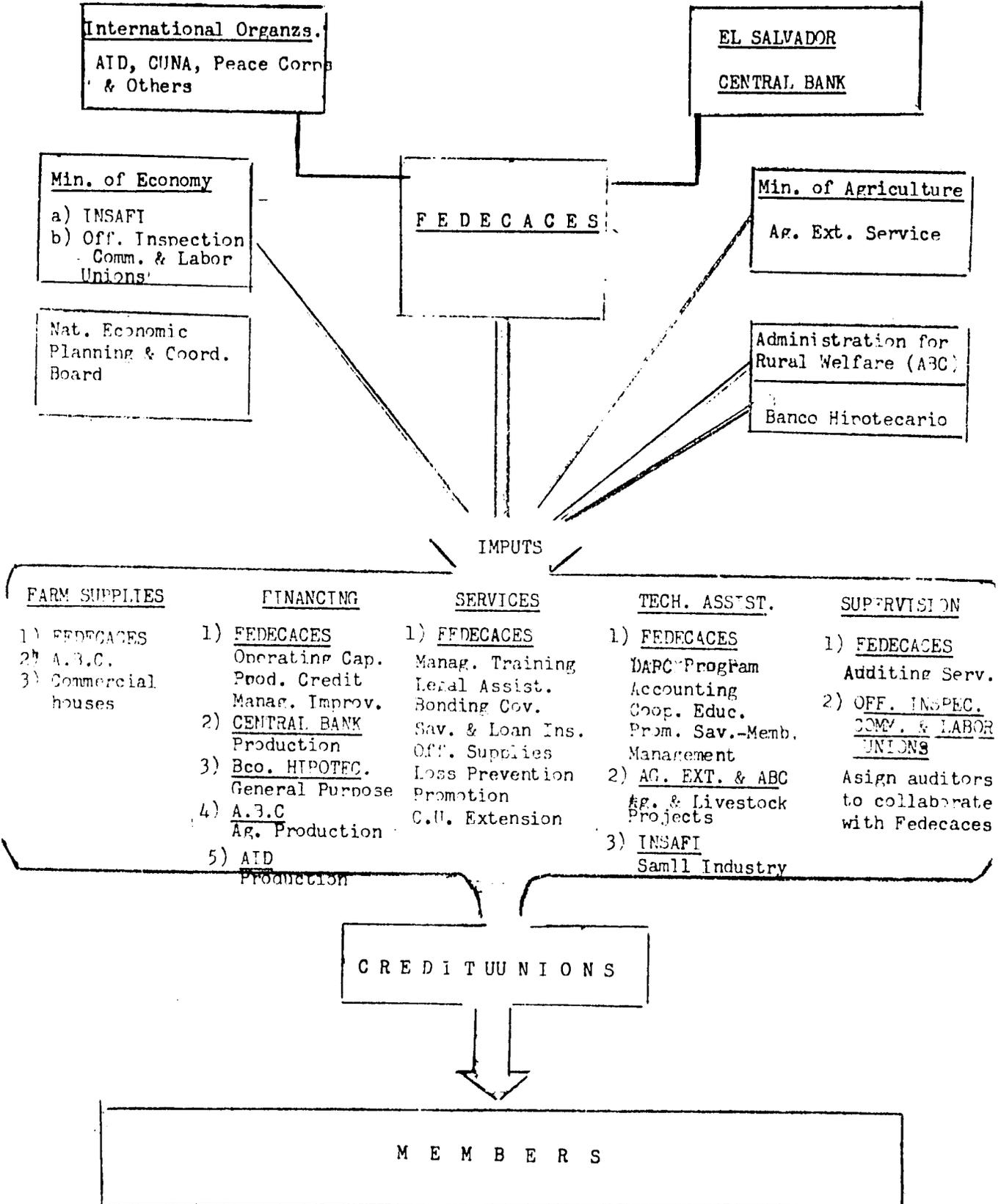
Urbana
Urbana
Urbana
Urbana
Urbana
Rural
Urbana
Urbana
Urbana
Urbana
Urbana
Urbana

UNCLASSIFIED

F E D E C A C E S
I N S T I T U T I O N A L R E L A T I O N S H I P S

ANNEX II
Exhibit A - 9 of 9
Attach 4 - Pg 1 of 1
Coordination
Imputs of loan funds
Tech. Assist & other.

LEGEND ---



SUMMARY OF CREDIT NEEDS OF CREDIT UNION SYSTEM

During the course of the intensive review Fedecaces conducted a survey among its affiliated credit unions to attempt to quantify the demand for credit over the next twelve months.

The following questions were asked:

1. How many credit applications are pending and what is the total amount?
2. If your credit union were to have additional resources available, what amount could be used by your members, in the following categories?
 - a. General purpose loans
 - b. Working capital loans
 - c. Fixed capital loans
 - d. Administrative improvement loans

49 credit unions of the 78 affiliated to Fedecaces, representing a total membership of 6,239, answered the questionnaire. This represents approximately 60% of the total system.

Projecting the credit needs of the total system (100%), the following results were obtained:

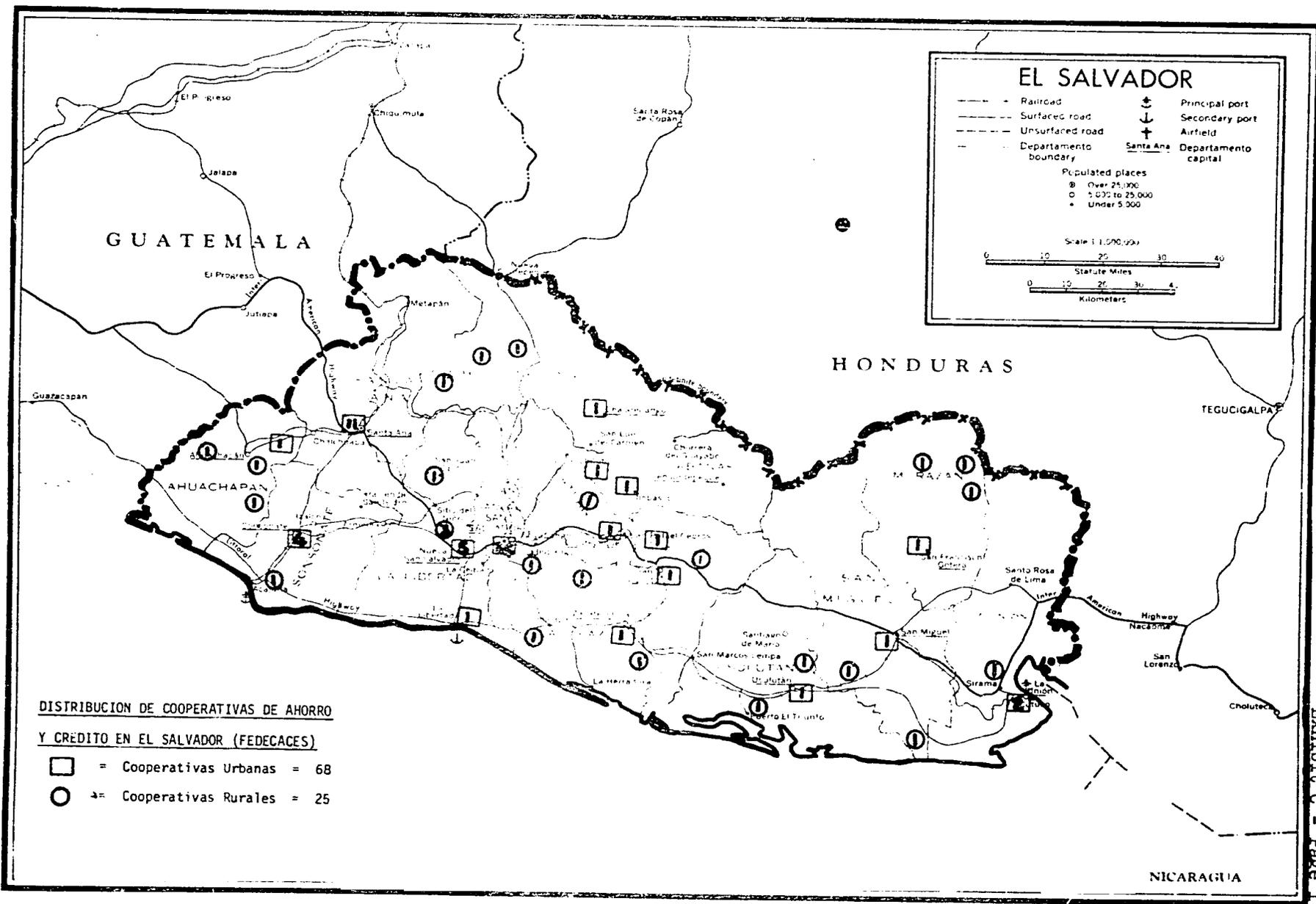
1. Credit applications pending: 870
2. Amount of pending applications: \$206,000
3. Twelve months needs:

UNCLASSIFIED

ANNEX II
Exhibit B, Page 2 of 2

<u>TYPE</u>	<u>Am^t. (millions)</u>	<u>%</u>
(a) General Purpose	\$1.7	33%
(b) Working Capital	1.4	28%
(c) Fixed Capital	1.6	32%
(d) Management Improvement	0.3	7%
	<u>\$5.0</u>	<u>100%</u>

The survey detail is available in Supplement 5.



EL SALVADOR

<ul style="list-style-type: none"> —+— Railroad — Surface road - - - Unsurfaced road - - - Departamento boundary 	<ul style="list-style-type: none"> ⚓ Principal port ⚓ Secondary port ✈ Airfield ⚓ Santa Ana Departamento capital 	<p>Populated places</p> <ul style="list-style-type: none"> ⊙ Over 25,000 ○ 5,000 to 25,000 • Under 5,000
--	--	---

Scale 1:1,000,000

0 10 20 30 40
Statute Miles

0 10 20 30 40
Kilometers

DISTRIBUCION DE COOPERATIVAS DE AHORRO

Y CREDITO EN EL SALVADOR (FEDECACES)

- = Cooperativas Urbanas = 68
- = Cooperativas Rurales = 25

UNCLASSIFIED

AID-DIC/P-890
ANNEX II
Exhibit C - Page 1 of 1

F E D E C A C E S

STATEMENT OF OPERATIONS (1966 -- 1969 Actual)
 STATEMENT OF OPERATIONS (1970 -- 1975 Projected)
 (In thousands of U.S. Dollar Equivalents)

	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975
INCOME										
Interest on Loans			.3	2.8	14.9	87.6	205.2	303.9	349.0	360.0
Affiliated Credit Union Dues	.5	2.2	3.5	5.2	8.5	12.4	18.2	29.5	44.5	64.0
Investments				.4	1.0	2.5	4.0	15.0	15.0	15.0
Sales of Supplies				3.3	4.5	6.1	8.1	9.5	11.7	14.7
Other Income	.2	.3	6.4	3.9	5.1	6.3	7.4	8.5	9.7	10.8
TOTAL INCOME	0.7	2.5	10.2	15.6	34.0	114.9	242.9	366.4	429.9	464.5
EXPENSES										
Operating Expenses	37.2	35.1	38.2	90.6	141.6	172.6	201.3	224.1	245.6	259.9
Depreciation			.3	.9	11.5	16.7	16.7	16.7	17.3	17.9
Interest on Borrowings										
1) AID Loan						19.0	40.0	40.0	40.0	40.0
2) E.S. Central Bank - Class A					4.0	6.0	6.0	6.0	6.0	6.0
3) E.S. Central Bank - Dev. Fund							13.7	37.0	65.5	68.0
4) Other				.8	1.4	-	-	-	-	-
TOTAL EXPENSES	37.2	35.1	38.5	92.3	158.5	214.3	277.7	323.8	374.4	391.8
NET OPERATING GAIN/LOSS (1)	<u>(36.5)</u>	<u>(32.6)</u>	<u>(28.3)</u>	<u>(76.7)</u>	<u>(124.5)</u>	<u>(99.4)</u>	<u>(34.8)</u>	42.6	55.5	72.7

(1) Net operating losses will be offset by AID grants through 1970, after which the AID loan becomes operative and any subsequent losses will be capitalized as a deferred expansion expense.

A.I.D. GRANTS TO FEDECACES 1966 - 1974

(In thousands of US\$ equivalents)

1966	Actual	68.2
1967	"	58.7
1968	"	74.1
1969	"	167.0
1970	Programmed	158.5
<hr/>		
1971	"	50.0
1972	"	30.0
1973	"	30.0
1974	"	- 0 -
<hr/>		
	TOTAL	636.5

NOTE: Technical assistance grants for operations terminate with 1970 as the loan becomes operative. Thereafter, limited grants are provided to assure effective management consulting services during the loan disbursement period, 1971 - 1973.

F E D E C A C E S

ACTUAL BALANCE STATEMENT 1966 - 1969
PROJECTED BALANCE STATEMENTS 1970 - 1975
(In thousands of U.S.\$ Equivalents)

	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975
ASSETS										
Cash	.1	3.6	4.0	3.1	2.1	5.5	2.6	150.5	273.4	468.8
Accounts Receivable		.8	1.5	3.4	3.4	5.0	5.0	5.0	5.0	5.0
Loans Outstanding	1.7	1.5	13.7	47.8	247.9	1228.2	2742.8	3438.3	4313.4	4500.0
Investments				8.9	8.9	8.9	8.9	8.9	8.9	8.9
Inventory			.4	3.4	5.0	5.0	5.0	5.0	5.0	5.0
Office Equipment		.9	2.4	13.0	52.1	46.5	41.1	35.6	30.1	24.6
Vehicles					20.9	35.9	24.7	13.5	19.6	25.1
Deferred Assets				1.8	3.0	3.0	3.0	3.0	3.0	3.0
Deferred Losses						99.4	134.2	91.6	36.1	
TOTAL ASSETS	1.8	6.8	22.0	81.4	343.3	1437.4	2967.3	3751.4	4694.5	5040.4
LIABILITIES										
Debts in National Currency										
1) Accounts Payable			.4	28.2	28.3	12.4	12.4	12.4	12.4	12.4
2) E.S. Central Bank - Class A				200.0	300.0	300.0	300.0	300.0	300.0	300.0
3) E.S. Central Bank - Dev. Fund							341.3	925.8	1635.7	1700.0
Debts in Foreign Currency										
AID Loan						949.8	2000.0	2000.0	2000.0	2000.0
TOTAL LIABILITIES			.4	28.2	228.3	1262.2	2653.7	3238.2	3948.1	4012.4

	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975
CAPITAL & RESERVES										
Share Capital	.6	1.4	3.2	4.7	28.1	76.3	187.2	352.4	542.5	742.5
Donations	1.1	5.2	15.9	43.0	80.2	80.2	80.2	80.2	80.2	80.2
Legal Reserve	.1	.2	1.7	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Bad Debts Reserve			.8	3.8	5.0	11.0	24.8	42.0	63.5	86.0
M.O.V. Reserves						6.0	19.7	36.9	58.5	81.0
Undistributed Earnings			-	-	-	-	-	-	-	36.6
TOTAL CAPITAL & LIABILITIES	1.8	6.8	22.0	81.4	343.3	1437.4	2967.3	3751.4	4694.5	5040.4

DEPRECIATION SCHEDULE

<u>EQUIPMENT</u>	<u>1970</u>	<u>1971</u>	<u>1972</u>	<u>1973</u>	<u>1974</u>	<u>1975</u>
BALANCE-BEGINNING YEAR	12,957	52,029	46,546	41,063	35,580	30,097
NEW AQUISITIONS YEAR	41,555					
LESS DEPRECIATION	-5,483	-5,483	-5,483	-5,483	-5,483	-5,483
DEPRECIATED VALUE YEAR END	<u>52,029</u>	<u>46,546</u>	<u>41,063</u>	<u>35,580</u>	<u>30,097</u>	<u>24,614</u>
<u>VEHICLES</u>						
BALANCE BEGINNING YEAR	-0-	20,944	35,904	24,684	13,952	19,598
NEW AQUISITIONS YEAR	26,928				17,952	17,952
LESS DEPRECIATION	-5,984	-11,220	-11,220	-11,220	-11,818	12,416
DEPRECIATED VALUE YEAR END	<u>20,944</u>	<u>35,904</u>	<u>24,684</u>	<u>13,464</u>	<u>19,598</u>	<u>25,134</u>

F E D E C A C E S

PROJECTED CASH-FLOW 1970 -- 1974
(In Thousands of U.S. Dollar Equivalents)

	1970	1971	1972	1973	1974	1975
CASH RECEIVED FROM:						
Net Gain/Loss						
Depreciation	(124.5)	(99.4)	(34.8)	42.6	55.5	72.7
Increase in FEDECACES Share Capital (1)	11.5	16.7	16.7	16.7	17.3	17.9
Loan Repayment from Borrowers	23.4	48.2	110.9	165.2	190.1	200.0
Increase in Reserves	34.3	306.6	1,443.3	2,738.2	3,430.9	4,298.4
Increase in Accounts Payable	1.2	12.1	27.4	34.4	43.1	45.0
Proposed AID Loan	.1	-	-	-	-	-
Proposed AID Grants	-	949.8	1,050.2	-	-	-
Proposed AID Equipment Donations	124.5	-	-	-	-	-
E.S. Central Bank - Class A	37.2	-	-	-	-	-
E.S. Central Bank - Dev. Fund	200.0	300.0	300.0	300.0	300.0	300.0
	-	-	341.3	925.8	1,635.7	1,700.0
TOTAL CASH RECEIVED	<u>307.7</u>	<u>1,534.0</u>	<u>3,255.0</u>	<u>4,222.9</u>	<u>5,672.6</u>	<u>6,634.0</u>
CASH DISBURSED FOR:						
Loans to Borrowers						
Acquisition of Fixed Assets	234.4	1,286.9	2,957.9	3,433.7	4,306.0	4,485.0
Repayments of Borrowings	71.5	26.2	-	-	17.9	17.9
1) E.S. Central Bank -- Class A	-	-	-	-	-	-
2) E.S. Central Bank -- Dev. Fund	-	200.0	300.0	300.0	300.0	300.0
Decrease in Accounts Payable	-	-	-	341.3	925.8	1,635.7
Increase in Accounts Receivable	-	15.9	-	-	-	-
Increase in Deferred Assets	-	1.6	-	-	-	-
Increase in Inventories	1.2	-	-	-	-	-
	1.6	-	-	-	-	-
TOTAL CASH DISBURSED	<u>308.7</u>	<u>1,530.6</u>	<u>3,257.9</u>	<u>4,075.0</u>	<u>5,549.7</u>	<u>6,438.6</u>
INCREASE/DECREASE IN CASH	<u>(1.0)</u>	<u>3.4</u>	<u>(2.9)</u>	<u>147.9</u>	<u>122.9</u>	<u>195.4</u>
CASH BALANCE -- BEGINNING OF YEAR	<u>3.1</u>	<u>2.1</u>	<u>5.5</u>	<u>2.6</u>	<u>150.5</u>	<u>273.4</u>
CASH BALANCE -- END OF YEAR	<u>2.1</u>	<u>5.5</u>	<u>2.6</u>	<u>150.5</u>	<u>273.4</u>	<u>468.8</u>

(1) Affiliated credit union are required to increase their share capital in FEDECACES by 5



INTER-AMERICAN DEVELOPMENT BANK
WASHINGTON . D. C.

UNCLASSIFIED
AID-DLC/P-890
ANNEX II
Exhibit E - Page 1 of 3

January 6, 1970

CABLE ADDRESS
INTAMBANC

Mr. Robert Kanchuger
Bureau for Latin America
Office of Development Resources
Agency for International Development
Department of State
Washington, D.C. 20523

Dear Mr. Kanchuger

With reference to Mr. Kenneth Davidson's letter of November 26, 1969, regarding a proposed loan to FEDECACES, a non-profit private sector national credit union federation in El Salvador, we wish to inform you that the Bank is not considering at present any operation of this type in El Salvador

Sincerely yours,

Sidney Schmukler
Assistant Program Advisor



INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

1818 H Street, N.W., Washington, D. C. 20433, U.S.A.
Area Code 202 • Telephone - Executive 3 6370 • Cable Address - INTBAFRAD

*Development
office*

UNCLASSIFIED
ANNEX II
Exhibit E - Page 2 of 3

December 2, 1969

Mr. Kenneth Davidson
Bureau for Latin America
Office of Development Resources
Department of State
Agency for International Development,
Washington, D. C. 20523

Dear Mr. Davidson:

Referring to your letter of November 26, 1969, I am writing to advise you that the Bank is not interested in considering for financing the project in El Salvador mentioned in your letter.

Best regards,

Sincerely yours,

Gerald Alter
Director
Western Hemisphere Department

FEDECACES - Credit Union - IRR

MINUTES

Export-Import Bank - AID

811 Vermont Avenue, N. W. - Room 1206

December 11, 1969

PRESENT: Export-Import Bank
Seymour Pollack

AID
Harold Holt

The Eximbank representative stated that the Board of Directors had reviewed the following projects and decided to return them to AID for the reasons indicated. (See agenda of December 11, 1969.)

Colombia - Government of Colombia
(Mineral Resources Survey)

The feasibility of this project depends on concessional financing terms since it will not generate any earnings.

✓ El Salvador - "FEDUCACES" Credit Union
(Seed Capital Loan)

This project is not appropriate for Eximbank consideration since its purpose is to provide low cost seed capital and the loan will primarily finance loan costs.



CONSEJO NACIONAL DE PLANIFICACION
Y COORDINACION ECONOMICA

UNCLASSIFIED
AID-DLC/P-890
ANNEX II
Exhibit F - Page 1 of 2

SAN SALVADOR,
FEBRERO 26 DE 1970.

Dr. LUIS E. GUTIÉRREZ
GERENTE,
FEDERACIÓN DE COOPERATIVAS DE
AHORRO Y CRÉDITO DE EL SALVADOR,
EDIFICIO LUZ - 1er. PISO
FUENTE LUMINOSA Y 25 Av. Nte.
CIUDAD.

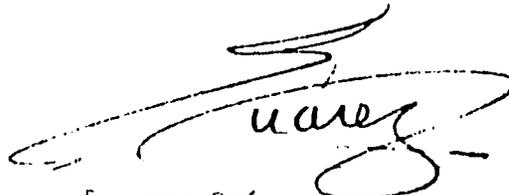
111413

TENGO EL AGRADO DE REFERIRME A SU ATENTA NOTA DEL 19 DE LOS CORRIENTES, ALUSIVA A LA VISITA QUE HE HICIERA EN FECHA RECIENTE, ACOMPAÑADO DEL SEÑOR KEN DAVIDSON, FUNCIONARIO DE AID, QUIEN LLEGÓ AL PAÍS PROCEDENTE DE WASHINGTON, D.C., CON EL OBJETO DE ESTUDIAR LA POSIBILIDAD DE QUE AQUEL ORGANISMO - OTORQUE UN CRÉDITO A FEDECACES, PARA QUE ÉSTA PUEDA FINANCIAR LAS NECESIDADES CREDITICIAS DE LOS SOCIOS DE LAS COOPERATIVAS AFILIADAS.

SOBRE DICHO PARTICULAR, ESTIMO OPORTUNO Y CONVENIENTE HACER DE SU CONOCIMIENTO LO SIGUIENTE:

- a) ESTA SECRETARÍA CONSIDERA DE SUMA IMPORTANCIA - UN FINANCIAMIENTO DE ESA NATURALEZA PUES CON -- ELLO SE CONTRIBUIRÍA AL DESARROLLO SOCIO-ECONÓMICO DE LOS SECTORES DE ESCASOS RECURSOS ECONÓMICOS DEL PAÍS.
- b) EL ACTUAL GOBIERNO Y EN CONSECUENCIA CONAPLAN - DAN SU PLENO APOYO AL MOVIMIENTO COOPERATIVISTA COMO UN MEDIO EFECTIVO PARA ACELERAR EL DESARROLLO ECONÓMICO DEL PAÍS.
- c) AUN CUANDO NO SE HAYA PROGRAMADO EN FORMA ESPECÍFICA Y CUANTITATIVA EL DESARROLLO DEL MOVIMIENTO COOPERATIVISTA, SE LE ESTÁ DANDO A ÉSTE TODO EL APOYO NECESARIO, ESPECIALMENTE A FEDECACES Y SUS COOPERATIVAS AFILIADAS A TRAVÉS DE LA COOPERACIÓN Y COORDINACIÓN DE DIFERENTES ORGANISMOS - GUBERNAMENTALES.

AL OFRECER NUESTRA COLABORACIÓN EN LO QUE ESTÉ A
NUESTRO ALCANCE, ME VALGO DE LA OPORTUNIDAD PARA SUSCRIBIRME CON
TODA CONSIDERACIÓN Y APRECIO.



EDGARDO SUÁREZ CONTRERAS,
SECRETARIO EJECUTIVO.



**BANCO CENTRAL DE RESERVA
DE EL SALVADOR**
1A. CALLE PONIENTE Y 7A. AVENIDA NORTE

UNCLASSIFIED
AID-DLC/P-890
ANNEX II
Exhibit G - Page 1 of 4

OFICINA DEL PRESIDENTE

San Salvador, 28 de octubre de 1969

Señores
Federación de Cooperativas de Ahorro
y Crédito de El Salvador (FEDECACES)
Presente.

7000

Estimados señores:

Tengo mucho gusto en comunicar a ustedes que, con el fin de proporcionar el adecuado apoyo financiero al esfuerzo cooperativista que esa Federación está desarrollando, nuestra Junta Directiva en sesión No. JD-50/69, celebrada el 21 de octubre del corriente año, resolvió aprobar, con cargo a sus recursos ordinarios, una línea de crédito a FEDECACES, bajo las siguientes condiciones:

MONTO: \$500.000.00 (QUINIENTOS MIL COLONES).

PLAZO: Hasta un año a partir de la fecha de los respectivos retiros.

INTERES: 2% anual sobre saldos, sin que cobren al usuario final más del 12% anual.

DESTINO: El destino del presente crédito deberá ser de tipo productivo. Dentro de esta finalidad se financiarán actividades agrícolas e industriales que estén clasificadas como crédito clase "A" en nuestro Manual de Clasificación del Crédito por Actividad Económica.

FORMA DE PAGO: Al vencimiento, antes si los usuarios de FEDECACES efectúan pagos anticipados.

SUJETO DE CREDITO: Las Cooperativas afiliadas a FEDECACES; y los afiliados a las Cooperativas, a través de éstas.

**BANCO CENTRAL DE RESERVA
DE EL SALVADOR**

14. CALLE PONIENTE Y 74. AVENIDA NORTE

UNCLASSIFIED
ANNEX II
Exhibit G - Page 2 of 4
Hoja No. 2

OFICINA DEL PRESIDENTE

San Salvador, 28 de octubre de 1969

Señores
Federación de Cooperativas de Ahorro
y Crédito de El Salvador (FEDECACES)

GARANTIA:

La propia responsabilidad de FEDECACES y pagarés otorgados por las Cooperativas y los afiliados a las Cooperativas, a favor de FEDECACES, debidamente endosados a favor de este Banco Central. La suma de dichos pagarés no podrá ser inferior al 125% del saldo deudor.

CONTROL DEL CREDITO:

El Banco Central podrá mantener un representante en el Comité de Créditos de FEDECACES, para asegurar que los créditos concedidos estén de acuerdo a las normas. FEDECACES remitirá al Departamento de Crédito del Banco Central un informe mensual de las operaciones realizadas.

OTRAS CONDICIONES:

- a) La presente línea de crédito se utilizará de acuerdo a las normas de crédito vigentes de este Banco Central.
- b) El Banco Central se reserva el derecho de vigilar el cumplimiento de la debida utilización del crédito. Si se encuentra que algún préstamo contratado ha sido otorgado parcial o totalmente en contra de las normas, inmediatamente procederá a cargarlo en la cuenta de FEDECACES.
- c) FEDECACES deberá comprometerse a proporcionar la debida asistencia técnica a los usuarios, así como a efectuar el control adecuado que requieran los créditos concedidos.

**BANCO CENTRAL DE RESERVA
DE EL SALVADOR**
1A. CALLE PONIENTE Y 7A. AVENIDA NORTE

UNCLASSIFIED
ANNEX II
Exhibit G - Page 3 of 4
Hoja No. 3

OFICINA DEL PRESIDENTE

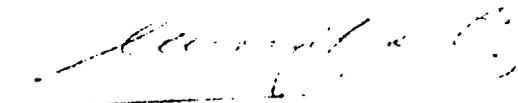
San Salvador, 28 de octubre de 1969

Señores
Federación de Cooperativas de Ahorro
y Crédito de El Salvador (FEDECACES)

- d) El Banco Central se reserva el derecho de suspender o dar por terminado el uso de la presente línea de crédito a - - FEDECACES, por incumplimiento de las estipulaciones establecidas por las presentes normas.

Para efectos de contratación, ruegole instruir a quien corresponda, se comunique con nuestros Departamentos de Crédito y Jurídico.

En espera que esa Federación utilice en la mejor forma posible los recursos puestos a su disposición, me es grato suscribirme de ustedes con toda consideración.


Alfonso Moisés Beatriz
Presidente

AMB:mlrl.

BANCO CENTRAL DE RESERVA
DE EL SALVADOR

14. CALLE PONIENTE Y 74. AVENIDA NORTE

UNCLASSIFIED
ANNEX II

Exhibit G - Page 4 of 4

OFICINA DEL PRESIDENTE

San Salvador, 10 de marzo de 1970

Señor Doctor don
Luis E. Gutiérrez, Gerente
Federación de Cooperativas de Ahorro
Crédito de El Salvador
Presente.

1636

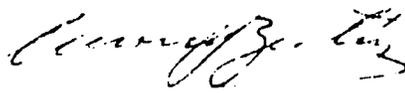
Señor Gerente:

Acuso recibo de su atenta nota fechada 20 de febrero pasado, en la que se refiere a la visita que usted me hiciera acompañado del señor Ken Davidson, Funcionario de AID, y me solicita le confirme los conceptos que en tal conversación expresó, en lo relativo a la canalización de recursos financieros a través de esa Federación, en favor de las Cooperativas afiliadas.

Sobre el particular, cumpliendo con sus deseos, gustosamente le confirmo la buena disposición que priva en este Banco Central por contribuir al fomento del movimiento cooperativista que promueve FEDECACES, en favor de la economía del país, y especialmente de los sectores Agrícola e Industrial. En prueba de lo antes expresado, como es de su conocimiento, nuestra Junta Directiva, después de conocer los estudios realizados al efecto, en sesión celebrada el 21 de octubre del año pasado, ha puesto a la disposición de esa Federación, una línea de crédito hasta por \$500.000.00 en condiciones favorables, la que servirá para financiar diversas actividades productivas.

En mi opinión, el buen aprovechamiento que se haga de las facilidades crediticias que les ha concedido este Banco Central, así como el debido cumplimiento de las obligaciones derivadas, servirán de respaldo para que en el futuro se pueda intensificar la asistencia financiera que ya se ha iniciado.

En espera de que la presente satisfaga su requerimiento, hago propicia la ocasión para renovarle las muestras de mi consideración y estima.


Alfonso Moisés Beatriz
Presidente

AMB:mlrl.



AGRICULTURAL CREDIT INSTITUTIONS

(By Clark Joel, Nathan Associates)

The purpose of this preliminary draft is to outline the existing institutional setup for channeling credit to the agricultural sector. A very detailed study of this subject (El Crédito Agrícola en El Salvador) was published in 1967 by the Grupo Permanente de Trabajo del Organismo Nacional, with technical assistance by experts from the Ministry of Economy, the Banco Hipotecario, and the Inter-American Bank. This memorandum aims only, as a first step, at summarizing the basic information in Vol. I, which runs to over 600 pages. I have also drawn on the Five-Year Plan for 1968-72 by the Ministry of Agriculture and Livestock, which contains pertinent information on the agricultural credit situation. No rechecking of the facts described or of the views expressed in these two documents has been undertaken ofar.

This paper is designed to provide the following information on each of the various organizations involved in extending agricultural credit: (1) sources of its funds; (2) the groups that are the major beneficiaries of the credit; (3) the exact purpose of the loan; and finally, (4) the shortcomings of the credit institution in terms of meeting the needs of the groups they are serving and in terms of fulfilling the broad requirements of the agricultural sector for working capital and for medium and long-term credits to finance expansion in productive capacity.

The following section summarizes the major deficiencies of the institutional agricultural credit structure as described in El Crédito Agrícola en El Salvador. It should be borne in mind that these deficiencies: a) are general deficiencies that characterize the agricultural credit setup as a whole, and do not necessarily apply to all agricultural credit institutions; b) refer to the situation that prevailed in 1965-67.

The major shortcomings of the agricultural credit system are summarized under three headings: 1) Institutional Sources of Credit; 2) Non-Institutional Sources of Credit; 3) Special Credit Programs.

a) Shortcomings of Institutional Sources of Credit (e.g. ABC, Cajas de Crédito, Central Bank, Banco Hipotecario, commercial banks etc.)

ANNEX II
EXHIBIT H

- 1) An overwhelming proportion of the credit made available by the formal institutions is for working capital. Conversely, the proportion made available to finance expansion and modernization of productive capacity is significantly below requirements.
- 2) The terms granted to farmers do not correspond to the farmer's requirements: Short-term credit is often granted when medium-term credit is required; the schedule of disbursements and repayments does not coincide with the "biological cycle", i.e. with the credit needs and repayment capacity of the farmer.
- 3) An overwhelming proportion of the total credit made available to agriculture goes to finance the traditional export crops - coffee, cotton and sugar; the/ ^{so} called subsistence or food crops are starved of credit funds.
- 4) Lack of initiative and dynamism on the part of the credit institutions. They generally follow a conservative approach designed to minimize risks. With the exception of institutions such as the ABC and the Cajas de Crédito, the credit system strongly favors the large and affluent borrowers because of credit standing, type of collateral they can pledge and the big-family ownership pattern that characterizes the commercial banking system.
- 5) Over-emphasis on real estate as collateral (and a concomitant reluctance to accept the pledging of crops or livestock as security) discriminates against competent small and medium-size farmers; it also means that the credit obtained is often not used for the purpose for which it was borrowed.
- 6) Shortage of overall financial resources; this together with the maldistribution of credit in favor of the export sector and the large landowners, compels medium and small-size farmers to borrow from private non-institutional sources at much higher cost.
- 7) Shortage of qualified technical personnel and absence of agricultural research (e.g. on the best potential uses of various types of land) and feasibility studies to serve as basis for loans.
- 8) Failure, particularly on the part of the commercial banking

ANNEX II
Exhibit H

system, to make loans available on the terms specified under the special programs of MEGA, META, and the Fondo de Desarrollo Económico of the Central Bank.

9) Very slow processing of loan papers and excessive centralization of decision-making. This causes loans to be untimely with respect to the needs of the recipient. Moreover, forms to be completed are often identical to those required of applicants for industrial credit, and are thus poorly suited for the purposes of the agricultural sector.

b) Deficiencies of Non-Institutional Sources of Credit (private suppliers of agricultural inputs and supplies, processors and exporters of coffee and sugar, commercial firms and private money lenders).

1) Credit is almost always short-term and for operating capital only, except in the case of sellers of costly agricultural equipment. In the latter case, terms are still relatively short - a maximum of three years.

2) Interest charges are relatively high, amounting, on the average, to 3½% above the commercial bank rate.

3) Credit extended by processors and exporters of coffee, sugar and honey is often part of a sales contract, binding the producer to sell his products at an agreed price which is frequently lower than that obtainable in the market. This has led some producers into serious financial difficulties.

4) Credit extended from these sources is quite insufficient to meet the need of small and medium-size farmers.

Nonetheless, these private suppliers of credit fulfill an important role owing to the wide gap left by institutional sources.

c) Shortcomings of special agricultural credit programs (META, MEGA, MEPO and the Fondo de Desarrollo Económico del Banco Central. These programs utilize the formal channels discussed under a) above as financial intermediaries).

1) Shortage of qualified technical personnel.

ANNEX II
Exhibit H

2) Failure to exercise effective control over the final use to which the funds are put.

3) The practice of leaving it up to the financial intermediaries to apply their own criteria with regard to choice of collateral, terms of loans, schedule of disbursements and repayments, choice of beneficiaries, etc. The standards of these financial institutions often conflict with those of the program itself.

4) Failure to establish proper coordination between the technical and financial aspects of the program: Technicians have often realized feasibility studies which have failed to result in loans owing to lack of loan funds or to the credit standards applied by the banks.

5) Absence of necessary research projects to determine the technical and economic feasibility of irrigation projects in the area of livestock development (especially MEFU).

6) Poor planning and follow-up on investment projects. This, as well as point 4 above, is related to the shortage of qualified technical personnel.

7) Failure to maintain proper coordination between the various agricultural programs, the Planning Council, the Ministry of Agriculture and Livestock and the various specialized organizations capable of supplying technical assistance.

I. INSTITUTIONAL SOURCES OF CREDIT

ORGANIZATION : ABC

RECEIVES FUNDS FROM

AID, annual Government budgetary appropriations, Government funds to finance META and MEGA programs, and recovering of previously made loans.

CHANNELS FUNDS TO

Small and medium-size farmers.

FOR PURPOSE OF

Ninety to ninety-three percent of its loans have gone for short-term credits to provide working capital (balance for fixed capital). Provides supervised credit when necessary. ABC extends credit for most agricultural uses - cotton, sugar cane, cereals, fruits and vegetables, pastures, livestock (especially cattle), aviculture and apiculture. Most important: cotton, corn and rice (the combined total of these three made up almost 90% of the total credit extended to the "Sub-sector agrícola" in 1966 and 1967).

SHORTCOMINGS

- 1) Did not have the required number and quality of extension workers.
- 2) Did not limit its operations to selected priority areas, extended instead its operations to the whole national territory.
- 3) Followed unscrupulous policies during the first years of its operations (this shortcoming has been largely corrected in recent years).
- 4) Concentrated on financing particular agricultural crops or activities of borrowers without analyzing their overall credit requirements and output and repayment potential (Volume I, page xvii of El Crédito Agrícola).
- 5) Failure to make loans for "basic credit", i.e. for purposes

ANNEX II
Exhibit H

such as rural housing, integration of minifarms, refinancing of debts, rural hygiene, soil improvement; in other words, the ABC failed to provide financial assistance to remedy the general problems of rural families resulting from the whole complex of socio-economic causes (page xvii). Loans are made to submarginal farmers without first ensuring that they are free from problems that interfere with their ability to produce and repay the loan.

6) Loans are often too small and for periods too short (page xviii).

7) The decision-making process is over-centralized (all loans above ¢2,000 must be approved by the central office), thus causing delays, inefficiencies, and inadequate attention to planning.

ORGANIZATION: Banco Hipotecario

RECEIVES FUNDS FROM:

Its capital (¢900,000) was contributed by the government in 1935. The shares are presently held by the Asociación Cafetalera de El Salvador (70%), Asociación de Ganaderos de El Salvador (20%) and private shareholders (10%): The Bank also accepts demand and time deposits. In addition, the Bank receives public funds to help carry out special programs such as META, MEGA, and the Fondo de Desarrollo Económico of the Central Bank.

CHANNELS FUNDS TO:

Mostly to large farmers and intermediarios able to pledge excellent collateral, generally in the form of real estate mortgages.

FOR THE PURPOSE OF:

Mostly to provide short-term credits for working capital. Medium and long-term loans are made in connection with the special META and MEGA programs, and with the Fondo de Desarrollo.

SHORTCOMINGS

- 1) Lack of dynamism.
- 2) The Bank requires an excessive amount of collateral, mostly real estate mortgages.
- 3) The Bank is not oriented to bring about agricultural development and has no definite agricultural credit policy.

ANNEX II
Exhibit H

- 4) Slowness and inefficiency in processing loan applications.
- 5) Loans are highly concentrated in the hands of a few borrowers with access to other credit sources (an annual average of \$14.2 million in credit were loaned in only 78 credit transactions (page ix of El Crédito Agrícola).
- 6) Shuns investment credit designed to expand agricultural productive capacity, except for funds provided under the special investment programs.

ORGANIZATION: Commercial Banks

RECEIVE FUNDS FROM:

Own resources (mostly from depositors), public funds under MEGA and META, special credit lines set up by the Central Bank for cotton and coffee, and resources from the Fondo de Desarrollo Económico of the Central Bank.

CHANNEL FUNDS TO:

Mostly to large farmers and intermediaries, as evidenced by the high average loan figure granted (\$44,200 for the period 62-65).

FOR PURPOSE OF:

Mostly to provide working capital to finance the traditional crops. For the years 1966 and 1967, 72 to 76 percent of total credit extended by commercial banks to the sub-sector agrícola went to coffee, cotton and sugar. (Plan Quinquenal, Table 11-27).

SHORTCOMINGS

- 1) As most commercial banks are family-held banks, their loans have catered mainly to small groups and are not oriented towards the needs of social and economic development. Loans are highly concentrated. In 1964, 75% of the total volume of credit was concentrated into 6.7% of total credit transactions, which probably account for no more than 5% of the total number of customers served.

- 2) The type of collateral required, especially on real estate property - is the type that can best be financed by the larger farmers. The commercial banks are concerned in the security of the loan and not in the size of either the farmer or the bank.
- 3) Bank offices are not concentrated in the cities, particularly in the capital.
- 4) Agricultural credit is highly concentrated on the traditional export crops - coffee, cotton and sugar. Other crops are neglected as they involve larger risks.
- 5) Credit is mostly short-term and for working capital purposes only. Almost all investment credit is provided through the FIDE granted under special government programs and the Fondo de Desarrollo of the Central Bank.

ORGANIZATION:

Central Bank (Banco Hipotecario de Guatemala) which is organized separately under law.

RECEIVES FUNDS FROM:

Own resources (its capital, deposits of commercial banks, the government and autonomous institutions), and credits from abroad, including foreign banks and international lending institutions. The Central Bank also acts as fiscal agent for the government in channelling MEGA, META and MEPO funds to the financial institutions (El Crédito Agrícola, page 63).

CHANNELS FUNDS TO:

Short-term funds are channeled mostly to commercial banks and the Banco Hipotecario through special lines of credit; these reflect the amounts of rediscounts the Central Bank is prepared to approve to finance particular activities.

FOR PURPOSE OF:

The Central Bank uses special lines of credit mostly to provide short-term operating funds to finance the cultivation, processing and marketing of cotton; and the processing and marketing of coffee and sugar. Credit for other crops is negligible (ibid, pages 77-78). The task of providing investment funds is left to long-term loans obtained from foreign lending institutions, special agricultural programs partly financed by foreign funds; and to the resources in the Central Bank's Fondo de Desarrollo (discussed separately below).

ANNEX II
Exhibit H

SHORTCOMINGS:

- 1) Very slow processing of loan papers and excessive centralization of decision-making.
- 2) Quotas set by Central Bank on the amounts commercial banks can lend for "commercial" (as opposed to "productive") purposes have adversely affected the production and distribution of agricultural commodities (Ibid, pages vi-vii).
- 3) Excessive rigidity also characterizes the terms of repayment granted which are often not consonant with the biological cycle and have generated financial difficulties for the borrowers (Ibid., iv-v).
- 4) Heavy emphasis on the financing of coffee and cotton at the expense of other agricultural sectors (page vi).

ORGANIZATION: Federación de Cajas de Crédito Rural

RECEIVES FUNDS FROM:

The Federation's original capital of \$201,600 in 1943 was obtained as follows: from the Mejoramiento Social (an institution now extinct) \$100,000; from the Banco Hipotecario, \$100,000; and from the 16 Cajas or local cooperatives, only \$1,600. The capital of the individual Cajas or Coops varies, depending on the contribution of its members. Value of shares is \$10 and no member can own shares exceeding \$3,000, except for the autonomous public institutions.

CHANNELS FUNDS TO:

Small and medium-size members of the credit union

FOR PURPOSE OF:

Debt refinancing, provision of working capital, purchase of land and other rural property, and financing of domestic needs (education, medical assistance, etc.). (El Crédito Agrícola, p. 166).

SHORTCOMINGS

- 1) The Federation failed to display initiative and dynamism, and made no attempt to change the structure or mode of operation of small and medium-size agricultural enterprises.

ANNEX II
Exhibit H

- 2) The Federation failed to establish cooperatives in the geographical areas of greatest need.
- 3) It ignored some of the basic principles of cooperative organization (such as democratic government, education of members, distribution of excess resources in accordance with services rendered by the members, etc.).
- 4) The Federation has operated without an agricultural development plan or investment policy.
- 5) Made loans without prior investigation of the current and potential productive and repayment capacity of borrowers.
- 6) Only a small proportion of credit extended is of the investment type.

ORGANIZATION: INSAFI

RECEIVES FUNDS FROM:

Government budget, loans from international institutions, repayments of previous loans. Capital owned entirely by the Government.

CHANNELS FUNDS TO:

Industrial enterprises. Does not lend to agricultural enterprises as such, except small amounts for poultry development. Most of its loans are medium and long-term.

FOR PURPOSE OF:

Promote, increase, diversify and rationalize industrial promotion in the country. From the viewpoint of agriculture, it is significant only insofar as its activities promote the development of industries using agricultural products and supplying inputs to the agricultural sectors (e.g. textiles, food processing, fertilizers, insecticides).

SHORTCOMINGS

- 1) Lacks dynamism and follows a conservative policy, demanding ample and traditional types of collateral for its loans.

ANNEX II
Exhibit H

- 2) Lacks adequate financial resources and technical personnel.
- 3) Has failed to conduct needed feasibility studies.
- 4) Concentrated on banking-type operations while neglecting its primary function of creating new industries.
- 5) A large proportion of the Institute's resources are directed to large enterprises, while neglecting small businesses (El Crédito Agrícola, pages xxiv-xxv).

ORGANIZATION: Cooperativa Algodonera

RECEIVES FUNDS FROM:

Members of the Cooperativa, loans from the Central Bank and from foreign banks.

CHANNELS FUNDS TO:

Cotton producers, processors and exporters that are members of the Cooperativa.

FOR PURPOSE OF:

The credit is mostly designed to enable the Cooperativa to pay producers at the time they deliver the cotton to the Cooperativa's ginning mills and warehouses. The Cooperative also provides credit in kind - for chemical fertilizers, seeds, insecticides and aerial spraying (El Crédito Agrícola, Volume II, page 499).

SHORTCOMINGS:

The credit serves the limited purpose of providing short-term funds to supplement the working capital of cotton growers, processors, and exporters.

**ANNEX II
Exhibit H**

ORGANIZATION: **Compañía Salvadoreña de Café**

RECEIVES FUNDS FROM:

Original capital of \$252,000 distributed as follows: \$180,000 to Asociación Cafetalera de El Salvador; \$60,000 to Banco Hipotecario and \$12,000 to private shareholders. El Fondo Regulador del Café was set up at the same time to be managed by the company for the purpose of stabilizing national coffee prices. This fund was constituted on the basis of the profits of the Asociación Cafetalera and with the resources of the Banco Hipotecario. As coffee prices rose in subsequent years, the Fondo was not required for purposes of price stabilization and it could be used for the granting of loans to coffee processors, exporters and producers. Additional resources for the Compañía are obtained regularly through the capitalization of part of the profits of the Compañía. In addition, loans may be obtained from domestic or foreign banks. Loans made by domestic banks are generally rediscounted, at least in part, by the Central Bank.

CHANNELS FUNDS TO:

Mostly to large coffee processors and exporters (two-thirds of the total credit extended in 1966 went to this group). More recently and to a lesser extent, credit has been extended to coffee cooperatives.

FOR PURPOSE OF:

Enabling the processor-exporters to purchase coffee or to extend credit to coffee producers. Credit is short-term and for the purpose of supplementing working capital. The funds loaned to the processor-exporters are used to purchase coffee or advanced to coffee producers as part of a purchase contract (with the future coffee crop pledged as collateral). The Compañía also makes such loans directly to producers. Loans for debt refinancing are made in some instances. No investment credit is granted.

resources as well as with resources obtained from national and foreign credit institutions. While manufacturing industry has first priority, 10% of its total loans have gone to agriculture and 15% to agrobusinesses (El Crédito Agrícola, page 434).

SHORTCOMINGS

The institution has made a substantial contribution to the financing of productive enterprises in the country, and placed \$17 million in a period of a year and eight months. The following shortcomings are noted:

- 1) The financing has been generally heavily concentrated on large enterprises. The small entrepreneur has been neglected.
- 2) The guarantees demanded have followed the traditional pattern, consisting almost entirely of real estate mortgages. Personal guarantees from individuals of known solvency and reputation have been accepted on occasion, but only for short-term operations.
- 3) The institution has not carried out its principal objective of helping to initiate new enterprises. These were to be turned over to independent private operators at a later date, with equity shares offered for sale to the general public.
- 4) From the viewpoint of agricultural development, a shortcoming is that most of the resources of the enterprise have gone to finance manufacturing industry. (page 445 of El Crédito Agrícola.)

ORGANIZATION:

ICR (Instituto de Colonización Rural)

RECEIVES FUNDS FROM:

Its capital was derived from the assets of the Junta Nacional de Defensa Social and from Mejoramiento Social, institutions now extinct. Additional increments to its capital were derived from investments realized during ICR's existence with subsidies from the State and its own revenues. Total present value of its capital is about \$12.5 million (El Crédito Agrícola, pages 29--292).

CHANNELS FUNDS TO:

Does not channel any funds. Its credit function is limited to

ANNEX II
Exhibit H

the distribution of lots and houses on credit to the settlers with provisions for payment in periodic installments. To satisfy other credit needs of settlers, ICR has acted as intermediary in attempting to obtain credit for them through the ABC, the Federación de Cajas de Crédito, and private banks.

FOR PURPOSE OF:

Improve living standards and the educational level of agricultural laborers; and increase agricultural production by means of a program of settlement of landless farmers and of land redistribution with the help of technical and credit assistance.

SHORTCOMINGS:

The ICR has no credit resources of its own and has often been unsuccessful in obtaining the credit needed by settlers from other institutions. Other deficiencies include:

- 1) Resources of the Institute are too small in relation to the problem at hand. While some redistribution of land has been effected, some settlers were resettled and various sanitary and educational facilities were erected, these activities bear no relationship to the magnitude of the problem.
- 2) The Institute has spread its activities over too many areas of rural welfare and agricultural development, thus diverting its resources from its principal objective, which is the purchase and distribution of lands.
- 3) In order to benefit the largest possible number of farmers, the Institute has distributed lots that are too small to support a rural family, a policy which has aggravated the problem posed by minifarms in the country (El Crédito Agrícola, pages 312-314).

ANNEX II
Exhibit H

II. NON-INSTITUTIONAL SOURCES OF CREDIT

ORGANIZATION: Commercial suppliers of agricultural inputs, including agricultural machinery and equipment

RECEIVE FUNDS FROM:

By order of importance: National credit institutions (mostly commercial banks); manufacturers and banks located abroad and from own resources (El Crédito Agrícola, pages xxxix and 504).

CHANNEL FUNDS TO:

Mostly to medium-size farmers, to a lesser extent small farmers, (the larger ones have access to commercial bank credit) (Ibid., pages xxxix and 499).

FOR PURPOSE OF:

Promoting the sale of agricultural inputs (fertilizers, seeds, insecticides, farm tools, etc.), and of agricultural machinery and equipment.

SHORTCOMINGS:

- 1) The cost of this type of financing is relatively high. While the nominal interest rate is reasonable, the manner of computing it and additional charges result in a total effective interest rate which is relatively high (about 3½% higher than the commercial bank rate).
- 2) The initial downpayment requirement removes the goods from the reach of many farmers. This is mainly the case for agricultural equipment.
- 3) This type of credit is not ideally designed for investment purposes, not only because of its high cost and downpayment requirements, but also because it is of relatively short duration. Thus, the maximum credit terms for heavy agricultural equipment

ANNEX II
Exhibit H

is three years. Nevertheless, this form of credit is performing a useful function in El Salvador. It has increased from \$17 million in 1961 to \$62 million in 1965. The credit offers the advantages of: (1) being directed to medium and small farmers which are neglected by most of the official institutions; (2) being obtainable with a minimum of red tape and delay; and (3) takes into account the reliability and repayment capacity of the borrower instead of relying exclusively on the security pledged as collateral (Ibid., pages xxxix and 507).

ORGANIZATION: Processors and exporters of coffee

RECEIVE FUNDS FROM:

By order of importance: own funds, commercial banks, and Banco Hipotecario, Compañía Salvadoreña de Café and foreign banks.

CHANNEL FUNDS TO:

Mainly to small coffee producers. Credit terms are short (less than a year). Credit from processors and exporters of coffee constituted 19% of total coffee credits from all sources extended during 1964/65.

FOR PURPOSE OF:

To insure themselves of an adequate supply of coffee for processing and export. Credit is granted as part of a sales contract - i.e. a pledge by producers to sell a stated amount at a given price or at a price to be set by agreement between the producer and purchaser at a later time. (The price will depend on the world price and on quota limitations). The coffee itself is pledged as collateral. The purpose of this credit is purely to provide working capital (pages 1 and 11, 511 and 521-522).

SHORTCOMINGS:

- 1) Cost of credit is significantly higher than from financial institutions. The interest rate is about 3½% above the commercial bank loan rate (the rate is generally between 9 to 10% a year).

ANNEX II
Exhibit H

- 2) Credit is limited to providing working capital, to increase productive capacity.
- 3) The system is conducive to lower prices for producers, a fact which has contributed to the insolvency of a number of coffee growers in the years 1961-62.

ORGANIZATION: Sugar Processing Plants and Exporters of Honey

RECEIVE FUNDS FROM:

Mostly own resources; are sometimes supplemented by credits from commercial banks and Banco Hipotecario; or from foreign firms and banks.

CHANNEL FUNDS TO:

Mostly to small, and to a lesser extent, to medium-size producers of sugar cane and honey.

FOR PURPOSE OF:

Assuring themselves a supply of the raw material at favorable prices
Loans on short terms exclusively for operating capital. Credit is extended as part of a purchase contract, with repayment of the loan at the time of delivery (El Crédito Agrícola, page 525).

SHORTCOMINGS:

- 1) The amount involved is small - only \$200,000 to \$360,000 a year.
- 2) Relatively high cost of credit - about 3½% above commercial bank loan charge.
- 3) This type of financing often results in lower prices to agricultural producers.
- 4) The credit is short-term and only for working capital purposes.

ANNEX II
Exhibit H

ORGANIZATION: Private Money Lenders and Merchants

RECEIVE FUNDS FROM:

Own resources, commercial banks and Banco Hipotecario, foreign firms and banks.

CHANNEL FUNDS TO:

Mostly small farmers unable to avail themselves of commercial bank loans or other types of institutional credit.

FOR PURPOSE OF:

- 1) Realizing profits from lending operations; 2) Assist agricultural producers in order to increase farm supplies available for sale.

SHORTCOMINGS:

This type of credit presently performs a useful function in El Salvador owing to the insufficiency of institutional credit available to small farmers and the many other shortcomings attending such credit noted above. Credit offered by private merchants and money lenders is characterized by speed, absence of red tape, convenience (the lender usually resides in the locality of the borrower), and the fact that the lender usually does not demand a real estate mortgage. Deficiencies include the high cost of credit in the form of high interest and other charges, and lower prices to the producers in many cases where the credit is part of a contract to deliver the crop. It is hoped that the development of institutional credit sources gradually will reduce the dependence by small and medium-size farmers on private lenders and merchants as major sources of credit.

ANNEX II
Exhibit H

III. SPECIAL AGRICULTURAL CREDIT PROGRAMS

The special credit programs described below use the institutional intermediaries described under I to distribute their credit resources. They do not have direct contact with ultimate users.

ORGANIZATION: META (Mejoramiento de Tierras Agrícolas)

RECEIVES FUNDS FROM:

Mostly from Government budget and AID.

CHANNEL FUNDS TO:

The program is intended for small and medium-size farmers; but in practice, most of the credit has gone to medium and large-size farmers (see data in El Crédito Agrícola, page 541). META channels its funds through Banco Hipotecario (40%), ABC (19%), commercial banks (19%), commercial banks (41%), (percentages for period from inception through Oct. 66, Ibid., p.539). The META program is administered by the Ministry of Agriculture and Livestock. The Central Bank, as fiscal agent for the government, administers the funds loaned by AID and rediscounts credits granted by the financial institutions participating in the program (page 539).

FOR PURPOSE OF:

Provide technical assistance and funds for conservation, drainage and irrigation work on small and medium-size farm properties for the purpose of increasing agricultural production, conserve national resources and improve cultivation techniques.

SHORTCOMINGS:

- 1) Shortage of qualified technical personnel, particularly irrigation and soil engineers.

ANNEX II
Exhibit H

- 2) Commercial banks have applied their own criteria with regard to acceptable collateral, timing on loans and repayments, choice of beneficiaries, terms, etc. These standards frequently conflict with the principles underlying the META program as spelled out in the "Manual de Operaciones" (see pages xlv, 542 and 566). Except for the Banco Hipotecario, other credit institutions have not cooperated satisfactorily (page xlvi). Note that all credit investigations of applicants are conducted by the financial institutions responsible, not by META personnel or by the Ministry of Agriculture.
- 3) Failure to establish proper coordination between the technical and financial aspects of the META program, due in part to factors 1) and 2) mentioned above.
- 4) Poor planning and control of investment project.
- 5) Absence of needed research programs: Research with respect to the irrigation appropriate for the various crops on different soils is indispensable to the proper functioning of the META program.
- 6) Absence of supplementary credit programs to promote effective utilization of the improvements resulting from the irrigation and drainage projects. (Page xlvi).
- 7) Neglect of conservation activities: About 90% of the loans made were utilized for irrigation and drainage, only 10% for soil conservation (page 564).

ORGANIZATION: MEGA

RECEIVES FUNDS FROM:

Government budget and AID.

CHANNELS FUNDS TO:

Funds are intended for small and medium-size owners of beef and dairy cattle. The maximum loan that can be extended to anyone borrower is \$30,000 (the original amount of \$10,000 was found to be too small). However, in practice, the larger livestock owners

ANNEX II
Exhibit H

have also benefited from the program through the device of having various members of the family negotiate separate loans (El Crédito Agrícola, page 586). While the program does not require the beneficiaries to be landowners, in practice, the program has greatly favored this group since all financial institutions with the exception of ABC have demanded real estate mortgages as securities for loans. The credit is channeled through the Banco Hipotecario, the commercial banks, the Federación de Cajas de Crédito and the ABC. (The ABC and the Banco Hipotecario are the most important, channeling 43.5% and 25.8%, respectively of the credit extended under MEGA up to September 30, 1966). MEGA funds are administered by the Central Bank, as for META.

FOR PURPOSE OF:

Improvements of herds through crosses with registered bulls, development of pure domestic breeds, improvement of physical facilities, and development of forage crops on livestock farms.

SHORTCOMINGS:

The program has been a definite success from the viewpoint of acceptance. Demand substantially exceeded funds available. Shortcomings include:

- 1) Less livestock was imported than originally planned because of delays in securing loans and excessive guarantees required. Producers resisted mortgaging their farms, to buy animals (they rejected the logic of this requirement since the livestock was covered by life insurance).
- 2) Technical assistance was inadequate both from the viewpoint of credit planning as well as project implementation. Technicians were handicapped by lack of knowledge of land utilization patterns and potential, as well as inadequate knowledge of principles of agricultural credit, farm management and agricultural economics. There are no general economic feasibility studies of livestock farming for the various regions of the country. Agronomical aspects also failed to receive sufficient attention (Ibid., page 605).

ANNEX II
Exhibit H

- 3) The cooperation given by private commercial banks leaves much to be desired. Most of the approved applications were from large ranchers, while many applications from medium-size applicants were rejected; almost all applications from small ranchers were turned down (Ibid., page 605).
- 4) The negotiation of loans was unjustifiably slow, thus causing prospective borrowers to miss their best opportunities.
- 5) An important problem was the collateral demanded by commercial banks as they refused to accept the livestock to be purchased as collateral and insisted on real estate guarantees.
- 6) Shortage of funds in the program as evidenced by the substantial discrepancy between the number of applications received and processed by the technical department as against the much lesser number approved by the financial institutions. (Page 606).
- 7) Absence of economic feasibility studies to indicate whether MEGA should give priority to the production of meat or of milk; studies should be undertaken to determine the type of livestock farming that is mostly economical for the different areas of the country.
- 8) Failure by the Central Bank to exercise any control over the disposition made of MEGA loans and rediscounts. Sanctions should have been imposed by the Central Bank on commercial banks that failed to comply with the objectives of the program to discourage violations.

ORGANIZATION: MEPO (Mejoramiento Porcino)

RECEIVES FUNDS FROM:

Program financed through ABC funds (page 606).

ANNEX II
Exhibit H

CHANNELS FUNDS TO:

Hog ranchers, small and medium-size. The maximum amount to be loaned to anyone user has been set at \$30,000 as for MEGA. All loans under the MEPO program are channeled exclusively through the ABC.

FOR PURPOSE OF:

Importation of improved animals to be followed by the expansion of the Centro de Reproducción Porcina at the Posta Zootécnica de Izalco; the establishment of operating pig farms; and the financing of operating expenditures (El Crédito Agrícola, pages 575-576). Thirty-six percent of the credit has been used for the purchase of breeding stock, 44% for the purchase of facilities, and 15% went for operating expenditures.

SHORTCOMINGS:

- 1) Up to now the program has been of little significance owing to shortage of funds. The MEPO program disposes of no funds of its own and relies on the resources of the ABC. This latter institution has been extremely conservative in its approval of loans.
- 2) There are serious problems regarding the economics of hog raising in El Salvador, owing to the high cost of feed and the absence of a marketing system. This situation underlines the importance of undertaking studies to suggest the best line of action.
- 3) Lack of technical assistance which is badly needed by the program owing to high costs of production and lack of experience in hog raising in the country.
- 4) The requirements of real estate mortgages have been the largest obstacles to expansion of the program as the small hog ranchers are unable to put up such collateral. (El Crédito Agrícola, pages 606-607).

ANNEX II
Exhibit H

ORGANIZATION: Fondo de Desarrollo Económico del Banco Central

RECEIVES FUNDS FROM:

Central Bank own resources resulting from accumulation of profits.

CHANNELS FUNDS TO:

To private and mixed enterprises. No restrictions are imposed on the nationality of the user; there are no provisions specifying whether user must be owner or renter, a natural or juridical person or describing types of beneficiaries. Loans are not subject to maximum or minimum amounts. Credit is extended through commercial banks, the Banco Hipotecario, INSAFI, la Financiera de Desarrollo e Inversión, S.A., Federacion de Cajas de Crédito and ABC.

FOR PURPOSE OF:

To alleviate the shortage of funds for medium and long-term investment in agriculture, industrial processing of raw materials and for tourism. The Fund is also to improve the marketing and distribution of agricultural products and to promote the development of the extractive industry (El Crédito Agrícola, page 610).

SHORTCOMINGS:

- 1) The limited resources of the Fund are dispersed over a broad area instead of being concentrated in agriculture. Agriculture in particular suffers from competition with tourism as the latter sector appears to offer lower risks, better guarantees and is more likely to attract private capital.
- 2) Since part of the Fund's resources are channeled to users through the commercial banking system, they suffer all the shortcomings that characterize commercial bank operations, including excessive mortgage requirements with little attention paid to the destination of credit, the social benefit, control over the ultimate use of funds, and the need for technical assistance. It may be presumed, therefore, that most of the Fund's resources did not reach the small and medium-size farmers.

ANNEX II
Exhibit H

- 3) The operating rules of the Fund do not include specific regulations under which the credit can be granted such as specifying size and type of credit and the specific uses; nor are there limits on minimum and maximum loans, maximum or minimum terms, grace periods, extension rights, etc. No mention is made of guarantees; and, most importantly, no provision is included for control over the use of the funds, a feature that is essential to all programs of agricultural credit. These aspects were left to the financial institutions which are generally interested only in real estate collateral.
- 4) The loan application requirements for agricultural credit are the same as for industrial credit, including presentation of a complex investment plan, feasibility studies, etc. which cannot be provided by the small and medium farmers.
- 5) Credits granted from the Fund were not administered properly owing to failure to maintain proper coordination with the Planning Council, the Ministry of Agriculture and Livestock and other organizations able to provide technical assistance (page 1 and 621).

AID 1240-2 (1-70)

CHECKLIST 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 made 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 1968.

App. - Foreign Assistance and Related Agencies Appropriations Act, 1970.

COUNTRY PERFORMANCE

Progress Towards Country Goals

1. FAA §.208; §.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.

1. A. (1) El Salvador is making appropriate efforts through its Supervised Agricultural Credit, Livestock Improvement Agencies, Agricultural price Stabilization Institute, and the Agrarian Reform Program implemented through its Rural Colonization Institute.

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

1. A(2) El Salvador is creating such climate by 1. Common market efforts, 2. investment protection laws, 3. investment guarantees, 4. free exchange, 5. tax incentives to new industries.

UNCLASSIFIED

ANNEX III, Page 2 of 19

AID 1240-2 (1-70)

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

1. A. (3) The public's role in the developmental process in El Salvador is increasing through the Savings & Loan Associations, Demographic Society, an expansion of private cooperatives encouraged by the 1969 Cooperatives Law, this project, the private industrial bank and other private institutions.

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

1. A. (4)(a) El Salvador is allocating substantial budgetary resources to development.

(b) Diverting such resources for unnecessary military expenditure (See also Item No. 18.) and intervention in affairs of other free and independent nations. (See also Item No. 17.)

1. A(4)(b) El Salvador does not appear to be taking these actions.

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

A. (5) Public and private Salvadoran entities will contribute substantial funds to the project.

UNCLASSIFIED

ANNEX III, Page 3 of 19

AID 1240-2 (1-70)

(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.

A. (6) El Salvador is making efforts to accomplish these reforms. Progress is being made in recognition of the importance of individual freedom, initiative, and private enterprise, and freedom of expression of the press exists.

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

1. A. (7) El Salvador is adhering to the principles of the Act of Bogotá and Charter of Punta del Este.

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

1. A. (8) El Salvador has consistently followed policies that encourage the repatriation of capital invested in other countries by its citizens.

(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.

A. (9) El Salvador is responding to these concerns and demonstrating a clear determination to take effective self-help measures as shown by its recent increase in real property taxes, and contributions from its own resources toward agricultural and educational reform, and other development projects.

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

1. B. - The above factors have been taken into account in the furnishing of subject assistance.

AID 1240-2 (1- 70)

Treatment of U.S. Citizens

2. FAA §.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?*
2. According to the best information available, no such indebtedness is owed to U. S. citizens.
- i. FAA §.620(e)(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?*
3. There is no evidence of such action.
4. App. D.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?*
4. It appears to be reasonably certain that GOES will not attempt 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. GOES does not now so discriminate.

UNCLASSIFIED

AID 1240-2 (1-70)

ANNEX III - Page 5 of 19

5. FAA §. 620(o); Fishermen's Protective Act. §. 5. *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,*

5. According to the best information available, no seizure of U. S. fishing vessels or imposition of sanctions or penalties against them have been made by El Salvador.

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

5. a. N/A

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

5. b. N/A

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?*

6. Assistance planned under this loan is for infrastructure and not for a productive enterprise which could compete 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?*

7. Such actions have not been permitted and adequate measures have been taken to prevent them.

UNCLASSIFIED

ANNEX III - Page 6 of 19

AID 1240-2 (1-70)

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?*
8. A bilateral agreement between the United States and El Salvador, relating to the guaranty of private investments, was signed at San Salvador January 20, 1960, and entered into force April 8, 1960.
9. FAA §.620(q). *Is the government of the recipient country in default on interest or principal of any A.I.D. loan to the country?*
9. El Salvador is not in default of any principal or interest on any loan made to it under the Act.
10. FAA §.620(t). *Has the country severed 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?*
10. El Salvador has consistently maintained diplomatic relations with the United States.
11. FAA §.620(u). *What is the payment status of the country's U.N. obligations? If the country is in arrears, were such arrearage taken into account by the A.I.D. Administrator in determining the current A.I.D. Operating Year Budget?*
11. El Salvador is not known to be delinquent on any of its U. N. obligations.
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. According to the best information available, El Salvador complies fully with these prohibitions against trade with or assisting Cuba and with permitting ships or aircraft under its registry to carry proscribed items to Cuba.

AID 1240-2 (1-70)

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.
13. The Secretary of State has determined that El Salvador is not controlled by the Communist movement.
14. FAA §. 620(f), App. §. 109. Does recipient country have a communist government
14. El Salvador does not have a Communist Government.
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 determination has been made that El Salvador is so involved.
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?
16. According to the best information available, no El Salvador ships or aircraft traffic with North Vietnam.

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? How much spent for the purchase of sophisticated weapons systems? (Consideration of these points to be coordinated with PPC/MAS.)
17. GOES 1970 DOD budget represents 6% and its Public Safety budget (National Guard, National Police, Fire Depts., etc.) represents 3.96% of its National budget or a total of 1.1% of GNP for the two items. Data on exact amount of foreign exchange resources spent on military equipment is not available. Mission has no available evidence that an inordinate amount of exchange resources will be spent for this purpose in the predictable future. No U. S. PL480 funds are used in El Salvador for military purposes. No determination has been made that GOES is devoting to military purposes a percentage of its resources which materially interferes with its development.

AID 1240-2 (1-70)

18. App. Q.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/JAS.)
18. GOES has not purchased sophisticated military equipment during current U.S. fiscal year.

CONDITIONS OF THE LOANGeneral Soundness

19. FAA Q.201(d). Information and conclusion on reasonableness and legality (under laws of country and U.S.) of lending and relending terms of the loan.
19. Loan terms are consistent with United States and El Salvador laws. The lending and relending terms are considered reasonable in comparison with other sources of financing available.
20. FAA §.251(b)(2); §.251(e). 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.
20. The activity is concluded to be economically and technically sound. An application has been received for this loan which gives sufficient information and assurance that the funds will be used in an economically and technically sound manner.

UNCLASSIFIED

ANNEX III - Page 9 of 19

AID 1240-2 (1-70)

21. FAA §.251(b). Information and conclusion on capacity of the country to repay the loan, including reasonableness of repayment prospects.
- Analysis of Borrower's cash flow indicates reasonable prospects of repayment (Annex II Exhibit A) Borrower will register loan with GOES to assure availability of dollars for repayment of interest, principal, or other payment obligations.
22. FAA §.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?
22. A reasonably firm estimate of the cost to the United States has been prepared, along with satisfactory financial plans.
23. FAA §.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?
23. No legislative action will be required for accomplishment of the purposes of the loan.
24. FAA §.611(e). If loan is for capital assistance, and all U.S. assistance to project does not exceed \$1 million, has Mission Director certified the country's capability effectively to maintain and utilize the project?
24. The Mission Director has certified this compliance.
25. FAA §.251(b). Information and conclusion on availability of financing from other free-world sources, including private sources within the United States
25. Other Free World sources of financing are not interested in financing this project at satisfactory terms and conditions. (See Annex II, Exhibit E)

AID 1240-2 (1-70)

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.
26. (a) The project's emphasis on these developments is discussed in Part II Section I, II, and III.
26. (b) This loan will have a direct effect on meeting the country's food needs through sub-loans to private agricultural cooperatives.
26. (c) Availability of trained manpower will be improved through the project's proposed technical assistance and training programs.
26. (d) Agricultural production increases caused by the project will result in more and better quality food for the population, thereby improving the general level of health.
26. (e) The project has a significant impact on the cooperative movement in El Salvador.
27. FAA §. 209. Is project susceptible of execution as part of regional project? If so why is project not so executed?
27. The project is not susceptible of execution as a part of a regional project.
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.
28. The activity is consistent with the objectives of the Country Assistance Program-Rural Development, and Institutional Development. By strengthening the technical and financial resources of Fedecaces, it will contribute to realizable long-range objectives and stimulate the development of viable production and consumer cooperatives with growth emphasis on the rural sector.

UNCLASSIFIED

ANNEX III - Page 11 of 19

AID 1240-2 (1-70)

28. *FAA §.251(i)(7). Information and conclusion on whether or not the activity to be financed will contribute to the achievement of self-sustaining growth.*
29. **The project will make a substantial contribution to self-sustained growth through its technical and financial assistance to the cooperative movement in El Salvador.**
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.*
30. **The activity has a basic relationship to eventual development and encouragement of democratic private and local governmental institutions, and will represent a strong contribution to the objective of assuring maximum participation by the people in the economic development of El Salvador.**
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.*
31. **The program supports these needs, desires, and capacities, and is supportive of institutional development.**

UNCLASSIFIED

AID 1240-2 (1-70)

ANNEX III - Page 12 of 19

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.*
32. **The loan will make a definite contribution to improve technical efficiency of agriculture and commerce through strengthening and expansion of cooperative savings and loan credit unions, thus increasing private enterprise, private initiative and competition.**
33. *FAA §.619. If assistance is for newly independent country; is it furnished through multilateral organizations or plans to the maximum extent appropriate?*
33. **El Salvador is not a newly independent country.**
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.*
34. **The Inter-American Committee on the Alliance for Progress has consistently supported the cooperative movement in Latin America as a means of achieving political and social development.**
35. *FAA §.251(g). Information and conclusion on use of loan to assist in promoting the cooperative movement in Latin America.*
35. **This loan is specifically related to the development of cooperatives.**

AID 1240-2 (1-70)

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.

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

37. FAA §.251(b)(4); §.102.
Information and conclusion on possible effects of loan on U.S. economy, with special reference to areas of substantial labor surplus, and extent to which U.S. commodities and assistance are furnished in a manner consistent with improving the U.S. balance of payments position.
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).*

36. This assistance is in-country oriented but will contribute to the economic and political integration of Latin America by creating a strong private sector cooperative savings and loan credit union system related through CUNA and other entities to similar institutions in other Latin American countries.

37. The loan will have no adverse effect on the U. S. economy. Procurement of U. S. commodities and assistance will be increased through the effects of utilization of loan funds so as to make a modest contribution in aid of the U. S. balance of payments.

38. Income resulting from newly created and expanded cooperative savings and loan credit unions will create an additional demand for U. S. imports to El Salvador and encourage the use of private trade Channels and the services of U. S. private enterprise.

UNCLASSIFIED

ANNEX III - Page 14 of 19

AID 1240-2 (1-70)

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?*
39. **Up to \$100,000 of loan funds may be used to procure professional services of U.S. firms, or from independent countries of the Western Hemisphere south of the U. S. (except Cuba)**
40. FAA §.602. *Information and conclusion whether U.S. small business will participate equitably in the furnishing of goods and services finance by the loan.*
40. **No direct procurement of goods is contemplated by Borrower under the loan. Technical services may be financed as noted in item 39.**
41. FAA §.620(h). *Will the loan promote or assist the foreign aid projects or activities of the Communist-Bloc countries?*
41. **This Section will be complied with. The loan agreement will preclude such use of this assistance.**
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.*
42. **Such assistance will be contracted from private firms from the U. S. and/or independent countries of the Western Hemisphere south of the U. S. (except Cuba).**

AID 1240-2 (1-70)

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.
43. This loan is being made directly to a private intermediate credit institution for sub-loans and for technical services to private sector member savings and loan credit unions.

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?
44. 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.
45. N. A.
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?
46. Equipment financed under the loan shall have its source/origin in and be procured from the U. S. or independent countries of the Western Hemisphere South of the U. S. (except Cuba).

AID 1240-2 (1-70)

47. FAA §.604(b). What provision is made to prevent financing commodity procurement in bulk at prices higher than adjusted U.S. market price?
47. No bulk commodity purchases are contemplated.
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?
48. Host country does not so discriminate.
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?
49. No such procurement is contemplated under the loan.
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?
50. This project is not a water or water-related land resource construction project.
51. FAA §.611(e). 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?
51. No construction contracts will be financed under this loan.

UNCLASSIFIED

ANNEX III
Page 17 of 19

AID 1240-2 (1-70)

52. FAA §.620(g). *What provision is there against use of subject assistance to compensate owners for expropriated or nationalized property?* 52. No loan funds will be used for these purposes. The loan agreement will preclude such use of loan funds.
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.* 53. As demonstrated in the loan paper, Salvadoran sources will contribute a substantial amount of the local costs of the project. There are no U.S. owned foreign currencies available for the project.
54. App. §.104. *Will any loan funds be used to pay pensions, etc., for military personnel?* 54. No such payments will be made under this loan.
55. App. §.111. *Compliance with requirements for security clearance of U.S. citizen contract personnel.* 55. To the extent that they may be applicable, these requirements will be met.

UNCLASSIFIED

ANNEX III - Page 18 of 19

AID 1240-2 (1-70)

56. *App. §.112. If loan is for capital project, is there provision for A.I.D. approval of all contractors and contract terms?*
56. All Borrower-contractors and the terms of the contracts will be approved by USAID.
57. *App. §.114. Will any loan funds be used to pay U.N. assessments?*
57. The loan agreement will preclude such use of funds.
58. *App. §.115. Compliance with regulations on employment of U.S. and local personnel for funds obligated after April 30, 1964 (Regulation 7).*
58. The loan agreement will reflect this requirement.
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?*
59. No non-U.S. vehicles will be procured.
60. *App. §.401. Will any loan funds be used for publicity or propaganda purposes within U.S. not authorized by the Congress?*
60. Loan funds will not be used for publicity or propaganda purposes within the United States.

AID 1240-2 (1-70)

- | | |
|---|--|
| <p>61. <i>FAA §. 620(k). If construction of productive enterprise, will aggregate value of assistance to be furnished by U.S. exceed \$100 million?</i></p> <p>62. <i>FAA §. 612 (d). Does the U.S. own excess foreign currency and, if so, what arrangements have been made for its release?</i></p> | <p>61. Aggregate value of assistance to be furnished by United States will not exceed \$100 million.</p> <p>62. U.S. does not own excess foreign currency (Colones) which could be used for the Project.</p> |
|---|--|

NOTE: This checklist does not include provisions passed in the FAA of 1969 or in the FY 1970 Appropriations Act.

DRAFT

LOAN AUTHORIZATION

PROVIDED FROM: Alliance for Progress Loan Funds
EL SALVADOR: Credit Union Development

Pursuant to the authority vested in the Deputy U.S. Coordinator, Alliance for Progress, Agency for International Development ("A.I.D."), by the Foreign Assistance Act of 1961, as amended, and the delegations of authority issued thereunder, I hereby authorize the establishment of a loan pursuant to Part I, Chapter 2, Title VI, Alliance for Progress to the Federacion de Cooperativas de Ahorro y Credito de El Salvador, "Fedecaces," ("Borrower") of not to exceed two million United States dollars (\$2,000,000) to assist in financing local currency costs of subloans by Fedecaces to member credit unions and thereby to assist in the development of a self-sustaining private cooperative federation ("Project"). Up to one hundred thousand United States dollars (\$100,000) of the loan may be used for technical assistance to the "Borrower". This loan shall be subject to the following terms and conditions:

1. Interest and Terms of Repayment:

- (a) Borrower shall repay the loan to A.I.D. in United States dollars within twenty five (25) years from the date of the first disbursement under the loan, including a grace period not to exceed seven (7) years. Borrower shall pay to A.I.D. in United States dollars, on the disbursed balance of the loan, interest at the rate of two percent (2%) per annum during the grace period and three percent (3%) per annum thereafter.
- (b) If prior to the date on which the first interest payment is due the Government of El Salvador ("Government") so elects, "Borrower" shall fulfill its dollar obligation under the loan by paying to Government in the currency of El Salvador the equivalent, at the times called for in the Loan Agreement, of the amounts payable under 1(a) above, determined at the rates of exchange prevailing on the dates of disbursement, and in the event of such election Government shall become the primary obligor and shall pay to A.I.D.:

- (i) Interest in United States dollars on the undisbursed balance of the loan at the rate of two percent (2%) per annum during a grace period of not to exceed ten (10) years ("Government Grace Period") and three percent (3%) per annum thereafter.
- (ii) Principal in United States dollars within forty (40) years including the "Government Grace Period."

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 or independent countries of the Western Hemisphere south of the United States (except Cuba).
- (b) United States dollars utilized under the loan to finance local currency costs shall be made available to Borrower or its designee upon request to A. I. D.
- (c) "Borrower" shall covenant that it and A. I. D. will jointly perform progress reviews, towards meeting the goals of the Project, as deemed appropriate by either party, and will reach agreement on the remedial actions, if any, to be carried out by Borrower.
- (d) A.I.D. loan funds will be made available to Borrower on a pari passu basis with paid in share capital of Fedecaces and member credit unions at the rate of one and one half percent ($1\frac{1}{2}\%$) of loan funds to one percent (1%) of paid-in share capital of Fedecaces and its member unions.
- (e) Prior to the disbursement of loan funds hereunder Borrower shall:
 - (i) Provide evidence in form and substance satisfactory to A.I.D. attesting that this loan will be backed by the full faith and integrity of Fedecaces and its member credit unions.

- (ii) Cause this loan to be approved by the responsible agency of Government under the Law of International Transfers (Ley de Transferencias Internacionales), and subsequently register this approval with the Central Reserve Bank of El Salvador so as to assure the convertibility of local currency to United States dollars to meet the needs of servicing the interest and principal payments of this loan.
- (f) The loan shall be subject to such other terms and conditions as A.I.D. may deem advisable.

Deputy U.S. Coordinator
Alliance for Progress

Date