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

PROJECT PAPER

Proposal and Recommendations
For the Review of the
Development Loan Committee

5280103

URUGUAY: Agri-Industry Development Loan

AID-DLC/P-2105

LA/DR
on-going

UNCLASSIFIED

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

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AID-DLC/P 2105

June 17, 1975

MEMORANDUM FOR THE DEVELOPMENT LOAN COMMITTEE

SUBJECT: Uruguay - Agri-Industry Development Loan

Attached for your review are the recommendations for authorization of a loan to the Government of the Oriental Republic of Uruguay in an amount not to exceed Five Million ($5,000,000) dollars to assist in financing the dollar costs of a program to provide medium and long term financing and technical assistance for the development and expansion of agri-industrial and related enterprises in Uruguay. An amount not to exceed $500,000 may be used for feasibility studies and technical assistance.

This loan is scheduled for consideration by the Development Loan Staff Committee on Monday, June 23, 1975; please note your concurrence or objection is requested by close of business on Wednesday, June 25, 1975. If you are a voting member a poll sheet has been enclosed for your response.

Development Loan Committee
Office of Development
Program Review

Attachments:

Summary and Recommendations
Project Analysis
Statutory Checklist

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*May be obtained from LA/DR uppn request.

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PART I - SUMMARY AND RECOMMENDATIONS

A. Borrower

The Borrower will be the Government of the Oriental Republic of Uruguay (GOU). The primary executing agency of the Loan will be the Ministry of Industry and Energy, with the Central Bank acting as GOU financial agent. The sub-borrower under the Loan will work through the commercial banking community.

B. Amount and Terms of Loan

The Loan is not to exceed US$5.0 million. It will be repayable over 40 years with a 10 year grace period on principal repayments. The annual interest rate will be 2 percent during the grace period and 3 percent thereafter.

C. Sector Goal and Project Purposes

The goal of the project is to create an agri-industrial infrastructure capable of expanding non-traditional exports, thereby contributing to a diversification of agricultural production, increased foreign exchange earnings and increased production, employment and income opportunities for the target group. The project purposes are: (1) to provide a package of financial and technical services to private entrepreneurs and cooperatives for the establishment or expansion of agri-industries (food processing): (2) to help establish an effective delivery system for these services: and (3) to stimulate new production and marketing alternatives for small and medium farmers through the establishment of viable agri-industrial enterprises.

D. Project Description

The proposed US$ 5 million A.I.D. Loan will assist the Government of Uruguay to address a major constraint to economic growth and development over the past two decades, namely the lack of medium and long-term credit for financing productive investments. The Loan will provide foreign exchange for capital goods imports, essential raw material working capital requirements (e.g. tin plate for processing plants) and related technical assistance in support of new or existing export-oriented food processing industries and related service industries. The GOU counterpart funds will finance local costs for civil construction, purchase of existing plant facilities, locally-made capital goods, working capital requirements, feasibility studies and technical assistance. As part of its counterpart contribution, the Borrower will establish an industrial credit insurance fund or guaranty arrangement to be administered by the Central Bank to protect commercial banks against a portion of commercial financing risks involved in sub-borrowing, as a means of reducing existing excessive collateral requirements.

The project will include a heavy emphasis on the institutional development of a special mechanism which will perform development banking functions to evaluate project proposals and channel medium-term credit through the commercial banks to the private sector.

The ultimate intended beneficiary of the project is the small and medium farmer who is the principal producer of non-traditional export crops and who will be stimulated to new production and marketing activities by the establishment, expansion or modernization of agri-industrial enterprises. The initial and intermediary beneficiaries will be the private entrepreneurs and cooperatives who will invest in and operate these agri-industrial enterprises. The productive sectors of the economy as a whole will also benefit from the creation of an intermediate financing mechanism for channeling credit and technical assistance to viable development projects.

E. Financial Plan

Of the total Loan amount of US$ 5 million, the bulk of the Loan will be utilized for capital goods imports in support of new or existing export-oriented food processing industries, which utilize inputs provided by Uruguay's small and medium farmers, and related service industries. In addition, the Loan will provide up to US$ 350,000 for technical assistance to sub-borrowers for conducting feasibility studies for prospective sub-projects and for assisting sub-borrowers in setting up new, or expanding existing, agri-industries, and up to US$ 150,000 for technical assistance to the implementing agency itself. Of the capital goods imports component, up to US$500,000 will be available to finance dollar cost procurement of farm machinery for farm machinery service programs by agricultural cooperative and/or private contractors to provide needed services to small and medium farmers who produce non-traditional export crops. The GOU counterpart funds will meet all necessary local costs of approved sub-projects under the Loan, with a minimum contribution of the peso equivalent of US$ 2.25 million, or 31% of total project funds.

The exact interest rate to the sub-borrower will be mutually agreed upon after a comprehensive examination to be undertaken by the GOU as a condition precedent to initial disbursement. It is contemplated that the total rate will be approximately 10% in real terms. This rate would also apply to local cost financing from GOU counterpart funds. The amortization period for sub-loans would vary between 3 and 10 years for capital goods procurement and related services, and up to 2 years for essential working capital requirements. Together with a possible grace period, final terms would depend on the nature of the sub-project proposed for financing. All sub-loans will be readjustable according to an approved index, most probably the Montevideo cost-of-living index. (This formula is consistent with that to be used by the IBRD Industrial Sector Loan). A fee for the cost of a credit insurance policy or credit guaranty arrangement will be in addition to the determined interest rate.

The following represents expected disbursements of project funds, by use, during the 3-year disbursement period:

	(CY)	76	77	78	Total	Percentage
1. AID (million US$)		.55	1.7	2.75	5.0	69%
2. GOU pesos (millions US$ equivalent)		.25	1.15	.85	2.25	31%
TOTAL		.8	2.85	3.6	7.25	100%

F. Other Sources of Financing

The EXIM Bank and the IDB have indicated they are not interested in financing this project.

This proposed Loan will directly complement a US$ 35 million IBRD Industrial Sector Loan, which will also provide financing for export-oriented industries in Uruguay. The IBRD Loan will utilize the same institutional mechanism (Unidad Asesora) for the capital imports component of its loan (US$ 14.5 million) which, while available for all export-oriented industries, will be primarily directed toward modernization or expansion of existing export-oriented industries other than food processing, in which area the AID Loan will be concentrated. IBRD was approached about financing this Loan as well, but AID was informed that sufficient Bank funds were not available at this time to adequately finance demand from the entire industrial sector and that complementary AID financing of the food processing sub-sector would be very important to sectorial objectives. Therefore, AID Loan funds under this project will concentrate on the agri-industrial (food) sector, and the portion of the IBRD loan related to financing capital investment, while available for all industries, will be primarily oriented to the non-food sector and thus directly complement AID funds.

G. Views of the Country Team

The Country Team considers this program to be a key element of the U.S. assistance program in Uruguay and recommends its approval at the earliest possible date.

H. Statutory Criteria

All statutory criteria have been met. (See Annex C).

I. Issues

There are no major issues to be resolved prior to Loan authorization. However, on two matters, while GOU agreement has been reached in principle, certain technical and operational details must be determined and agreed to prior to disbursement. A summary of these matters is presented below: more detailed discussions of each is contained in the text.

a. Sub-Loan Interest Rates.

Given Uruguay's high inflation in recent years, full provision for maintenance of value of the agri-industrial fund resources (both dollar and peso) is essential. The GOU is in complete accord, and full readjustability of sub-loans was accepted as a premise for establishing sub-loan terms. Because of time limitations, the Project Committee was unable to fully address certain technical aspects of the sub-loan interest rate question. Among the factors to be more fully analyzed concern the use of an index for the readjustment of sub-loans. The GOU suggests the cost of living index is the only reliable index for this purpose and the Mission will review the GOU's analysis in support of this suggestion. Sub-loan rates will also include an appropriate margin for the participating commercial banks. This margin should be sufficient to offer an incentive for these banks to participate in and promote the program to potential sub-borrowers. Also, the final cost to the borrower will likely include some incentive to use the resources of the Program. In the analysis to be undertaken, the real cost of capital in other international markets for similar uses will be used as a reference mark.

The Project Committee's recommendation for the USAID's negotiating objective is sub-loan rates set at or near 10%, fully readjustable, denominated in dollars. The rationale for such a rate is the following. There is no desire on the part of either AID or GOU to unnecessarily subsidize target industry activities. The cost of capital in international markets currently is approximately 9%. (The proposed IBRD Industry Sector loan is expected to be offered at 8 1/2% to the GOU). To this base, a margin for the participating commercial banks must be included, probably within the range of 1.5 to 2%, in nominal terms. The total recommended rate objective therefore is approximately 10%. (If the GOU desires, an additional margin could be added for services to be provided by either the Unidad Asesora or the Central Bank. The GOU's indication of intent not to add service charges in effect offers a small incentive or subsidy to the potential borrower to seek financing for his project under the agri-industry development program.) Such a sub-loan rate objective compares favorably with rates offered by the GOU for long-term, fully readjustable, dollar denominated bonds.

During July an IBRD Appraisal Mission will examine in detail the above, and possibly other factors as a basis for recommending sub-loan rates and terms under the proposed IBRD Industry Sector Loan. The conclusions of that analysis will serve as the basis for joint GOU/USAID negotiations and agreement on sub-loan rates for this project.

b. <u>Credit Insurance Fund or Loan Guaranty Arrangement</u>.

GOU and Project Committee analysis of the commercial banking system strongly indicated that the proposed program would not be effective in assisting significant numbers of new entrepreneurs and/or cooperatives unless a way could be devised to induce commercial banks to reduce currently high to very high collateral requirements. One suggested method to accomplish this involves establishment of a credit insurance fund by the Central Bank which, for a fee, would insure participating commercial banks against sub-loan defaults. A second method involves a risk sharing approach in which the commercial banks would bear the "front-end" or initial risk up to a ceiling exposure of e.g., 25%, with the Central Bank bearing the remaining portion. Adequate time was not available to establish the advantages of either system or others during project negotiations. The GOU, with Mission, AID/W, or other U.S. or international agency assistance (OPIC appears to be a prime source of expertise in each of these methods), will examine this matter subsequent to authorization and prepare a time-phased implementation plan as a condition precedent to disbursement.

J. Recommendations

On the basis of the conclusions of the Capital Assistance Committee that the program is technically, economically and financially justified, it is recommended that a loan to the Government of Uruguay for an amount not to exceed US$ 5 million be authorized with the following conditions and covenants:

a. Conditions Precedent to Initial Disbursement for Dollar Costs of Technical Assistance to the Borrower.

Prior to the first disbursement or to the issuance of the first letter of commitment document under the Loan for eligible technical assistance to the Borrower, the Borrower shall, except as AID may otherwise agree in writing, furnish to AID, in form and substance satisfactory to AID, the following:

1. Evidence of the establishment by the Central Bank of a special fund for the purpose of administering the AID Loan and the Government of Uruguay counterpart resource contribution to the Project.

2. Evidence that it has authorized the Unidad Asesora of the Ministry of Industry and Energy to serve as the technical review group and principal executing agency for the administration of this Project.

3. Evidence of the establishment and responsibilities of a Special Commission whose functions will include the approval of sub-projects for financing with the resources of the Program.

4. Copies of:

(a) the approved operating policies of the Unidad Asesora;

(b) the approved organization and staffing pattern of the Unidad Asesora;

(c) an approved plan for carrying out objective and comprehensive reviews and appraisals of sub-projects submitted to the Unidad Asesora under the Project;

(d) a statement setting forth the standards and procedures which will be followed in approving and monitoring sub-loans and in providing, or facilitating the provision of, technical assistance to sub-borrowers:

(e) a plan for strengthening the professional and technical capacity of the <u>Unidad Asesora</u> in regard to project review, appraisal and monitoring, and the provision of technical assistance to projects in areas such as export promotion and export market development, and providing for the inclusion of an agri-industry advisor(s) to promote and assist agri-industrial enterprises in identifying and preparing sub-projects for financing.

b. <u>Conditions Precedent to Subsequent Disbursement of Loan Funds.</u>

Prior to the first disbursement or the issuance of the first letter of commitment document under the Loan, for purposes other than technical assistance to the Borrower itself, the Borrower shall, except as AID may otherwise agree in writing, furnish in form and substance satisfactory to AID, the following:

1. Evidence that the tax on banking activities ("Impuesto Unico") will not be applied to any transactions financed under this Program.

2. A Central Bank circular describing the guidelines and regulations for utilizing the resources of the Project.

3. A proposal, including a time-phased implementation plan, for the establishment of a credit insurance fund or guaranty arrangement, to be administered by the Central Bank, to protect commercial banks against a portion of commercial financing risks involved in sub-borrowing.

4. A statement of the interest rate policy to be utilized under the Project in determining interest rate charges to sub-borrowers for approved sub-loans, including criteria for determining periods of amortization and grace, and the indexing system and the manner in which it will be utilized for readjustment of the outstanding principal amounts of sub-loans approved under this Project.

c. Covenants

1. The Borrower covenants that all commercial banks will have equal opportunity to participate in the Program, and that all commercial banks so participating in the Program will be treated equally with respect to all administrative prodedures of the Program.

2. The Borrower covenants that the Central Bank circulars and guidelines regarding the implementation of this Project will not be changed without prior consultation and approval of AID.

3. The Borrower covenants that its contribution to this Project will be equal to no less than 30% of the costs of the Project, as described more fully in the Project Description - Annex A to this Agreement, and that it will make available in a timely manner the local currency for the requirements of the sub-projects approved for financing. The Borrower further covenants to meet jointly with representatives of AID once every six months, or more frequently as AID and the Borrower may jointly agree in writing, for the purpose of determining the projected levels of local currency the Borrower will make available to the Project in the subsequent period.

4. The Borrower covenants that all future reflows from this Loan will be allocated to finance costs of future agri-industrial projects.

5. The Borrower covenants that in implementing this Loan, special priority and preference will be given to those agri-industrial sub-projects which maximize the benefits to small and medium farmers involved in the production of raw agricultural inputs, and to cooperatives.

6. The Borrower covenants that all sub-projects approved by the Special Commission which would utilize in the aggregate over $350,000 in A.I.D. funds will be submitted to A.I.D. for review and approval.

K. Project Committee

Thomas O. Stephens, Food and Agriculture Officer, USAID/Uruguay
Lauryn C. Drengler, Controller, USAID/Uruguay
Juan C. Crespi, Executive Assistant to the AID Representative, USAID/Uruguay
Gerald Warner, Agri-Industry Consultant
Jaime Barceló, Assistant to Loan Office, USAID/Uruguay
Edward Lijewski, Loan Officer, AID/Washington
Scott E. Smith, Loan Officer, AID/Washington

Approved by: Leonard J. Horwitz, AID Representative
USAID/Uruguay

PART II - ECONOMIC SETTING

A. The Background

Uruguay's economic performance over the past two decades has been among the poorest of any country in the free world not afflicted by war or natural disaster. It has been beset variously by stagnation of production, chronic high inflation, recurring fiscal and balance of payments deficits, high unemployment and underemployment, declining real income, deteriorating physical infrastructure, institutional paralysis and continuing emigration.

The basic causes stem from a long history of inappropriate economic policies resulting in serious structural distortions in the economy.

A serious imbalance exists between a large urban sector (80 percent of the population) which is heavily dependent on the small agricultural sector (17 percent of GDP) which contributed 85 percent of Uruguay's export earnings and pays for most imports. The import demands of the urban sector, primarily to support a highly protected industrial sector, have far outstripped the capacity of the agricultural sector to generate foreign exchange earnings. The resulting balance of payments constraint on imports has been the principal factor in limiting growth, particularly in the industrial sector.

To support the consumption and social welfare aspirations of the urban sector, the agricultural sector has, in the past, been subjected to tax, pricing and exchange rate policies designed to produce large income transfers to the urban sector. The result has been to provide disincentives to agricultural investment, inhibit the introduction of new technology and stagnate production. Likewise, a highly protected urban industrial sector, mostly geared to supply a small domestic market, soon exhausted its growth possibilities and produced stagnation in that sector as well. To mitigate the economic squeeze, past Uruguayan governments have sought to control every economic variable in sight. The GOU created a large, costly bureaucracy designed to allocate scarce resources and intervene in private economic decision-making. To the extent the bureaucracy became dysfunctional in carrying out its interventionist role, the private sector was adversely affected together with economic growth.

B. National Development Plans and Policies

After a political restructuring took place in 1973, the Bordaberry Administration began a fundamental development-reform effort. It approved a National Development Plan (1973-77) and at the San Miguel and Nirvana meetings (August and October 1973), translated the broad goals of the Plan into specific policy and program guidelines. Essentially, these guidelines call for (1) a gradual reduction of state intervention in the economy to allow productive patterns to be determined by market forces, (2) rejuvenation of agriculture through a variety of incentives, including higher producer prices and a gradual substitution of land productivity taxes for export taxes, (3) realistic exchange rates, (4) elimination of impediments to export and liberalization of imports, and (5) restructuring of production toward an export orientation and along the lines of international comparative advantage.

The National Development Plan (1973-77) contains an exceptionally candid diagnostic of the historical causes of stagnation and inflation which in great measure confirms the analyses of international experts and development agencies over the years. The Plan does not pretend to formulate a complete macro-model nor provide comprehensive sectoral analyses backed by medium or long term investment programs. Rather, it provides a coherent set of national development goals, defines a strategy, and enumerates a number of the policy, program, and institutional changes needed if the goals are to be realized. While its sectoral assessments are uneven as to scope and quality of analysis, those pertaining to agriculture and industrial development contain a clear orientation and focus that serve as guides to policy and program action. The authors of the Plan recognized the dynamic nature of the Plan and stressed the need for extensive work in refining the assumptions, expanding sectoral analyses, formulating policies, programs, and investment plans needed for the Plan's rational implementation.

It remained for the high level meetings of civilian and military leaders at San Miguel and Nirvana (August and October 1973) to flesh out the Plan and define the indicated policy and program actions to advance toward the agreed goals and strategy. An analysis of the San Miguel and Nirvana policy guidelines is contained in the 1973-74 DAP for Uruguay. Some twenty months have gone by since San Miguel and Nirvana and by any measure, overall performance has been impressive in initiating the policies and programs called for in these guidelines.

For example, during 1974 and 1975, there has been steady progress in gradually moving away from statist intervention in the economy toward a free market orientation. There has been selective liberalization of price controls and more rational criteria are being applied in considering price increases. Industrial promotion and foreign investment laws have been put into effect. A perceptible improvement has occurred in the operations and financial management of several state enterprises (airlines, ports, postal and rail systems). Prices of goods and services provided by state enterprises have been raised appreciably to reduce operating (and fiscal) deficits. A reform of the banking system is being carried out to help develop a functioning capital market, enhance its role as an instrument of development and establish a rational credit system. Export procedures are being simplified and the import regime liberalized. A system of monetary correction (readjustment) of bank loans for productive investments will soon be initiated.

A basic reform of the tax system took place in 1974 designed to reduce or eliminate a number of low yield nuisance taxes and to increase the incidence of the value added tax (IVA), the land productivity tax (IMPROME), and excise taxes on total revenues. In line with GOU fiscal strategy, these taxes will become the GOU's principal revenue sources. A basic reorganization of the tax administration system was initiated in early 1975.

A fundamental restructuring of the trade and payments system was launched in 1975 as part of the GOU's economic program agreed to with the IMF. Likewise, as part of this agreement, a stabilization program is now in effect designed to cut the inflation rate in half in 1975 from the 107 percent recorded in 1974. The exchange rate system has also been reformed involving a liberalization of the financial foreign exchange market and a dramatic reduction in the past overvaluation of the commercial rate until at present the two rates are close to equilibrium.

The agricultural sector has been incentivized by favorable price, exchange rate, tax, and credit policies, which has resulted in growth of the crop sector while the livestock sector continues to stagnate due to external factors. Programs to develop new agricultural technology and extend it to rural producers have been initiated. A major effort is underway to expand exports of traditional and non-traditional agricultural products.

A civil service reform has been advanced designed to reduce excess personnel and retrain others to affect a more rational utilization of manpower. Reform of the social security system continues under study as efforts are made to design the reform along lines consistent with the GOU's economic stabilization-development program. A new social security reform law is promised for 1975.

Intensive sectoral studies (assisted by IBRD/UNDP) are underway for the agricultural and transportation sectors designed to formulate long term investment programs. Important progress has been made in planning and implementation of the energy sector program, with the Salto Grande hydroelectric project in construction, plans for interconnection programs with Argentina, and probably Brazil, completed and the feasibility established of the Palmar hydroelectric project on the Rio Negro for which financing arrangements are well advanced.

Perhaps the most positive factor benefitting GOU development prospects was the appointment in July 1974 of Alejandro Vegh Villegas as Minister of Economy and Finance. Vegh, an experienced economist/engineer and a highly regarded development planner, committed himself to a vigorous implementation of the National Development Plan and the San Miguel and Nirvana policy guidelines. His market-oriented economic policy was launched by action in October 1974 to liberalize the financial foreign exchange market and modify the interest rate structure. Also, in October 1974, Vegh requested an IMF Standby Agreement and IBRD development assistance. The IMF and IBRD agreed to begin negotiations on the basis of GOU agreement to prepare a comprehensive macro-economic program encompassing both stabilization and development goals. The program, to be described below, was developed between December 1974 and March 1975 and was finally accepted by the country's highest political and military authorities. On May 12, the IMF Board of Executive Directors approved the GOU request for a Standby Agreement (First Tranche).

C. Recent Economic Developments 1/

1. Trends through 1974

Recent economic developments in Uruguay have been dominated by large swings in the international terms of trade. In 1973 an increase in world prices for Uruguay's two major exports, beef and wool, led to a marked improvement in the balance of payments. The favorable terms of trade were short-lived, however. Higher prices for petroleum at the beginning of 1974 completely wiped out the previous gain, and the subsequent downturn in meat and wool prices late last year left the terms of trade at the end of 1974 worse than at any time in the past several years.

Largely because of these price developments, Uruguay's balance of payments on current account went from a surplus of SDR 31 million in 1973 to a deficit of SDR 88 million in 1974 (Table 1). About two-thirds of this deterioration can be accounted for by higher costs of petroleum imports, which rose from SDR 45 million in 1973 to SDR 126 million in 1974, with only a 2.5 percent growth in volume. The remaining deterioration in the current account also appears to have been caused by price changes (principally higher import prices for sugar, wheat, fertilizer, and industrial raw materials), as the volume of imports declined while the volume of exports rose slightly in 1974. These price and volume series for international trade goods must be regarded as only rough approximations, but they indicate that the loss of income to Uruguay between 1973 and 1974 resulting from unfavorable movements in the terms of trade was equivalent to about 8 percent of GDP.

Uruguay's overall balance of payments has followed the same path as the current account, switching from a surplus of SDR 73 million in 1973 to a deficit of SDR 48 million in 1974. Despite this large deficit, the gross foreign assets of the monetary authorities declined by only SDR 3 million in 1974, after purchases of almost SDR 47 million under the Fund's 1974 Oil Facility. At the end of 1974, Uruguay's gross international reserves were SDR 206 million, equivalent to about six months of imports. Gold--valued at SDR 35 per ounce--comprised SDR 124 million of these reserves, but about one-fifth of the gold had been pledged temporarily to a foreign commercial bank as collateral for a medium-term loan.

1/ This section excerpted from IMF Staff Report on Uruguay, SM/75/96, April 25, 1975.

Table 1: Uruguay: Summary Balance of Payments
(In millions of SDRs)

	1972	1973	1974	Projected 1975
Goods, services, and transfers	41.9	31.2	-88.2	-100.0
Trade	0.1	32.7	-85.4	- 85.0
Exports	(259.4) 1/	(275.3)	(318.5)	(300.0)
Imports, c.i.f.	(197.1)	(242.6)	(403.9)	(385.0)
Other	-18.0	-1.5	-2.8	- 15.0
Capital (including errors and omissions)	-24.3	41.6	40.1	19.7
Allocation of SDRs	7.3	--	--	--
Counterpart of reduction in gold reserves	-37.1	--	--	--
Net foreign assets of monetary authorities (increase -)	12.2	-72.8	48.1	80.3

Sources: Central Bank of Uruguay; and IMF staff estimates

1/ Includes SDR 62.2 million proceeds from sale of gold.

Against this background of a deteriorating external position, Uruguay's wage-credit-price-exchange rate spiral accelerated further in 1974. According to the consumer index, prices rose by 107 percent compared with 78 percent in the previous year. Nominal wage adjustments also were larger, but real wages are estimated to have declined by about one percent following a two percent decline in 1973. Continuing the policy of frequent, small adjustments of the exchange rate, the peso in the commercial market was depreciated thirteen times for a cumulative depreciation of 77 percent in terms of pesos per U.S. dollar. This was much faster than the 28 percent depreciation in 1973, but less than would have been indicated by differential price movements in Uruguay and the outside world. Total bank credit increased by 84 percent in 1974 (as a percentage of monetary liabilities outstanding at the beginning of the year) compared with 48 percent the previous year.

The central government finances weakened considerably in 1974, the deficit reaching over 26 percent of expenditure compared with nine percent in 1973. This was caused by several factors, including particularly the authorities' attempts to protect domestic consumers and producers from the deterioration in the terms of trade, described above. Public sector wages were increased sharply early in the year, and the domestic consumer prices of wheat, fertilizer, and sugar were subsidized from the budget to offset the rise in their imported prices. Moreover, as world prices declined for beef and wool in the second half of 1974, the export taxes on these products were virtually eliminated, further weakening the Treasury's position.

GDP at constant prices is estimated to have risen 1.9 percent in 1974, which is about the same as the average growth rate of the past decade.

2. Prospects and Policies

The world market for Uruguay's principal exports has continued to be unfavorable in the early months of 1975, and total export earnings are expected to decline this year. In particular, average prices for beef exports, which were US$1,700 per ton in the first quarter of 1974 and US$1,300 per ton for the full year 1974, were below US$1,100 per ton in the first months of 1975. World prices for wool also have declined to about one-half the level at the beginning of last year, although -- as in the case of beef -- they remain well above the prices received in 1971. Apart from the low world prices, Uruguay recently has been faced with a problem of exporting beef at any price. Because of domestic over-supplies, the EEC, which bought about half of Uruguay's beef exports in the early 1970s, has been closed to imports since June 1974 and is not expected to reopen on a large scale in the near future. This reduction in demand for meat is particularly unfortunate for Uruguay because of the heavy investment to improve pastures and increase herds which has been made in recent years with assistance from the IBRD. The detailed projection of Uruguay's 1975 balance of payments, with a prospective deficit of SDR 80 million, is presented in a separate staff report on Uruguay's intention to request a purchase under the 1975 Oil Facility, which will be circulated shortly.

3. GOU Stabilization-Development Program

Against this background of a large balance of payments deficit and continued unfavorable prospects for exports, Uruguay has adopted a financial program for the period April 1,1975-March 31,1976 in connection with a request for an IMF Standby arrangement in the first credit tranche. In essence, Uruguay's program is designed to reduce the budget deficit to about 14 percent of expenditure, and to limit inflation to 30 percent and the balance of payments deficit to US$70 million in the 12 months from April 1975 through March 1976. (This payments deficit in the program year is considerably smaller than that projected for calendar 1975, mainly because beef exports are expected to begin recovering in the early months of 1976.)

This 12-month plan was initiated at the beginning of April with a series of adjustments in wages, prices, and the exchange rate designed to create an appropriate point of departure for a pause in the wage-price-credit-exchange rate spiral. The April measures included an increase in private and public sector wages of 30,000 pesos per month-representing an average of 10 percent; increases in public sector tariffs of between 10 percent and 20 percent; and a further 10 percent depreciation of the peso, following a particularly rapid depreciation during the previous six months, as explained below.

The projected improvement in Uruguay's fiscal position in the next 12 months will result mainly from a substantial increase in taxation on petroleum products, other smaller tax adjustments, and improvements in tax administration, together with the elimination of subsidies on major consumer products, which accounted for four percent of total budget expenditure in 1974. Some of these measures were announced early this year and the remainder in April. Reduction of the budget deficit was an important precondition for the successful implementation of the credit program, which is designed to be compatible with the balance of payments target and the sharp reduction in the rate of inflation.

In addition to the quantitative targets, Uruguay's program for the next 12 months includes several measures to reduce the restrictiveness of the exchange and trade system. The Uruguayan authorities believe that the complex exchange system and the virtual quota system for imports which have existed in recent years were major roadblocks to vigorous economic growth, and they attach high priority to the early removal of these restrictions. Consequently they have announced the elimination, effective June 1, 1975 of the system of deposit-free quotas for imports, and effective July 1, 1975 of the minimum 180-day financing requirement for private sector imports. The dual exchange market is being retained for the time being, but the spread between the commercial and financial rates has been reduced from about 40 percent last October to only about 10 percent in mid-April. This narrowing of the spread was achieved mainly by a rapid depreciation of the peso in the commercial market, which in the past six months has totalled 67 percent in terms of pesos per US dollar, while domestic inflation in this period is estimated to have been 45-50 percent.

For further details and discussion of Uruguay's economic situation and stabilization-development program, see IMF Papers included in Appendix A.

The GOU stabilization-development program is probably the most ambitious and comprehensive series of economic reforms Uruguay has undertaken in recent years. Unlike previous IMF Standbys which focused primarily on austerity measures to reduce inflation, the present program seeks to link austerity with a complementary development effort assisted by IBRD and private bank loans, which will stimulate productive sectors and help maintain reasonable levels of employment and economic activity.

Most important however, it represents an effort simultaneously to stabilize and restructure the economy away from its past inward-looking focus on import-substitution industrialization toward an export orientation for both agricultural and agri-industrial products and agricultural diversification through expanding non-traditional exports.

Equally significant to the economic policy reforms are the institutional reforms announced. The Bank of the Republic (BOR) has been virtually stripped of its past pervasive control over foreign commerce and its freedom to operate independently of GOU credit programs. Hereafter, the Central Bank, now dominated by supporters of Minister Vegh, will manage the import regime and control BOR credit emission through its rediscount facilities. This latter reform was insisted on by the IMF to ensure that the BOR would not emit credit beyond the limits of the agreed credit program indicated in the Standby.

On the basis of the IMF authorization of a Standby, the IBRD is actively moving ahead to provide substantial development assistance in the industrial, agricultural, energy, and transportation sectors. It is well advanced toward making a US$35 million industrial sector loan and a US$15 million livestock development loan in 1975. In addition, it is planning a major lending program in the energy sector in 1976 including partial financing for the Palmar Dam and a national power distribution network. It is also carrying out sectoral analyses in agriculture and transportation which could lead to substantial new Bank lending in these sectors by 1977.

Implementation of the GOU's stabilization-development program will naturally involve some short term strains including some decline in real incomes as Uruguayans take the long-awaited "cure" toward the restoration of the country's economic health. However, given the critical economic problems afflicting the country, and the firm political-military support given so far to Minister Vegh's program, Uruguay appears to be in the most auspicious position in years to make real progress in attaining its goals of self-sustaining growth.

An IMF Standby should also likely trigger additional credits from international banking institutions to assist the GOU in dealing with its balance of payments problems in 1975. GOU agreement with a syndicate of private banks for a US$[illegible] million loan, guaranteed by gold, is in final stages of negotiation.

Thus, the IMF Standby, which Minister Vegh believes is important for internal economic discipline, will also lead to significant additional international assistance geared both to help Uruguay to cope with her short term balance of payments problems and also to provide the necessary external resources for the country's longer term development effort.

An important new factor to be taken into account is a new economic cooperation agreement between Uruguay and Argentina. The agreement provides capital goods import credits and trade concessions which will permit a range of Uruguayan exports to enter the Argentine market without duties. The agreement also provides a US$50 million credit to the GOU Central Bank for financing private sector capital goods imports. A similar agreement is being negotiated with Brazil which should be signed in 1975. Conversations have been held with Bolivian and Paraguayan authorities for complementary economic cooperation agreements. Thus, for the first time in many years, Uruguay will have access to the markets of her large neighbors and expanded trade relations with Bolivia and Paraguay. This is especially significant for the proposed AID loan in agriculture since Brazil in 1974 became Uruguay's most important export market, especially for meat. There are many indications that the Brazilian market is ready to absorb substantial amounts of agricultural exports from Uruguay, particularly wheat, and a variety of non-traditional products. If these new agreements function as expected and if Uruguay can effectively implement its export development strategy, the medium and long term development prospects would appear to be favorable.

D. Agricultural Development Policy and Programs 1/

1. Sectoral Plans

The National Agricultural Development Plan sets forth the goals and production targets for 1973-77 and contains an extensive diagnosis of the factors contributing to the stagnation of the agricultural sector over the past two decades. It also sets forth a sectoral strategy, an investment plan and indicates policy, programs and institutional reforms necessary to achieve Plan goals and targets.

The Plan contains three major goals which relate to the proposed loan: (a) to increase exports of traditional and non-traditional agricultural products so as to expand foreign exchange earnings and import capacity for economic growth; (b) to expand rural employment opportunities and integration of agriculture with other key sectors by promoting diversification into lines of projection which take advantage of external markets and are labor intensive while permitting adequate agri-industrial development; and (c) to distribute income more equitably within the agricultural sector through pricing, taxation, credit and exchange rate policies which will accelerate this process.

Over the past two years, the GOU has made significant progress in improving the economic policy framework affecting agriculture, which has, in turn, begun to incentivize producers to invest in their land, apply modern technology and improve farm management practices. An improved economic policy framework is a necessary, but not the only, element in attaining Plan objectives since it cannot by itself increase productivity or efficiency of Uruguayan agriculture.

Other constraints must be overcome to assure improved land use, adequate credit, the application of modern technology, timely availability of inputs, and the development of profitable marketing alternatives. The latter three constraints have been diagnosed as the most critical to the smaller farmers and as such have been made the focus of this, the IATA, and CALFORU loan projects.

1/ For further details on recent production trends in agriculture, see IMF document SM/75/97, Uruguay - Recent Economic Developments, dated May 1, 1975, pgs. 4-7 included in Appendix A.

2. Agriculture in the Uruguayan Economy

Uruguay, with its 65,000 square miles, is about the size of Iowa and, like Iowa, well over 95 percent of the land area is classified as agricultural. Since beef, wool, mutton and other crops generate most of the foreign exchange earnings on which future growth depends, the agricultural sector is the backbone of the Uruguayan economy.

For well documented reasons, the land use pattern in Uruguay is one of extensive rather than intensive use of the available soil and water resources. Over 90 percent of the total agricultural land area is used for livestock production. Much of the total agricultural land area is used for livestock production. Much of the crop land is now used for wheat, other cereal grains and vegetable oil crops. Present production of other crops, fruits and vegetables is still of relatively minor importance. The GOU strategy recognizes that the potential for expanding agricultural production using traditional extensive technology is extremely limited. Therefore, it will require improved efficiency in the use of livestock land and the release of some of the more fertile land now in livestock for diversified crop production, particularly for non-traditional exports.

Uruguayan agriculture has been stagnant for the past twenty years. In five of the past ten years, there have been production decreases. This problem has been studied exhaustively but little effective remedial action was taken until the present administration initiated a series of corrective measures, including pricing, tax, exchange rate, and credit reforms. These have caused a healthy shift in attitudes of farmers and ranchers.

Short term production credit appears adequate and responsive to demand. However, with the exception of the projects supported by IBRD and IDB, there is practically no intermediate and long-term credit. This is true of the private banking system as well as with the BOR. The GOU is trying to introduce readjustable loans and improve credit administration to increase capital flow for on-farm investments in order to increase productivity and exports. An analysis of the agricultural credit situation in Uruguay is contained in Annex J.

On the important question of marketing policy, the GOU is well advanced in organizing several special commissions to coordinate all aspects of marketing for key agricultural commodities. Both the public and private sector representatives have membership on these commissions.

The need for land reform is a less serious constraint in Uruguay than in other Latin American countries. Relatively speaking, there are good agricultural land resources to satisfy a small, diminishing rural population. Much land in large properties is not being used productively and a large part of the farming population suffers from having inadequate land resources, as well as the lack of technical assistance.

Through a revitalized colonization program being carried out by the National Colonization Institute (INC), implementation of a new land taxation system based on soil productivity (IMPROME), and by income redistribution schemes favoring the small farmer, the GOU is carrying out a land reform program emphasizing improved land use. Under the INC program, individual properties that exceed 5,000 hectares are to be expropriated, as well as parts of holdings between 2,500 and 5,000 hectares that are not being used productively. Lands so acquired will be distributed so that farmers will be able to acquire economic-size units. In this way, it is planned to redistribute over one million hectares.

In respect to the agricultural crop sector, a series of positive measures have resulted in an expansion of 1974 production (5 percent over 1973). Favorable price policies, correcting previous distortions, have spurred agricultural crop output. Non-traditional exports, primarily agricultural products, increased some 60 percent over 1973. Support prices for wheat, sugar and sunflower oil have been raised to levels designed to incentivize production and thereby eliminate deficits. A significant example of how the Uruguayan farmer responds to price incentives has been demonstrated in the case of wheat production. With a price to the producer close to the world market price, wheat production in the 1974-75 harvest rose to approximately 526,000 tons, leaving about 100,000 tons available for reserves and export. This compares to a 380,000 ton wheat harvest in 1973-74, which fell some 20,000 tons short of requirements. Unfortunately, due to world market conditions, the livestock sector was seriously depressed in 1974, accounting for a growth rate of around one percent.

During 1974, export taxes on wool have been virtually eliminated and those on beef substantially reduced. While there was some revenue loss in 1974 which contributed to the fiscal deficit, the GOU is compensating for the loss by increasing the land productivity tax (IMPROME). Collections from IMPROME have risen from 5.2 billion pesos in 1972 to 26.8 billion in 1974 (in real terms an increase of 46 percent), thus shifting the major tax burden for farmers to land ownership and away from other production factors (inputs). This should serve as an incentive to more productive use of agricultural land.

3. <u>Outlook</u>

Perhaps a significant long term factor favoring Uruguay's prospects is the role it can play in helping to alleviate world food problems. Uruguay has an extraordinary resource base and comparative advantages in food production. Given the right set of internal policies which stimulate the producer, and with the application of appropriate new technology, Uruguay can one day hope to become a contributor of food exports to a hungry world. While Uruguay may never loom large in the world food market, her expanding contributions of food supplies can be instrumental in covering shortages in Latin America and in so doing, relieve somewhat the burden on the U.S. of covering such shortages.

PART III - THE INDUSTRIAL SECTOR

A. Overview *

Uruguayan industry is essentially devoted to the production of final consumer goods for the local market. Manufacturing accounts for about 23% of GDP and provides for 32% of employment. There are about 1,700 manufacturing enterprises in Uruguay, most of which are small and family-owned. About two-thirds of the enterprises employ 10 and 50 people, and only 12% employ more than 100 people. About three-fourths of the enterprises are located in the area of Montevideo. Exports, principally wool tops, finished and semi-finished leather, cement and ceramic items, account for only about 5% of industrial output. As Table 2 indicates, over 50% of industrial production in terms of value added is in food processing, beverages and tobacco, textiles, and shoes and clothing. Intermediate products account for only 27% and capital goods less than 14% of production. Annex H, Exhibit 2 provides a more detailed description of the major industrial branches, including their structure, policies which have affected their development in the past, and long term prospects.

Between 1957 and 1973, the level of industrial output in Uruguay increased at an average annual rate of less than 0.5%. There was a moderate recovery in 1974, when total industrial production rose by 3.6%, due principally to increased activity in meat packing, Uruguay's major industry. The stagnation in the country's industrial sector reflects the fact that, while industrialization through import substitution reached its limits years ago, economic policy has not been reoriented away from that objective.

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* Summarized from IBRD, Economic Memorandum on Uruguay, August 1974, pp. 38-50, and IMF - Uruguay: Recent Economic Developments, April 1975, pp. 7 - 9.

TABLE 2

STRUCTURE OF INDUSTRIAL PRODUCTION

(in percent of total value added)

	1955	1960	1970
1. Traditional Industries	59.4	[illegible]	[illegible]
Food	[illegible]	19.1	[illegible]
Beverages	7.7	[illegible]	11.1
Tobacco	[illegible]	[illegible]	[illegible]
Textiles	15.7	[illegible]	[illegible]
Shoes and clothing	4.8	[illegible]	[illegible]
Wood and products	[illegible]	[illegible]	[illegible]
Furniture	1.4	[illegible]	[illegible]
Leather	1.5	1.1	1.5
2. Intermediate Industries	[illegible]	[illegible]	[illegible]
Paper	0.9	[illegible]	[illegible]
Printing	[illegible]	[illegible]	[illegible]
Rubber	1.0	[illegible]	[illegible]
Chemicals	[illegible]	[illegible]	[illegible]
Petroleum	5.1	[illegible]	[illegible]
Non-metallic minerals	[illegible]	[illegible]	[illegible]
Basic metals	[illegible]	[illegible]	[illegible]
3. Capital Goods	17.6	[illegible]	[illegible]
Metal products	[illegible]	[illegible]	[illegible]
Non-electrical machinery	[illegible]	[illegible]	[illegible]
Electric machinery	[illegible]	[illegible]	[illegible]
Transport equipment	[illegible]	[illegible]	[illegible]
4. Others	1.1	[illegible]	[illegible]
TOTAL:	100.0	[illegible]	100.0

Source: Office of Planning and Budget

TABLE 3

URUGUAY: INDUSTRIAL PRODUCTION 1/

(In percentage change at constant prices)

	1972 Weight 2/	1970	1971	1972	1973	1974
General index	(100.0)	4.1	-1.8	-0.4	-0.7	3.6
Food processing	(25.7)	4.6	-11.[illegible]	-0.8	1.5	7.4
Beverages and tobacco	(19.2)	13.5	4.5	-5.4	5.8	0.1
Textiles	(14.0)	-6.0	-8.1	10.9	-9.2	1.8
Clothing, shoes	(5.4)	-11.4	-5.6	-11.5	-7.4	2.[illegible]
Chemicals	(8.7)	8.9	9.9	-7.4	11.0	4.5
Petroleum and coal products	(6.3)	--	[illegible].1	1.2	-4.6	4.7
Construction materials	(6.8)	27.4	5.8	0.4	9.2	7.6
Electrical	(3.1)	-5.9	7.9	-9.5	-9.6	-2.7
All other	(10.8)	16.5	-0.[illegible]	1.9	1.6	2.7

Source: Central Bank of Uruguay

1/ Includes mines and quarries.
2/ Percentage contribution to gross industrial product in 1972.

This has been the case despite the fact that there is strong world demand for many manufactured or semi-manufactured agricultural-based products which Uruguay is capable of producing. Table 3 shows changes in industrial production in Uruguay since 1970.

In March 1972, a major revision in exchange rate policy was introduced which involved a series of mini-devaluations designed to maintain a realistic relationship of the peso to other currencies. This was followed by reintroduction and expansion of an export incentive program involving tax rebates (reintegros) on the value of exports of non-traditional manufactured products. The percentage of the rebate to the exporter varies by item in accordance with the proportion of value added in production, the use of domestic raw materials or intermediate products, and net foreign exchange earnings. As a result of these policies, exports of non-traditional manufactured goods have increased considerably. While the export rebate program is currently being scaled down, reflecting movement toward more realistic exchange rates, additional policies to encourage exports of non-traditional products, are being implemented by the GOU. Prospects for increased production and exports of woolen clothing, leather products, shoes, processed foods and fish, and non-metallic material are good.

In 1974, the value of total exports increased 11% compared with 1973, despite the difficulties in the international meat market. This was due to increased exports of processed rice and of small diversified products. In 1974, under stimulus of growing export sales, the clothing, shoes, textile and rubber industries showed renewed growth, while other sectors, such as beverages and electrical products continued at a low level of activity. There was an expansion of non-traditional exports of over 60% in 1974, mostly raw and processed agricultural based products.

Developments in 1974 suggest that Uruguayan industry is beginning to respond to efforts to increase industrial and export expansion and to secure increased access to neighboring markets for certain products.

During the last six years, the Government has obtained several foreign industrial credits. The most important are: a US$ 50 million loan from Argentina to finance capital goods imports from Argentina; a US$ 5 million loan from Bulgaria to procure industrial machinery in Bulgaria; a US$ 15 million loan from AID to finance capital good imports from the United States, which is fully disbursed; a DM 12 million loan from Germany to finance the international procurement of capital goods for medium and small-size industries; and a US$ 5 million credit from Italy for machinery and equipment, which is fully disbursed. Also, in 1970 IDB made a US$ 6 million loan to finance medium and small-size industries, which was cancelled in 1974 when disbursements lagged.

In respect to existing industries the foreign exchange constraint and the lack of credit for working capital, however, continue to prevent the full utilization of plant capacity; the poor business climate during 1973 and most of 1974 was manifested in low levels of investment, helping to accentuate the degree of obsolescence in machinery and equipment. The following table on import of capital goods since 1970 illustrates the low levels of investment.

TABLE 4: IMPORTS OF CAPITAL GOODS
(In millions of US$)

Years	Total	Industrial Machinery and Equipment	% of Total Imports
1970	23.8	13.7	4.8
1971	21.9	11.1	8.3
1972	11.2	7.1	2.7
1973	8.3	6.3	1.2
1974	n/d	n/d	n/d

Source: O.P.P. - Foreign Commerce

The main constraint on industrial expansion is on the supply side, set by a past history of tax and price policies which have hindered rationalization and investment in modern equipment. Enterprises have been almost completely dependent upon their own resources to finance local costs for modernization and/or expansion, while Central Bank regulations have required that virtually all imported capital equipment must be financed through suppliers' credits. While the present administration is attempting to change these policies, a major constraint to industrial development remains the obsolete and depreciated condition of the industrial plant, due to an almost complete lack of investment for over a decade.

Despite the promising economic and institutional reforms initiated by the GOU, during the next 12 to 18 months the industrial sector's activity is likely to be affected somewhat by the economic stabilization program and the foreign exchange constraint. The GOU has stated that it will give highest priority in the allocation of foreign exchange to exporting industries; therefore, exports will be the sector's motive force. As was noted above, the principal impediments to industrial expansion in the past two decades were inappropriate economic policies, inflation, the balance of payments constraint, inadequate financing for expansion and lack of an effective mechanism to mobilize internal and external financing for medium and long term investments and to channel these productive investments. The problems of financing industrial development are further analyzed in the following section.

B. Industrial Development Policies and Plans

1. The National Development Plan (1973-1977)

The general objective for the industrial sector in the National Development Plan is to increase cumulative production output by about 5% annually during the life of the Plan.

Specific objectives are: to diversify the manufacturing sector, with emphasis on exporting those products made primarily from local raw materials; (e.g. agri-industrial products); to generate more employment in the productive sectors; and to increase the general level of productivity and efficiency, which is considered indispensable for competing in foreign markets.

This strategy is based on increasing agricultural production to a level which would permit increased exports. The foreign exchange inflow from these exports would then allow the industrial sector to overcome the production limits which are imposed upon them by the limited size of the domestic market. This strategy will be accompanied by a realistic exchange policy, an industrial development law and the creation of a development bank which will permit the channeling of increasing amounts of medium and long term credit to the industrial sector.

These changes will be accompanied by the gradual revision of the protectionist policy which, in itself, is considered an effective stimulus to more productivity and efficiency.

2. The Industrial Promotion Law

The Industrial Promotion Law approved in 1974, provides two major incentives to attract capital investments. These are: credit assistance and tax relief.

Included under the former are credits of 20 years for land acquisition, plant construction and improvements, 8 years for acquisition of machinery and spare parts, 5 years to finance the rollover of accumulated debt, 2 years to cover the cost of assembly, installation and initial operating expenses of new machinery, one year for the purchase of domestic raw materials, and foreign currency loans and guarantees for the importation of capital goods and raw materials.

Tax benefits provide for exemptions and rebates on taxes for services performed by state agencies, exemption of up to 60% of contributions to public welfare agencies, exemption from all corporate income taxes and exemption from port charges, customs duties, tariffs and surcharges on imports.

To qualify for any of these promotional benefits, a company must submit a well-documented application to the Unidad Asesora operating in the Ministry of Industry and Energy (MIE). If the Unidad Asesora considers the project beneficial to the nation, it will recommend that the firm, sector or industrial concern be declared "of national interest", which is a pre-requisite to the granting of any of the above-mentioned promotional benefits.

The exact amount and duration of promotional benefits is negotiated with each applicant on a case-by-case basis.

The philosophy of the Unidad Asesora has been to limit promotional benefits to those necessary for the successful implementation of a particular project.

The benefits of this law are open to both foreign and domestic investors.

3. The Foreign Investment Law

The Foreign Investment Law, approved in 1974, in itself provides no incentives; it was meant to operate in conjunction with the Industrial Promotion Law. What the law does provide are: guarantees of annual remission of profits of up to 20% of invested capital without penalty (a tax of 40% is applied to remission of proceeds exceeding 20%); guarantee that the Central Bank will provide the foreign exchange for such remissions; and a guarantee that invested capital may be repatriated after the third year from the date of its entry into the country.

For the purpose of the law, a company will be considered a foreign capital company when it is an enterprise whose capital originating from abroad is more than 50%. However, a company with less than 50% foreign capital may also receive the benefits of the law with the special permission of the Office of Planning and Budget (OPP).

While giving the foreign investor a number of guarantees, the law also prevents the use of medium and long-term internal credits. The law requires the express authorization of the Executive Branch for investments in the following sectors: electricity, hydrocarbons, basic petrochemicals, atomic energy, exploitation of strategic minerals, finance, agriculture, meat-packing, railroads, telecommunications, radio, press, television, and those, which by law, are to be carried out by government agencies.

Applications for investments under the terms of this law must be submitted to a five-member Advisory Group which must issue a resolution, approving or disapproving the application, within 30 days of receipt.

Foreign companies already in the country were given a time period, which expired in May 1975, to decide whether or not to come under the benefits of the law. Companies with foreign capital already established in Uruguay which do not choose to qualify for operation under the Foreign Investment Law will continue to operate under the existing regulations in force prior to the date of issuance of the Law.

Since the relatively short period of its inception, one new investment has been made under the terms of this law.

In sum, the provisions of the Foreign Investment Law allow substantial flexibility for foreign investors wishing to operate in Uruguay and is not discriminatory with regard to foreign capital of any country.

4. Law on Readjustable Instruments

Private companies whose stock is quoted in the local Stock Exchange were authorized to emit readjustable obligations by a law passed in September 1974. The following are the requirements for the emission of such obligations: (a) the total amount emitted cannot surpass 30% of the capital and reserves in the last annual adjusted balance of the company; (b) the periodic readjustment to be applied to the value of the obligations must not surpass the annual increase registered in the average wage increase; (c) the time period and other conditions for collection and amortization of these obligations will be fixed by each issuing company with the approval of the Stock Exchange; (d) the capital invested in these obligations is exempt from the tax on capital (impuesto al patrimonio), whether the holder of the obligation is an individual or a corporation. To date, we know of no company which has issued these obligations.

5. Proposed Monetary Correction Law

A bill was submitted to the Council of State in April 1975, which proposed the authorization of medium or long-term "development loans" with readjustable or indexed repayment terms. The proposed law would allow local currency credits of greater than two years, to be made available to the manufacturing and agricultural sectors, which presently have access, through the banking system, only to short term credits (i.e. one year or less for regular loans and two years for some capital goods loans).

In recent years indexed credits have been limited to the housing sector, through the State Mortgage Bank, a moderate number of supervised pasture improvement loans under the IBRD-financed Livestock program, implemented through the BOR, and credits under the now expired USAID capital goods import loan (L-022).

These development loans would be obtained through the BOR and through other commercial banks. However, the private banking system would also be authorized to grant readjustable loans for long term investments, to firms which have been declared "of national interest" under the terms of the Industrial Promotion Law. If enacted, this law would be another step toward implementing the guidelines of the August 1973 San Miguel meeting, which called for the creation of readjustable monetary correction systems in priority development sectors, among other reforms.

6. Other Tax Incentives

In early August 1974, shortly after taking office, the new Minister of Economy and Finance, Alejandro Vegh Villegas, repealed personal income and inheritance taxes, eliminated a number of minor taxes on consumer items and greatly reduced export taxes on wool and beef.

The elimination of the personal income and inheritance taxes was designed primarily to make the country more attractive to investments, both foreign and internal. Both taxes provided relatively insignificant amounts of revenue to the central government and were difficult to collect due to inefficiencies of the local tax system. The elimination of minor consumer taxes was an effort to reduce consumer prices on these items, to slow down the increase in the cost of living. The reduction in export taxes was designed to stimulate traditional exports in a period of falling world prices.

C. Trade Cooperation and Development

1. Uruguay, through the Latin American Free Trade Association (LAFTA), participates in complementation agreements with member countries in a numuer of manufacturing sectors. The most important of these in recent years has been the automobile sector, which requires Uruguay to export component parts, tires and tubes to Argentina and Brazil in a volume equal to the value of imports of automotive kits from those countries. The value of Uruguay's exports of automotive parts increased by over 300% between 1972 and 1973 (US$500,000 to US$ 2.3 million). Final figures are not yet available for 1974 exports but it is estimated that these increased by over 100% to about US$ 4.5 million.

2. Argentine and Brazilian Treaties of Economic Cooperation and Trade

On March 31, the Argentine Government issued a decree which eliminated tariffs on 504 Uruguayan-made products whose entry had been the subject of quotas negotiated under terms of the August 20, 1974 Treaty of Economic Cooperation and Trade. The duty-free quotas theoretically represented 5% of 1973 Argentine production of the approved products. The 504 products were selected from over 10,000 submitted by Uruguay; however, a decree granting duty-free entry to an additional 600 products is reported to be in preparation.

This trade treaty represents the first step in the Uruguayan policy (as outlined in the 1973-77 development plan) of gaining access to markets in neighboring countries. By these means, it is hoped to increase the efficiency of the Uruguayan manufacturing sector, which has been hampered for many years due to insufficient domestic or export markets, the lack of export orientation on the part of some firms, inadequate supply of raw materials, due to import constraints, and an inability to compete in world markets due to antiquated plants and outdated marketing practices.

In many cases, the duty-free export quotas greatly exceed the presently available production capacity. However, because access to these quotas is guaranteed for ten years, an orderly expansion is now possible, Since many of the liberated products are also presently in short supply in Argentina, there should be no immediate marketing problems for them.

In a complementary agreement, also signed in August 1974, the Argentine Central Bank opened a US$ 50 million line of credit to finance Uruguay's imports of capital goods from Argentina. The terms of the credit are ten years, with a 21 month grace period, at 7 ½% annual interest on the balance. Imports under this loan have recently begun.

A similar pair of agreements, granting access to the Brazilian market and providing a line of credit for the purchase of Brazilian capital goods, have been completed and will be officially signed on June 12, 1975. The trade agreement is basically the same as that negotiated with Argentina. The US$ 50 million capital goods credit is being made by the Banco do Brazil to the Central Bank of Uruguay and terms are for 10 years, with 21 months grace period at 7 ½% interest.

Other minor agreements have also been negotiated with Paraguay and Bolivia, in a GOU effort to establish bilateral trade agreements as an alternative to LAFTA integration which , in the eyes of many Uruguayan officials, has failed to live up to expectations regarding access to the markets of neighboring countries for Uruguay's products.

D. Financing for Industry Development [1]

1. Introduction

Uruguayan capital and financial markets have undergone profound transformations over recent periods, changes which have arisen from characteristics of the system itself and from the economic evolution of the country. Some of the more salient of these in terms of this project are presented below.

Uruguay experienced very slow growth in terms of gross national product in the recent years as shown by the following table.

Table 5

Uruguay - Growth in G.N.P.

Period	Avg. %
1945 - 50	5.4
1950 - 55	4.3
1955 - 60	0.3
1960 - 65	- 0.4
1966 - 71	1.7

During the period 1955-60, per capita income dropped by 1.1%, continued dropping during the period 1960-65 by 1.8% and was essentially stagnant during the period 1966-71.

Such data indicate an unfavorable environment for the development of financial and capital markets to provide financing for development in the private sector for two basic reasons. First, the absence of growth reflects a shortage or lack of opportunities to expand existing activities. This is not to suggest that such opportunities did not exist, but rather that given the economic and financial environment of the recent period, such opportunities as existed and were identified could not profitably be undertaken. An example of the implications of this point is the low profitability of the shares which were traded on the Uruguayan stock exchanges.

1/ Sources of all statistical data presented in this section are research papers presented at the OAS sponsored "Seminar on Capital Markets" of December, 1973, published by the Banco Central of Uruguay in a bound volume.

(described below). Secondly, as per capita income diminishes, the rate of savings drops even more, contributing to an even greater scarcity of savings for productive investment. The rate of savings and investment in Uruguay, in fact, declined from 14% in 1955 to 9% in 1970.

Among those reasons which can be cited to explain the slow economic growth of Uruguay are two which have importance with regard to financial and capital market activities in support of industry development: the rate of inflation, and the inefficient allocation of internal resources.

Inflation has unquestionable repercussions on the entire financial system, seriously affecting the value of fixed income assets such as bonds and debentures, especially when they are long-term and are accompanied by institutional rigidities regarding affixing of interest rates or the mobility of financial resources. With regard to resource allocation, the economic development model followed by Uruguay since the beginning of the Second World War was one of emphasizing import substitution with emphasis on industrial development to supply the internal market. This model exhausted its growth capacity in a few years, given the small internal market, and contributed to problems which acted as a brake on development for other sectors of the economy. With economic stagnation, and balance of payments difficulties, foreign investment capital, which had earlier been an important support for national development, also decreased significantly. Continuing problems in the foreign trade sector contributed to the development of numerous policies which distorted the allocation of resources and which were reinforced by policies designed to contain inflation without at the same time containing the tendencies for expansion of public sector spending.

That the Uruguayan authorities have recognized the defects of earlier policies and are taking appropriate corrective action in regard to fiscal, monetary, wage and price, and trade and investment policies has been described in earlier sections. If, as expected, the new policies result in more efficient internal resource allocation, resultant growth in the nation's capital and financial markets will be a powerful assistance for accelerating development.

2. Characteristics of the Capital Markets in Uruguay

The formal market channels financial resources through two basic subsystems: through the banking system, and the stock exchange. A third informal or unofficial system of financing ("para-bank") is composed of business credits, consumer credits, and other "extrabank" credits, the importance of which increased over recent decades as the formal market was unable to respond to the requirements of the financial needs of the economy.

The formal market financial system is largely state-directed and private sector involvement in it is subject to strict regulations. The GOU has a monopoly in the mortgage area, and the Bank of the Republic (BOR), the bank of the Government, supplies 41% (1973) of the bank credits which the private sector received, and channelled almost all the bank credit (81%) directed to the Government in the same period. Of the issues traded on the stock exchange in 1973, 80% corresponded to issues of the government sector or its institutions.

Within Uruguay, there is no clear division between the short term money market and the medium-long term capital market.

a. The Bank of the Republic (BOR)

In actuality, the BOR is the largest commercial bank in the country, and is also the depository of the funds from the public sector. The BOR participates in both the money market and the capital market, the latter by virtue of providing financing over one year term through its Development Promotion Division (see below).

b. Commercial Banks

There are 28 private commercial banks in Uruguay, in addition to a "casa bancaria", which cannot receive deposits but can make loans and operate with foreign credits, and a "caja popular", which cannot operate with foreign money. The functions of the commercial banking sector are those of the typical role of short term financial intermediation. The number of commercial banks declined substantially in the recent years. In 1961 there were 61 commercial banks; also in 1961, [illegible]1 "cajas populares" were doing business.

c. Other Institutions

In addition to the above, the Banco Hipotecario del Uruguay (Mortgage Bank), the Caja Nacional de Ahorro Postal (Postal Savings Bank), the Banco de Seguros del Estado (Insurance Bank) and the Banco de Previsión Social, operated in their respective non-industry support areas. Also, under the category of "other financial intermediaries" are businesses which provide short term consumer credit.

3. Activities

Uruguay's capital market experienced a rapid expansion during the period of 1940 to 1950. Because of the importance of its financial sector which was noted for its agility and efficiency, it was considered to be the "Switzerland" of Latin America. This privileged position deteriorated over time and the financial system contracted as measured in real terms or in terms of the national capital of the country. On the other side, the informal market grew, particularly in recent years although data to confirm the exact extent and size of this growth does not exist.

a. Banking Sector

Table 6

Banking Credit to the Public Sector
(Millions of 1961 pesos)

		Index
1941	656	100
1950	1,261	192
1960	809	123
1970	1,223	186

As shown in the above table, between 1940 and 1950 banking credit to the Government practically doubled, experienced a strong contraction in the initial period of the sixties and recovered somewhat in 1970. The figures for the recent period are somewhat misleading however, since a great portion of the credit issued by the BOR and the Central Bank between 1960 and 1970 was channelled directly to the Government.

Table 7

Banking Credit to the Private Sector
(Millions of 1961 pesos)

	Banks Local Currency	Banks Foreign Currency	Mortgage Bank	Total	Index
1940	2,361	-	1,528	3,889	100
1950	4,357	265	2,024	6,646	171
1955	5,119	559	2,453	8,131	209
1960	4,673	706	1,499	6,878	177
1970	1,887	729	125	2,741	70

As can be seen in Table 7 , the expansion of credit towards the private sector was sustained in the period 1940-55, the period of rapid growth in the general economy. With the beginning of the decade of the 1950's, foreign credits flowing into the country augmented the flow of internal banking resources and were a stabilizing element in an otherwise contracting situation. Also at this time the mortgage system was expanding, contributing to internal financial growth.

A major element of the expansion of private sector credit was the GOU's use of rediscount mechanisms which during 1950 to 1960 were directed almost exclusively to this sector. The utilization of this mechanism subsequently had great influences on the financial system, creating distortions in resource allocations and contributing to inflationary pressures through injudicious usage. The increase in credit to the private sector continued until 1958, the year marking the end of the period which could be called one of mild inflation (less than 15%), and the following year price increases amounted to 44%. These years were also the period of initiation of economic stagnation, with the GNP growing at an average rate of 0.3% per year. During the period 1958 to 1970, private sector credit dropped to a third of the 1955 level.

Primary causes for the decline in credit were: the inflationary process which accelerated considerably and which brought as a consequence a general decline in bank deposits; the rediscount policy of the Government which channelled monetary expansion towards public sector activities instead of the private; and lastly, banking charges increased substantially as banks sought to cope with inflation and declining deposits increasing the restrictive effect of the decline in deposits.

As shown in the following table, bank deposits practically doubled between 1941 and 1950, remained relatively constant between 1950 and 1960 and then declined significantly.

Table 8

Total Bank Deposits (Pesos and other Currencies)
(Millions of 1961 pesos)

	Public Sector	Private Sector	Total	Index
1941	128	2,448	2,576	100
1950	470	4,427	4,897	190
1960	891	4,056	4,947	192
1970	802	1,909	2,711	111

Since the figures above include foreign funds, the following breakout is presented to indicate more clearly the behaviour of local internal resources separated into sight and time deposits.

Table 9

Private Sector Deposits in Uruguayan Pesos
(Millions of 1961 Pesos)

	Sight Deposits	Time Deposits	Total	Index
1940	618	1,584	2,202	100
1950	1,499	2,928	4,427	201
1955	1,010	2,764	3,774	171
1960	1,140	1,893	3,033	138
1970	672	980	1,652	75

This table indicates that deposits doubled in the period 1940 to 1950 followed by a decline in the period to 1960 and 1970. The table also indicates the relative importance of sight deposits over time deposits during the period. In 1940, 28% of total deposits were sight deposits as compared with 41% in 1970. In absolute terms total sight deposits show no variation when comparing totals for 1940 and 1970, although there was considerable fluctuation in intervening years. The reduced total availability of funds is caused by the variation in time deposits.

b. The Stock Exchange.

The second center of formal financial activity is the stock exchange. Between 1946 and 1950, the Uruguayan stock exchange was a center of great activity which brought together capital from diverse sectors including those resources of foreign investors who were seeking new horizons in countries not affected by the Second World War. However, beginning in 1951, a process of constant decline began which extends to the present, as shown by the following table.

Table 10

Total Movement on the Uruguayan Exchange (Bolsa)
(Millions of 1961 Pesos)

	All Fixed Income Securities	All Shares	Total	Index
1946	962	265	1,227	100
1950	859	209	1,068	87
1955	505	86	591	48
1960	331	69	400	33
1966	303	87	390	32
1970	89	18	107	9

The decline in activity corresponded to a loss of profitability in shares (and business) and a deterioration in the expectations of future profits, all due to elements such as inflation, the economic stagnation, and the resultant decrease in dividends distributed to shareholders provoked by problems of cash flow, increasing labor costs, growing taxation burdens, and restrictive regulation on banking and production. The bulk of the issues traded over the period were fixed payment securities, with interest rates of 5-6%, which represented substantial negative rates of return to investors as inflation worsened.

4. Sources of Financing for Industry Requirements.

As the above sections indicate, the Uruguayan economy as a whole has been essentially stagnant for some time, and the private sector has received a continually decreasing share of financing available from the financial and capital markets. In particular, there has been an almost total absence of availability of credit on longer than commercial or short term schedules to facilitate capital plant replacement, expansion or development. Nonetheless, limited industry activities do go on and the question which arises concerns how the private sector obtains needed financing, given limited or minimal capital market availabilities. The table presented below presents an average picture of sources and uses of funds by Uruguayan industries.

Table 11

Sources and Uses of Funds in Industrial Enterprises
(percentage)

Uses	1966-67	1967-68	1968-69	1969-70
1. Current Assets	80	88	75	76
2. Non-Current Assets	20	12	25	24
Sources				
3. External (to the firm), short-term	41	58	47	51
4. External, long-term (mainly taxes-"fiscales")	21	8	14	17
5. Internal (Retained Earnings Depreciation)	26	25	31	20
6. External, Private	12	9	8	12

The following principal observations are suggested from this data:

- the high proportion which current assets represent in regard to total uses (between 75-88%), most of which represents investment in inventories and raw materials,

- investment in fixed assets represents a low proportion of uses although it has tended to show a small rise in recent years,

- the very low proportion of internally generated funds as a source of financing, no more than 20% in 1970 (compared with 42% in 1960),

- bank credit has become the principal source of short-term financing replacing suppliers credits.

In sum, the data present a picture of the low or non-availability of funds at medium to long-term for industry which corresponds to the reduced rate of savings and investment available within the country in the last twenty years, produced largely by the inflationary process which tended to detour investment funds towards short-term activities with higher returns and more manageable lesser risks or into flight capital.

An additional factor to be noted regarding the low investment of funds in fixed assets is that a significant, increased portion of that investment, financed from a reduced base of savings over recent years, has been directed to replacement of existing plant and equipment as shown in the following table.

Table 12

Gross Domestic Investment

Years	Rate of Savings and Investment	Percentage of total Investment used for Replacement
1955	14%	30%
1960	17%	21%
1965	10%	31%
1970	9%	38%

a. Primary Sources of Credit for Industry - Financial Market

The credit made available to the private industry sector is channeled primarily through the BOR, the official commercial bank which handles the largest volume, and the other commercial banks.

The BOR attempts to meet the credit requirements of the industry sector through three services: "Industrial Credit", the Division of Development Promotion and the Department of Foreign Negotiation.

Industrial Credit attends the working capital requirements of business, raw materials and materials and various expenses of construction. The operations of this section follow a strict commercial banking approach.

The Division of Development Promotion was set up to provide credit assistance to projects which produce substantial benefits to the country. This division also attempts to channel resources from international financial organizations as well as its own to such beneficial projects. Its specific objectives are to promote industries which have important import substitution aspects and those which increase exports. The credits available from this Division represented practically the sole source of medium or long-term financing for industry, with the exception of an occasional special line of credit for the purchase of machinery or capital goods channelled through this Division directly to the entire banking system. Processing of loan requests frequently was exceptionally slow due to excessive bureaucracy. In addition to project financing, pre-investment studies could also be financed. Terms of loans provided with available funds are up to 10 years with 2 to 3 years grace; up to 80% of the total amount of the project may be eligible. Interest rate charged is 11.75% payable in the currency of the loan.

The Department of Foreign Negotiations finances certain industry import and export operations. Existing lines of credit available are limited by the budgetary allocations and special requirements of the operating policies of the BOR itself, in terms of procedures and restrictions. Within the area of pre-export financing, the Department administers a line of credit originating from funds generated under an earlier PL-480 program, and subsequently augmented with the BOR's own resources. This line finances working capital for exporting. Requests to use this credit are sent first to the Ministry of Industry and Energy which, through the Technology and Productivity Center, makes a technical analysis of the proposal, and may also make specific technical recommendations which are to be included in the credit agreement concerning organization or administrative matters of the business applying for the credit. This program represents the sole mechanism in the entire industrial credit sector which comprises aspects of a supervised credit approach, although, in practice, the system does not work always as intended for lack of technical personnel for follow-up.

The table presented below indicates the percentage of total credits made available by the divisions of the BOR for industry and external trade of its total availabilities.

Table 13

Placements by the Bank of the Republic
(Outside the Banking Sector)

(Percentage)

Years	Agropecuaria	Industry	External Trade	Commercial	Consumption	Others	Total
1967	17	16	11	7	17	32	100
1968	31	12	8	4	17	28	100
1969	27	17	6	5	17	28	100
1970	35	23	8	6	11	17	100
1971	33	25	16	5	14	7	100
1972	31	22	15	5	11	16	100

Within the private banking sector, all assistance is concentrated in short-term credits, given the term structure of financial resources as well as organization at orientations of the intermediaries. Available lines of credit basically attend working capital needs and, rarely, through rediscounts mechanism in the Central Bank, investments in equipment.

5. Conclusions

Within the Uruguayan financial structure, there is a near complete predominance of activity in the money markets (short term financing) over the capital markets (medium/long term financing). Businesses experience frustration or at best great difficulty in reaching sources of medium and long term credits. The Division of Promotion and Development in the BOR has been unable to meet the financing needs of industry, and alternate sources of required financing do not exist. As a result, industry investment in fixed assets for expansion or development of new activities is very low. Self-financing through internally generated funds by enterprises assumes very low proportions due to reasons such as the narrow and small national markets which tend to restrict in size instead of enlarging problems relating to liquidity, government price regulations, etc. The overall financial needs of the industrial sector are poorly attended. There are few, and in some cases inoperative, lines of credit on medium and long terms for investment in the sector.

Furthermore, credits to this sector are administered with a commercial banking approach with little or no effective application of appraisal banking or supervised credit techniques. It is fitting to note in this regard that the exporting sector has received better service and attention than the rest of the industry, but still at a level very low in comparison with other countries. Other sources of medium and long term financing practically do not exist. (A significant recent exception is the Argentine and Brazilian Line of Credits for Capital Goods imports described in an earlier section). The Uruguayan capital market under present economic and financial conditions of the country serves almost exclusively as a market for the placement of readjustable government issues, which also offer tax discounts.

The foregoing analysis has attempted to establish the financing needs of the industry sector, and to indicate the lack of an effective institutional mechanism for mobilizing savings and other capital for relending at medium and long terms. The evidence presented and the picture described strongly suggests that one means of solving some of these problems would be through the establishment of an institution such as a development bank. Uruguay does not have a development bank although such institutions have been recognized as needed and desirable frequently in the past. Numerous past attempts to create such banks have been unsuccessful for various reasons. However, it is precisely those functions which are performed by a development bank which are currently in such need by Uruguayan industry: financial intermediation (medium and long term especially); development of managerial capacities through technical assistance and coordination; transfer of technologies; and promotion of capital market development activities through equity investments and trading of shares.

The USAID policy as set forth in the CASP as well as the policies of other international assistance agencies is to actively encourage the GOU to authorize the creation and efficient and effective functioning of private development banks. There currently exists broad sympathy in the GOU and the private sector for the establishment of a private development bank. The essential item required to achieve this is a law which will allow private development banks to receive and make medium and long term adjustable loans. In line with current GOU liberalization policies toward private sector activities and complementing measures indicated above, it is clear that influential GOU elements are now moving forward towards the creation of private development banks. While the legal and organization measures necessary to establish such banks may take some time (e.g. 1 to 2 years) a number of specific measures that the GOU will take in administering this and the IBRD Industry Sector loan represent major advances towards this goal. Since a development bank essentially contains investment promotion, project appraisal, and financial management capabilities, it is clear that the policies and mechanisms reflected in this loan in effect would constitute transitional, if informal development banking mechanism. Also critical to the successful establishment of a private development bank will be the GOU's success in its current efforts to stabilize and move the economy forward. Actions taken and to be taken by the GOU are expected to produce renewed confidence in the authorities and a revitalized interest in private sector investment. If they are successful as anticipated, the pressures for an environment conducive to creating a development bank will be increased.

PART IV - THE PROJECT

A. Project Rationale and Justification

A key goal of the National Development Plan is to expand both traditional and non-traditional exports in order to increase foreign exchange earnings and import capacity. This will be attained primarily through diversification of agricultural production along lines of comparative advantage and through agri-industrial integration, all of which will expand employment, income, and general levels of economic activity.

To create the appropriate economic climate conducive to attainment of this goal, the GOU has launched a comprehensive stabilization-development program in agreement with the IMF and IBRD, involving a variety of policy, program and institutional reforms previously described. The Project Committee is satisfied that the measures already taken and those planned for the near future will provide a suitable economic environment appropriate to provide incentives for stimulating new investments in the agricultural and industrial sectors.

Under such circumstances, the GOU is undertaking a vigorous effort to revitalize and diversify agricultural production and to restructure its existing industrial plant toward an export orientation. It has taken a number of economic reform measures (e.g., a realistic exchange rate policy, liberalization of the import regime), which will, in time, reduce substantially the past heavy protection of import-substitution industries and will induce a restructuring of industry toward an export orientation, in which competition and efficiency will be spurred by the need to relate to the international market. As this restructuring process gets further along, a gradual reallocation of resources-human, physical and financial - will occur , away from import substitution and toward export oriented industries which utilize domestic raw material and produce export products in which Uruguay has a comparative advantage. Since Uruguay's economy is based on agriculture, the transformation of its industrial structure will essentially mean the development of agri-industries, including food processing and storage, including meat and fish products and leather and fibre processing. As the reallocation of industrial resources takes place, a new export-oriented industrial infrastructure will be created which will induce a diversification and expansion of agricultural production to provide the inputs to the new industries and new employment opportunities at the farm producer and the industrial processor level.

It is within this context that the basic rationale for the proposed AID loan and the complementary IBRD Industrial Sector Loan is to be found. The AID loan will assist in developing a private agri-industrial infrastructure for food processing and related activities while the IBRD loan will similarly assist the establishment of such an infrastructure, primarily in non-food processing activities.

The AID loan's emphasis on food processing and related industries is designed to ensure that the agri-industries assisted will maximally benefit the target group - Uruguay's small and medium farmers who typically specialize in fruit, vegetable, citrus and dairy production and produce most of the country's non-traditional exports. It will do this by helping to establish agri-industrial enterprises which at once will offer new production and marketing alternatives not previously available.

Since the key to success of any food processing enterprise is the way in which raw material production is organized, the enterprise will necessarily have to structure, incentivize and assist the farm producer to provide a dependable and quality supply of inputs to the plant. Thus, the agri-industrial enterprise will induce small and medium farmers to develop new lines of production needed to supply the plant, to take advantage of new marketing alternatives, which, in turn, should incentivize the producer to adopt new technology and farm management practices to better serve this dependable new marketing outlet.

Given the fact that the GOU's stabilization-development program and export promotion strategy are of recent origin, there has not previously existed in Uruguay an organized availability of the technical or financial services needed to assist the rational development of food processing or, for that matter, any other industries. Nor does there presently exist a functioning capital market in Uruguay nor a suitable development banking mechanism capable of channelling medium and longer term credit or technical assistance to private investors.

In addition, a number of other constraints have hindered the development of export-oriented agri-industries. Except for very few vertically integrated industries, most export industries have serious problems with the production capacity and quality of the various small but vital supporting industries which produce components needed to export the finished product. This is specially true of food industries. Many industries have serious problems in obtaining spare parts and this acts as a disincentive to increase production for export. The problem of raw materials is of major importance for many export industries which need imported products (such as tinplate for canning) to complement the basic locally produced raw materials and also for the support industries which work mostly with imported raw materials. Export industries also need lines of credit at promotional interest rates for working capital, since the existing pre-export financing line does not cover all exports, and normal bank credits are short term and not always readily available, especially for the smaller industries.

The proposed AID loan seeks to provide a package of technical and financial services directly to the agri-industrial entrepreneur, including dollar and local cost financing for feasibility studies, capital and intermediate goods, construction, working capital, and technical assistance requirements necessary to permit sound planning and implementation of industrial projects. In a sense, the proposed loan essentially provides a program of supervised industrial credit geared to the special needs of the growing food processing industry in Uruguay. It also provides the means for assisting small and medium farmers directly through financing farm machinery imports to agricultural cooperatives or contractors which will permit them to organize more efficiently their production for supplying agri-industries or the export market.

The proposed AID loan and the complementary IBRD Industrial Sector Loan also provide a new and viable mechanism for channelling official medium and longer term credits to private sector enterprises thus overcoming a critical past constraint to Uruguayan development. The mechanism, involving a project review process by the Ministry of Industry's <u>Unidad Asesora</u> and a Mixed Committee for final approval, for the first time provides a means of appraising development projects for their technical, economic and financial feasibility and a simple method of channelling official credit through the commercial banking system. This mechanism represents an important preparatory and transitional step to the longer range goal of establishing private development banks, a step long advocated by the international assistance agencies and which now appears to have influential support within the GOU.

The principal established in the proposed loan that the private banking community can participate on equal terms with the Bank of the Republic (BOR) in the AID and IBRD loan programs represents a major breakthrough in incentivizing the private banks to move toward a development financing orientation and compete on equal terms with the BOR in the medium and long-term financing area. For example, the credit insurance or guaranty mechanism incorporated under this and the IBRD loans will significantly reduce excessive collateral requirements in the banking system which have long thwarted financing of productive investments. Likewise, the GOU agreement to remove the six percent banking tax, applicable heretofore only to private banks, will serve to give these banks equal treatment with the BOR in channelling credit to the private sector.

Finally, the proposed loan uniquely complements AID loans previously prepared and authorized in FY 1975. The Agricultural Research and Technical Assistance Loan(US$4.85million)will serve to assist the expansion of a national network of research and technical assistance centers which will produce applied technology and organize its dissemination to the farmer to help expand his productivity and income. The Agricultural Cooperative Development Loan (US$2.0 million) will assist a national secondary-level federated service cooperative to provide reasonably priced inputs to small farmers and help them market their output in the export market.

This proposed loan will provide the final element of USAID's agricultural development strategy by assisting in establishment of new or expanding existing food processing or related industries which will spur new production and marketing opportunities to the same target group. Over the years, agricultural development was severely constrained by the lack of modern and efficient marketing facilities. This loan represents a major step in overcoming that constraint.

The proposed AID loan also complements an IBRD Industrial Sector Loan (US$35.0 million) which will attend primarily non-food processing industrial projects and will utilize the same mechanism and provide financing on the same basic terms and conditions as the AID loan. Likewise, the IDB is planning a US$23.0 million Fisheries Development Loan, providing financial and technical assistance in procurement of fishing boats, construction of port infrastructure and financing private fish processing plants.

Given the currently favorable economic policy framework, the proposed loan complimented by the IBRD and the IDB programs in the agri-industrial sector, could make a significant and relatively rapid contribution to Uruguay's economic recovery and to the institutional development of a functioning capital market. It also will represent the capstone to other AID programs in improving the income and productivity of the small and medium farmers of Uruguay.

B. Project Description

1. Project Background

In FY 1970, AID made a US$15 million Capital Goods Loan (AID L-022) to the GOU designed to spur industrial and agri-industrial development primarily for export and establish a GOU mechanism for reviewing import requests. A key condition of the loan was that the GOU obtain an IMF Standby Agreement, which condition was met. Shortly after the loan agreement was signed in 1970, an IDB loan was made to the GOU for meat packing plant development and this sub-sector was subsequently excluded from eligibility under the AID loan. The mechanism established for processing import applications functioned well after some initial delays and was fully suitable for project implementation purposes. (In fact, in light of its effective performance in channelling medium-term import credits to the private sector, a similar mechanism is being devised by the IBRD in channelling funds from its proposed US$35 million Industrial Sector Loan. The mechanism proposed in this project is a substantially elaborated version of the earlier device.)

During 1970-73, when the GOU restricted normal capital goods imports due to balance of payment stringency, the AID loan was the only source of medium term financing for such imports for the industrial sector. While the private banks participated in the program, most of the transactions under the loan were processed by the BOR given that institution's exemption from a 6 percent bank transaction tax payable by the borrower, which is applied only to private bank transactions.

The peso generations under the loan are, by mutual agreement between AID and the GOU, being relent to the private sector for industrial construction, tourist hotels, and locally made capital goods. The local demand for these funds is strong.

The initial interest rates for AID import financing to the sub-borrower ranged between 6-8 percent with 3-10 years maturity depending on the project and sub-loans were readjustable according to the peso/dollar exchange rate at time of amortization and interest payment.

A further report with statistical appendices on this loan is contained in Annex I.

Given the important function of the AID Capital Goods Loan in financing industrial expansion during its period of implementation, the GOU in

October 1973 requested a supplementary loan of between US$15-20 million. This loan request was indicated in the FY 1973-74 DAP and an IRR was reviewed by the DAEC in January 1974. The results of the DAEC review are contained in State 26780 (see Appendix B). Since one of the loan purposes was to assist in overcoming the balance of payments constraint limiting capital goods imports, the DAEC imposed the pre-condition of an IMF Standby Agreement, prior to further AID consideration of the project.

No action was taken by the GOU to obtain a Standby Agreement until October 1974 when the newly appointed Minister of Economy and Finance formally requested such an Agreement together with IBRD assistance. (An IMF Standby Agreement was eventually concluded and signed in May 1975 - see Appendix A.)

In the meantime, in February 1975, the GOU through its Office of Planning and Budget (OPP), requested a restructuring of its earlier loan request indicating its desire to reorient the loan toward agri-industrial export development and to incorporate a technical assistance component to the original proposal. In light of balance of payments assistance being obtained from the IMF, IBRD, and other sources, the GOU's request for a restructured loan was based on a developmental rationale and not on balance of payments grounds. Aside from the removal of the balance of payments purpose and the inclusion of the technical assistance component, the basic objectives and design of the loan as originally proposed remain the same. The request for a restructured loan, is contained in letters to the AID Representative from GOU Planning Director, J.J. Anichini, dated February 28, 1975 and June 6, 1975 and attached as Annex E.

Once it had satisfied the basic AID pre-condition of an IMF Standby, the GOU reiterated its request for the restructured loan in May 1975 and work to prepare the CAP began in late May. This proposed loan was included as a shelf loan in the FY 1975 Congressional Presentation.

2. Introduction

The project will seek to create an agri-industrial infrastructure capable of expanding non-traditional exports, thereby contributing to increased foreign exchange earnings and increased production, employment and income opportunities for small and medium farmers who produce inputs for processing industries. This objective will be encouraged by the provision of a package of financial and technical services to private entrepreneurs and cooperatives for the establishment or expansion of agri-industries, principally in the food processing area, and by helping to establish an effective delivery system for these services. In addition, the project will stimulate new production and marketing alternatives for small and medium farmers through the establishment of viable agri-industrial enterprises which utilize their products and assist them in production and marketing techniques. As used in this project, agri-industry refers to all aspects of food production, processing, storage, distribution and marketing activities, and related activities directly supportive of these, such as those providing necessary agricultural and non-agricultural inputs, e.g., seeds, packaging materials, agricultural machinery and land development and management services critical to improved functioning of the target enterprises.

Of the proposed US$ 5 million AID loan, the bulk of the loan or approximately US$ 4,500,000 will finance foreign exchange costs for imports of capital goods, spare parts, and essential raw or intermediate processed materials for export-oriented agri-industries and related service industries. Up to an additional US$350,000 of loan funds may be used to finance the foreign exchange costs of technical assistance to assist private entrepreneurs or cooperatives in conducting feasibility studies, in project preparation, and in the administrative, technical and operational aspects of establishing or expanding an agri-industry financed by the project. Finally, up to US$150,000 of the loan will be available for technical assistance to the Borrower for the services of an agri-industry advisor to assist in execution of the Program.

Under the capital goods imports portion of loan funds, sub-borrowers would be able to purchase equipment, machinery and spare parts for all agri-industries, especially industries which process fruits or vegetables, and related service industries, such as those making tin cans, packing boxes, and plastic bags, as well as transportation and storage operations, essential to the production and export of agri-industrial products. A number of industries will, however, be specifically excluded from financing with project funds, including meat packing, fish or fish processing, manufacture of shoes or leather products, textile production, or production of alcoholic beverages. Imports of essential raw or intermediate materials, such as tinplate or other packaging materials, which if unavailable locally act as a constraint to full and efficient production capability, will also be considered eligible if financing for these items is unavailable elsewhere.

The GOU is presently considering the initiation, on a pilot basis, of a program to encourage the establishment of farm machinery service contracting operations in rural areas. Established and managed either by cooperatives or private contractors, these enterprises would possess a package of machinery which would provide needed services to farmers, including land preparation, cultivation and harvesting services, clearing or leveling, work on irrigation canals, and clearing penetration paths to assist in marketing farm produce.

These small farm machinery contract enterprises would own, operate, and maintain a package of farm machinery on a custom fee basis and sell their services to groups of small producers located in defined geographic areas and engaged in the production of similar commodities. The geographic areas would be limited only by the distances that the contractor could cover and still make machinery services available efficiently, timely, and at reasonable costs. The farm machinery "package" would not be standard, but would vary in composition as to type and kinds of implements depending upon the crops and production practices of each contractor's clientele.

Best information indicates that there are about 16,000 farm tractors in Uruguay. However, many of these tractors (a UNDP technician estimates that it could be as high as 50%) are either inoperable or cannot be operated economically due to age and the lack of repairs. If it is assumed that only one-half of the tractors in Uruguay are still operating (8,000), and since Uruguay has a total of about 1,500,000 hectares under cultivation, this means that there is one farm tractor for each 187 hectares (462 acres) under cultivation. This ratio would be considered barely adequate for the most extensive types of farming, such as cereal grain and forage production, but it is totally inadequate for the 50,000 farmers whose enterprises are less than 50 hectares in size. Consequently, the Minister of Agriculture has requested that agricultural production machinery to establish these contracting enterprises be eligible for acquisition under this loan. Because of this GOU pilot initiative, the importation of a package of farm-related machinery by cooperatives or private entrepreneurs will be an eligible component of this project, and up to US$500,000 in dollars may be used in support of approved sub-projects of this type. The farm machinery contract service would operate strictly as a business enterprise and financing for such projects under this loan would be subject to project design, development, feasibility studies, and the same evaluative criteria as any other eligible agri-industrial enterprise. In order to receive financing with loan funds sub-project proposals will have to demonstrate their impact on small and medium farmers and include as part of their project design and feasibility study a satisfactory administrative control procedure to ensure that a major proportion of the farm machinery services will be provided to these farmers.

The technical assistance services to be provided with loan funds will be used to assist sub-borrowers in several areas where present deficiencies exist. A portion of the funds may be authorized to assist prospective sub-borrowers complete comprehensive feasibility studies if their preliminary sub-project proposals meet the selection criteria and warrant further development. Terms for such loans will be recommended by the Unidad Asesora but should not exceed two to three years. In many cases, locally available consultants may be utilized to assist sub-borrowers in this effort, but in others, for instance the establishment of a new enterprise or expansion of a plant into a new line of production, foreign consultants may be required for some aspects of the feasibility study.

A critical element in project development which many prospective sub-borrowers lack is adequate knowledge of and experience in good project design. Therefore, technical assistance from foreign consultants may be justified and authorized to assist sub-borrowers in this area. While this will have the immediate benefit of improved sub-project design for agri-industrial projects financed under this loan, it can also be expected to have long-term benefits in terms of improved design capability within the Uruguayan private sector.

Sub-borrowers may also require outside expertise to implement effectively approved sub-loans. This is most likely to be the case for projects which entail creation of a new industry, in which the entrepreneur may need assistance in equipment installation and rationalization and other aspects of initiating production. Funds for use of outside experts for these purposes would be authorized as an integral part of a sub-project approved under the loan. It is likely that such experts would be recruited with the assistance of the International Executive Service Corps.

The GOU contribution to the project will be equal to at least 31% (US$2.25 million) of total project funds. This amount is approximately 50% of the total amount of peso recuperations from sub-loans made under AID Loan-022 which will be received during the project disbursement period, i.e., through 1978. While, the GOU has not yet specifically identified the source of its counterpart contribution, it is expected that, particularly in the first year of this project, a portion of the GOU counterpart funds may be drawn from these reflows. The counterpart contribution to the project will complement AID dollar funds by financing local costs of civil construction, purchase of existing plant facilities, locally-made capital goods, working capital requirements, and feasibility studies and other technical assistance which are part of approved sub-projects. The GOU has agreed that all local cost needs for approved sub-projects will be met; if these requirements exceed the US$2.25 million initial GOU contribution to the fund, the GOU has indicated it would be prepared to agree with AID on additional contributions.

The GOU, as an additional element of its counterpart contribution, will establish an industrial credit insurance fund or guaranty arrangement to be administered by the Central Bank. A key constraint to medium and long-term industrial investment in Uruguay at present is the excessively high level of collateral required by the commercial banks on loans, which can sometimes be as high as 300%. The purpose of this credit insurance fund or guaranty arrangement would be to protect commercial banks against a substantial portion of the commercial financing risks involved in sub-borrowing as a means of reducing existing collateral requirements which hinder investment credit. The fee for this insurance or guaranty mechanism would be passed on to the sub-borrower as part of the sub-loan financing agreement. This credit insurance or guaranty arrangement would be optional for the sub-borrower although we anticipate that the majority will take advantage of it. The Central Bank will either earmark a portion of its reserves to support this credit insurance fund or alternatively agree to guarantee each commercial bank loan up to 70-75%. The GOU will prepare, as a condition precedent to initial disbursement, an acceptable, specific proposal, including a time-phased implementation plan, for the establishment of this credit insurance fund or guaranty arrangement.

3. Target Group, Beneficiaries, and Benefits

The ultimate intended beneficiary and target group of the project is the small and medium farmer who is the producer of crops used as inputs by non-traditional export-oriented agri-industries and who will be stimulated to new marketing and production activities by the establishment or expansion of agri-industrial enterprises which use their produce. The initial beneficiaries of the project will be the private entrepreneurs and cooperatives who will invest in and operate the agri-industries financed through the loan. This group will act as intermediaries in extending the intended benefits to the small and medium farmers and will benefit themselves by receiving credit for their agri-industrial sub-projects and techncial assistance in project design and implementation. The productive sectors of the economy as a whole will also benefit from the creation of an intermediate delivery mechanism for channeling credit and technical assistance to viable development projects.

The exact number of small and medium farmers who will benefit from the project is unknown, as it depends to a considerable extent on the location and types of agri-industrial enterprises that will be financed. However, by end of the third year of the project it is anticipated that a significant portion of Uruguay's approximately 75,000 farmers will have benefitted in some significant way.

Uruguay has very few of the small, subsistence-level farmers living on a fractional piece of land who are outside the market economy and who generally constitute the "poorest of the poor" in many other Latin American countries. Nor does Uruguay have any large numbers of farm workers (empleados rurales). While there are a number of partially-employed people who rent a small piece of land near Montevideo to produce enough to survive while waiting for job openings, the great majority are producing some cash crops. Unfortunately, there is very little income distribution data available at present, although

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the results of a national census conducted in May 1975 should provide this kind of information. In addition, as part of both the recent AID loans to IATA and CALFORU, baseline information on the target farmer will be compiled which will provide a greater data base on this group. Accordingly, this loan project must be considered in the context of Uruguay's social and economic development with an agricultural sector quite distinct from other countries in the region.

Uruguay considers "minifundia" to be defined as follows:

Livestock	Less	than	200 ha.
Crops	"	"	50 ha.
Dairy	"	"	50 ha.
Fruits and Vegetables	"	"	20 ha.
Vineyards	"	"	5 ha.

Under this definition, 68% of Uruguay's farmers qualify as small farmers. Producers of non-traditional export crops (e.g., fruits and vegetables) are typically at the lower range of the farm income scale, i.e., relative to producers of traditional exports (beef and hides). Therefore, the selection of this target group is consistent with AID priorities to reach lower income farmers in the context of the country being assisted.

Small farmers are located in greater intensity in the area around Montevideo, particularly in the Departments of Canelones, San José, the southern part of Florida and the southeastern part of Lavalleja. In the rest of the country, small farmers are located near department capitals and the large towns, due primarily to better transportation and other facilities, rather than to type or quality of land. Their location, thus, allows small and medium farmers to greatly benefit from agri-industries which might be established or expanded, which generally will be located in Montevideo or other large towns.

a. Characteristics of Land Holdings and Land Use

There have been no recent comprehensive studies on land use in Uruguay agriculture, the lack of which has been a major impediment in sectoral planning. To remedy this deficiency, the IBRD will carry out a six month agricultural land use and diversification study, financed by UNDP at a cost of $350,000, on actual and potential productivity of arable land. A key objective of the study is to identify viable agricultural development projects appropriate for IBRD and/or other assistance agency financing.

Information available is from the agricultural census of 1972 which gives the total number of farms in the different size groups, the total hectareage and general use of the land in these size groups.

The types and size of farms are distributed geographically over the country on the basis of soil type. The larger farms are on the shallow soil grazing area; the mixed grain and livestock farms are on the deeper soils; and the smaller fruit and vegetable farms on the deep soils closer to the urban areas.

The three smallest size groupings -- those under 20 hectares -- tend to concentrate on horticulture and fruitculture and account for about half of the nation's total area in fruits, vegetables and vineyards. If one also includes the farms in the 20 to 49 hectare group, 77 percent of the total area in vegetable, fruits and vineyards is accounted for.

Field crops constitute over 10 percent of the land use in the next four size groups -- those from 20 hectares to 499 hectares. (As pointed out earlier, fruitculture and horticulture are important in the 20-49 hectare group.) One also finds the majority of the dairy cattle in the 20 to 499 hectare groupings. A 1968 study by the Ministry of Agriculture determined that the average size of a dairy farm was 104 hectares.

While field crops constitute an important source of income in the 20 to 500 hectare size groups, these farms typically are mixed livestock-grain farms. Statistics indicate that from nearly 70 percent to over 85 percent of such land is used for grazing.

Those farms with over 500 hectares are basically grazing operations. Field crops are not so significant in the total income per farm; nevertheless, they account for about 40 percent of the total national area in field crops, chiefly wheat.

b. Facilities Available to Target Farmers

The target farmer who lives near Montevideo and the other cities, generally has good roads, school and health facilities. As one gets farther away from the urban centers, these facilities become scarcer and of a poorer quality.

Less than five percent of all farm families have electricity. All have adequate water available, for the nation has good ground water resources.

Rural credit facilities include: (1) private banks, mostly providing short-term capital for purchase of livestock; (2) the Bank of the Republic (BOR) which has a number of short-term credit lines mainly for crop production, and two year credits for purchase of livestock and machinery; and (3) IBRD and IDB sponsored intermediate and long-term loans for the livestock and citrus programs. (See Agricultural Credit Study contained in Annex J.)

The target group of farmers is thought to be receptive to change. However, before they will adopt new techniques, they must be convinced of three things: (a) that policies affecting agriculture will be favorable and maintained over time; (b) that markets and marketing facilities will be available; and (c) that they will have a good return on their investment in new technology.

c. Economic Profile - Fruit Farm

As an illustration of the farm operation of a member of the target group, the following profile of a fruit farm is included. While useful for illustrative purposes, many small farmers who will be benefitted by the project probably earn substantially less than indicated in this model.

Deciduous fruits are produced in Uruguay, essentially on farms from 1 to 500 hectares in size. However, two thirds of the peaches and a half of the Delicious apples in 1970 were produced on farms less than 20 hectares in size.

A unit of fifteen hectares of fruit which typically would have a hectare of vineyard and another of uncultivated grazing land for the family cow, is used for the economic profile of this target farmer.

Orchard	Hectares	
Peaches	5.8	
Apples	2.8	
Pears	.7	
Plums	.7	
Quince	1.0	
Total Orchard	11.0	
Vineyard	1.0	
Uncultivated Land	2.0	
Grazing	1.0	
Total Farm	15.0	
Gross Income from Sales		$4,800
Production Costs		3,000
Net Farm Income		$1,800
Plus Value of "on farm" consumption		400
Net Family Income from Fruit Farm		$2,200

4. Project Functioning

The project will place a major emphasis on establishing a special mechanism within the GOU to evaluate development project proposals and channel a package of medium-term credit and technical assistance quickly and effectively to the private sector. The principal GOU agency which will be involved in this mechanism, the Unidad Asesora in the Ministry of Industry and Energy (MIE) is described in Part V., Section A. The mechanism to be used for the project will work as described below.

In order to be eligible for financing under this project, sub-projects must meet the following selection criteria:

1. Target group - The sub-project must have a significant impact, in terms of increased employment, increased production or marketing opportunities, and/or increased income benefits, to small and medium farmers in Uruguay. The description of the target group will be refined in quantitative terms (i.e. income levels and number of hectares farmers) by the Unidad Asesora in the course of developing plans, standards and procedures for project review and appraisal, in accordance with Conditions Precedent to this loan. Potential sources of relevant data for determining quantiative definitions of the target group may be found in early results of (a) the May, 1975 Agricultural Census and (b) data to be developed on similar target groups under the IATA and CALFORU projects.

2. Characteristics of the enterprise - Priority consideration will be given to sub-projects which (a) utilize normal agricultural raw material which has been produced or has potential for increased production; (b) involve minimum packaging costs and complexity; (c) utilize uncomplicated technology; (d) maximize utilization of existing facilities; (e) complement existing facilities; (f) involve uncomplicated marketing; (g) operate effectively within existing limitations; and (h) complement the domestic market. In addition, enterprises financed under the project must not receive excessive protection, must exhibit good management, must be solvent according to normal commercial bank or Bank of the Republic standards, and must have an internal rate or return of at least 10%.

3. Export orientation - Sub-projects chosen for financing should be export-oriented in one of the following ways: (a) actual production is substantially export-oriented; (b) present production is only export-oriented to a minor degree, but prospects for increased exports are good; (c) interesting export prospects exist if equipment is modernized; and (d) new enterprises whose production will be principally export-oriented either at the outset or after filling an existing domestic demand.

4. Excluded enterprises - The following types of enterprises will be excluded from financing under the project: (a) meat or meat-packing facilities; (b) fisheries or fish processing activities; (c) textile manufacture; (d) shoe manufacture; (e) leather or leather products processing; (f) manufacture or marketing of alcoholic beverage; (g) wool processing or manufacture; (h) those which involve purchase of property owned by the GOU or any instrumentality thereof.

The Unidad Asesora will follow procedures similar to those outlined below in appraising each sub-project. The Technical Unit of the Unidad Asesora has elaborated a detailed project evaluation procedure for all projects it analyses, on which the following discussion is based. These procedures will be supplemented to a small extent for projects reviewed for approval under this project. Therefore, while the specific procedures adopted by the Unidad Asesora for this project may be slightly modified to be more fully in accordance with local conditions and their normal operating procedures, the appraisal process will involve all of the major components mentioned below.

A private entrepreneur or cooperative will present an agri-industrial project or ante-project for financing to a commercial bank or the BOR. The sponsors of the proposed sub-project will prepare a questionnaire, which will accompany their initial proposal to the Unidad Asesora through the sponsoring bank. (The form of this initial questionnaire is set forth in Annex K, Exhibit 1.) The bank, after screening the sub-loan request in regard to general aspects of the proposed project and financing request, as well as credit standing, references, and other typical concerns of commercial banks, will present the proposed sub-project to the Unidad Asesora. The Unidad Asesora will review the questionnaire and prepare a written summary identifying, among other items, the following: (a) items in the questionnaire which require additional data from the applicant; (b) references to be checked; (c) financial analysis required, including the nature of the investment proposed and alternative means of structuring financing; (d) technical review required, including time phasing; (e) market data needed;* and (f) a preliminary assessment of the overall prospects of the proposal, including the degree to which the proposal satisfies the selection criteria. In determining the eligibility of the sub-project according to the selection criteria, the Unidad Asesora will complete a Project Assessment Form (Annex K, Exhibit 2) based on the information submitted by the prospective sub-borrower and use this as a basis for applying these criteria.

The Unidad Asesora will then make a decision as to whether an intensive examination of the proposal is warranted, and will notify the sponsor as to the results of its review. If the sub-project meets the project eligibility criteria, but is incomplete, poorly designed, or in need of further feasibility study, the Unidad Asesora may authorize the use of project funds as a loan to the applicant to finance technical assistance in conducting the required studies or in project design. If and when the sub-project proposal contains the necessary information and feasibility studies, the Unidad Asesora will appraise in detail the sub-loan proposal to establish its technical, economic, and financial feasibility.

(*) It is expected that a satisfactory marketing analysis will accompany the feasibility study for each sub-project. Such analysis will document opportunities for domestic or export sales (as appropriate), expected revenues, and any steps necessary (e.g., improvement of processing quality control or grades of produce processed) to insure successful sales in the market(s) selected. An initial survey of market potential may also be required in the pre-feasibility stage of a given sub-project.

Following confirmation of the completeness of the proposal and its eligibility under the project, the Unidad Asesora will examine the sub-project's cash flow and ability to amortize the proposed sub-loan within a 5-10 year period. In addition, the Unidad Asesora will examine in detail the following aspects of the sub-project proposal:

1. Quantifiable indicators

(a) Its profitability and contribution to GNP through cost-benefit analysis and assessment of its internal rate of return.

(b) Its contribution to exports through computation of net foreign exchange earnings.

(c) Its contribution to employment generation.

(d) The percentage of domestic raw materials used (must be over 50% to be approved).

(e) Its profitability and international competitiveness, through analysis of its: (1) ability to produce at international prices; (2) profitability to the entrepreneur; (3) break-even point; (4) financing arrangement; (5) operating capacity; and (6) accordance with the legal framework. Other indicators of productivity, degree of mechanization and degree of organization will also be evaluated.

2. Unquantifiable indicators

Subjective but reasonable assessments will be made of its contribution to the improvement of income distribution, diversification of production, industrial integration with neighboring countries, and production capacity of basic inputs needed by other Uruguayan industries which meet these same criteria. A key element of each feasibility study will concern the plans of the sub-borrower to organize the needed raw material production on which the agri-industry must depend.

Technical analysis of the proposal will be undertaken by the Unidad Asesora, consulting, as appropriate, with other technical branches of the MIE or other GOU Ministries or agencies. In particular, in the case of project proposals for farm machinery packages by cooperatives or private contractors, proposals will be referred to the appropriate offices of the Ministry of Agriculture, as necessary, to insure thorough technical analysis. The Unidad Asesora estimates that depending on the type of sub-project and the quality and completeness of the proposal, its analysis should take from 3-5 months.

The Unidad Asesora, on the basis of its in-depth appraisal of the sub-project proposal, will recommend whether the sub-loan should or should not be made using project funds. If it concludes the project should be financed, it will prepare a report of its appraisal, which will include a completed Project Assessment Form and the Unidad's suggestions for the amortization terms for the sub-loan, and forward its recommendations to the Office of Planning and Budget (OPP), the Ministry of Economy and Finance, and the Central Bank. These entities will review the Unidad Asesora's report and recommendations, and at a time to be set by OPP, representatives of each will meet as in constitution of a Mixed Commission which will determine the sub-project's conformity with the project selection criteria and GOU development policies and priorities. The Mixed Commission, which will function in the capacity of a board of directors, will then approve or disapprove the sub-project. Approval must be by unanimous vote. AID will reserve the right to review and approve sub-projects using over US$350,000 of AID dollar funds, following Mixed Commission review and approval.

As part of its sub-project analysis and approval process, the Unidad Asesora will determine whether the sub-borrower requires technical assistance of any kind in order to implement effectively the sub-project. If it determines technical assistance is necessary, it will arrange financing for this and include it as part of the sub-loan package. A major obstacle in providing appropriate technical assistance to sub-projects is the lack of knowledge of experts in the particular areas of agri- industrial activities. While the prospective sub-borrower and the Unidad Asesora may agree that specific technical assistance is required, substantial effort and time may be spent by each in identifying and facilitating the contracting of such expertise as appropriate. Therefore, as a means of dealing with this constraint, the Unidad Asesora, upon Mixed Commission project approval, and subject to AID review of contracts, will contract with an appropriate entity, e.g., a specialized U.S. consulting firm, or possibly the International Executive Service Corps, for the identification of qualified expertise and assistance in arranging for the technical assistance required by the sub-borrower.

The Mixed Commission, through OPP, will certify its approval of the sub-project to the Unidad Asesora, which will notify the sponsoring bank. The bank will then apply to the Central Bank for (1) local-cost and foreign exchange financing, (2) a credit insurance policy or guarantee arrangement, and (3) arrangements for the import transaction. Mixed Commission approval of a project would automatically authorize the Central Bank to rediscount the commercial bank's sub-loan. The sub-loan would then be made by the sponsoring bank.

The sub-borrower, at his discretion, may wish to further apply to the Unidad Asesora for qualification of his sub-project under the Industrial Promotion Law in order to take advantage of the incentives contemplated by that Law. It is anticipated that, if this application is made at the time the sub-project is initially submitted to the Unidad Asesora, processing of qualification under the Industrial Promotion Law will proceed coincidentally with appraisal under this project. The Unidad Asesora, then, upon making its recommendation to the Mixed Commission for sub-project approval, would recommend to the Minister of Industry and Energy that the sub-project be declared qualified to receive benefits under the Industrial Promotion Law.

The Unidad Asesora, upon Mixed Commission sub-project approval, would be responsible for notifying AID of the foreign exchange requirements of the approved sub-project and make similar arrangements with the Central Bank for the local currency portion of the sub-loan. In response, an AID Letter of Commitment will be opened or increased with the appropriate U.S. bank. Responsibility for opening and processing Letters of Credit will belong to the sponsoring banks on behalf of their sub-borrowers.

The Unidad Asesora currently consults on a regular, but informal, basis with private sector representatives and plans to continue this interchange in implementing this project. It will also set up a private sector advisory panel composed of various representatives of the business and industrial community. It will consult periodically with this panel to discuss the needs and problems of the private sector and ways in which the Unidad might be responsive to them in its sub-project guidance and appraisal.

C. Other International Donor and Bilateral Assistance Activities Related to Project

1. IBRD

On conclusion of an IMF Standby Agreement with the GOU during May 1975, the IBRD began processing a US$35 million Industrial Sector Loan. The loan, expected to be authorized in late Fall 1975, is geared to financing both imports of industrial raw materials, spare parts, and balancing equipment and for plant renovation and expansion. Of the total amount, approximately US$20 million will be allocated for imports of industrial raw materials, spare parts, and balancing equipment which amount will be disbursed within a year and essentially serve as balance of payments support. US$14.5 million is proposed for financing capital goods imports for industrial sector development (primarily non-food processing industries) projects with an export orientation. Sub-projects will be evaluated by the Ministry of Industry and Energy's Industrial Project Evaluation Unit

(Unidad Asesora) and policy approval will be accorded by a Mixed Commission consisting of representatives of the Central Bank, OPP, and Ministry of Economy and Finance.

The proposed AID loan has been prepared in close collaboration with IBRD officials so as to ensure that both the AID and IBRD loans are channelled through the same mechanism and will be utilized by sub-borrowers on substantially the same terms and conditions.

The IBRD plans to allocate the remaining US$500,000 of the loan funds for three technical assistance purposes: (1) to provide a team of experts to strengthen the Office of Planning and Budget and the Unidad Asesora's project review and evaluation capabilities; (2) to strengthen export marketing capabilities and (3) to strengthen the quality control of Uruguayan products. An IBRD Appraisal Mission for this loan will arrive in Montevideo on June 23, 1975. Besides the proposed loan, the IBRD is also the executing agency for a UNDP financed study (US$350,000) aimed at developing a strategy to diversify agricultural production. The Study will also provide a plan of action for the GOU to carry out the strategy and a ten year investment program for agricultural projects.

The IBRD also plans a Livestock Development Loan of approximately US$ 15.0 million to the GOU during CY 1975. This loan will be the fifth installment of IBRD lending in this sector, which is administered by Plan Agropecuario, an agency of the Ministry of Agriculture and Fisheries (MAP). To date the IBRD has made US$54.7 million in loan funds available to this program.

2. Inter-American Development Bank (IDB)

The IDB has made several loans to the GOU in the agri-industrial development area with poor results so far. A US$6.0 million small and medium industry development loan, made in 1970, and channelled through the BOR, was cancelled in 1974 due to the BOR's inability to make disbursements.

A US$13.4 million meat packing loan, made in 1970, has so far only disbursed some US$4.4 million. The principal reasons for slow implementation stem from cost increases of projects due to inflation changes in project design, and slow BOR disbursements.

A principal problem in BOR's disbursement record is its requirement for excessively high collateral requirements from sub-borrowers. Discussions are currently well advanced between the GOU and IDB to cancel or restructure the loan in ways to permit its expeditious implementation.

The IDB has signed in 1974, a US$3.0 million citrus development loan, to be administered by Plan Citrícola, an agency of the MAP with private sector representation. The loan will finance technical assistance and credit for citrus production.

The IDB is also planning to make a US$23.0 million Fisheries Development Loan to the National Fisheries Institute (INAPE) to finance fishing boats for private sector enterprises or cooperatives, fish processing and marketing installations, and port infrastructure. It is expected that this loan will be made in 1975 or early 1976. It is anticipated that the IDB and GOU will agree to use the Unidad Asesora as the project review group for evaluating private sector projects under this loan.

The GOU has requested a US$20 million loan for development of fruit and vegetable production. The loan would be administered by Plan Granjero, another MAP agency with private sector participation. The IDB has financed an Israeli team of experts to assist in the development of this loan. The primary purpose of the loan will be to finance technical assistance and investment credit to farmers working in fruit and vegetable production. Major policy decisions are pending within the GOU on restructuring Plan Granjero before the loan program can be advanced. It is unlikely that this loan would be authorized prior to late 1976.

3. UNDP

The UNDP is providing financing (US$350,000) for an IBRD directed study of land use patterns and agricultural diversification in Uruguay (see above). It will attempt to formulate a long term public investment program for the agricultural and agri-industrial sector and an inventory of projects suitable for international agency financing. The study should be completed by March 1976.

The UNDP is currently financing four UNIDO experts to assist the Unidad Asesora upgrade its project evaluation capabilities. The UNDP is also providing assistance to the Laboratory of Testing and Analysis (LAE), a privately-financed, but MIE-operated quality control agency and materials testing facility. This agency is responsible for certifying quality control on agri-industrial exports.

The UNDP is also providing technical assistance to the Center for Productivity and Technology, an industrial development and technical assistance agency of the Ministry of Industry and Energy. The assistance is oriented to export market development of shoe and leather products industries. UNDP is also financing assistance to the Foreign Commerce Bureau of the Ministry of Foreign Relations in carrying out export market studies for leather garments, shoes, woolen knitwear, and selected food products.

4. Federal Republic of Germany (FRG) Assistance

In 1974, the FRG, through the Kreditanstalt Bank, made a DM 5 million loan to the GOU for capital goods imports for the industrial sector primarily for export orientation. The executing agency for this loan is OPP which carried out project reviews on sub-loan applications, and the BOR acts as the financial agency for carrying out the import transaction. All funds under this loan are ready for disbursement once certain legal procedures within the GOU are complied with. A replenishment of this loan to increase available funds up to DM12 million is now under negotiation with the FRG. Loan terms to the GOU are 2% interest, with 10 years grace period plus 20 years to maturity. It is understood that responsibility for undertaking project reviews of sub-loans under this credit will soon be transferred to the Unidad Asesora.

5. Argentine Capital Goods Loan

In 1974, the Argentine Central Bank made available a US$50 million line of credit to the Uruguayan Central Bank to finance capital goods imports from Argentina. Terms to the Central Bank are 10 years, 21 months grace period, and $7\frac{1}{2}$ percent interest. Terms to the sub-borrower are the same but the commission of the intervening commercial bank (about $1\frac{1}{2}$ percent) will be added. The sub-borrower makes principal and interest payments to the Commercial Bank in the peso equivalent of the dollar denominated debt converted at the commercial exchange rate. The loan has recently begun to function. Import applications will be reviewed by the Central Bank without a detailed project review, since the majority of imports will be for equipment acquisition and replacement rather than for development projects. (See page 57 for a discussion of the effect of this line of credit on this Program.)

6. Brazilian Capital Goods Loan

The Brazilian Government, through the Banco do Brasil, has agreed to make a US$50 million line of credit available to the Central Bank of Uruguay to finance capital goods imports from Brazil. The agreement will be signed on June 12, 1975. Terms to the Central Bank are 10 years, 21 months grace period, at $7\frac{1}{2}$ percent interest payable in dollars. Terms to the sub-borrower will be the same except for the commission of the commercial bank. The procedures will be essentially the same as for the Argentine credit. Imports will be channelled through the commercial banks in accordance with a procedure and criteria to be included in a Central Bank Circular. (See page 57 for a discussion of the effect of this line of credit on this Program.)

D. Place in Country Program and Relationship to On-Going Projects

The political and economic situation in Uruguay has undergone substantial change since 1973. (See FY 1975 DAP and CASP, and FY 1976 FBS.) The Bordaberry administration has taken a series of actions that have indicated to other international agencies as well as AID, that Uruguay has indeed begun a serious stabilization-development-reform effort that merits support. Conditions now are most propitious for helping to achieve the goal of the National Agricultural Development Plan emphasizing rapidly increased production ar export of non-traditional, as well as traditional crops.

This project, which aims to expand and increase the industrialization and processing of non-traditional agricultural production and thereby provide additional production marketing and export alternatives for Uruguayan farmers, will contribute substantially to achievement of the GOU's goals which are fully supported by the Mission and consistent with AID priorities. Within the total country program, the project is assigned a crucial role in attaining AID objectives in Uruguay.

As described earlier, the proposed loan will provide the final element of the USAID's agricultural development strategy by assisting agri-industrial-food processing-development which will spur new production and marketing opportunities to the target group. As such, the proposed project uniquely complements previously authorized FY 1975 loans and on-going grand-funded technical assistance activities.

A key support element for the proposed agri-industrial project are the activities, research findings, and studies of an AID grant-financed Agricultural Production and Marketing project. Under this project, a consortium of U.S. universities (Penn State, Michigan State, and Texas A&M) provides both long and short term technical assistance in agricultural research specifically in the area of fruits and vegetables, the production of which will be a major component of the proposed project. Through this project, the Las Brujas Research Station of the Ministry of Agriculture (MAP) has been improved to the extent that it now represents a very respectable production support asset for fruit and vegetable growing projects. This technical assistance is due to end in March 1976.

The proposed project also will derive support from, and is complementary to, the Agricultural Research/Technical Assistance Loan recently authorized. That project will create within the Ministry of Agriculture a research and technical assistance network, coordinated with other public and private technical assistance organizations, capable of delivering modern agricultural technology to the Uruguayan farmer.

The USAID has suppc ted a major participant training program financing both long and short-term training in all major fields of agriculture. Training efforts have concentrated on agricultural economics, research, and fruit and vegetable production, with limited training in livestock production.

E. Impact on the U.S. Economy

The overall effect of this project on the U.S. economy will be very positive.

The bulk of the loan funds proposed for this project, US$ 4.5 million, while open for procurement from Code 941 countries, are expected to be utilized largely for U.S. procurement, either capital goods, spare parts, essential raw or intermediate materials, or technical assistance. In this regard, the proposed loan will have a favorable impact on the U.S. economy. As described in other sections of this paper, Uruguay will have credit lines available for capital goods imports from other countries, specifically Argentina and Brazil. However, it is the intent of the GOU authorities who approve the use of such credits to direct foreign procurement by Uruguayan firms to those countries offering the lines of credit. In addition, the specific design and features of this project offer advantages over these other credit lines. As a consequence, it is anticipated that a substantial amount, if not most, of the procurement under the proposed credits will be placed with U.S. businesses.

Further, the expected commercial and trade relationships which will be developed under the proposed project between Uruguayan agri-industries and U.S. supplier firms which are either sources of capital goods and services or market outlets for distribution should grow over time as sub-projects assisted and developed with the proposed resources expand their operations. To a significant degree, as Uruguayan agri-industries expand into more complex and larger scale operations, the sole or predominant source of technology in food processing will be the U.S., given the leading position of U.S. technology in this area. Both in the provision of technical assistance and in the development of export marketing outlets, the services of such groups as the Agri-Business Council and OPIC will be enlisted.

Uruguay's exports of processed non-traditional agricultural commodities generated by this project will have no impact on the U.S. economy. Major export markets for Uruguayan agri-industries are and will continue to be Argentina and Brazil (especially given the current trade agreements between Uruguay and these countries), and European countries. Only a small portion of production will likely enter U.S. markets, and that probably only after Uruguayan agri-industries grow substantially in scale, to meet the production needs of U.S. markets, and improve overall quality of production to U.S. standards. Overall, the expected volume of production, concentrated in fruits and vegetables, will be so small relative to the U.S. or world markets that Uruguay could make 20 to 50 percent annual increases in its exports of these items, and still have no discernible effect on these markets.

F. Consistency with CIAP Reviews

The October 1973 meeting of the Sub-Committee on Uruguay made the following recommendations:[x]

"15. Traditionally the private sector has had a predominant role in the Uruguayan economy. It not only has the largest participation in almost all aspects of national life, but it also has a key responsibility in the agricultural, agri-industrial and export sectors. The Uruguayan delegation outlined to the Sub-Committee its Government's general economic policy, which favors the liberalization of the private sector from state controls, stimulating private initiative, and orienting government action toward the formulation of national development plans and programs, promoting and expediting private and public efforts in order to achieve these plans and programs, take the primary responsibility for certain critical or strategic activities, and protect these activities in accordance with the planned National Development Strategy.

"16. According to this Plan, the principal activities to be developed will be an export-oriented manufacturing industry, the agricultural sector, construction and exports in general. The proposed Law for Industrial Promotion and the structural changes in the BCR creating the Development Division, allow the intensification of the credit and tax incentives to promote industrial activities. The continuation and expansion of the agricultural development program will stimulate agricultural activities. The expansion of housing plans will reactivate the construction sector. Simultaneously, the foreign exchange policy plus a concerted effort to reestablish equilibrium in relative prices will complete the institutional framework which will encourage productivity in the private sector in order to achieve the established goals.

"17. The Sub-Committee agreed with the Delegation from Uruguay in assigning fundamental importance to those efforts that they could make to increase productivity, especially in the agricultural sector. This augmentation of productivity is an essential condition in achieving an internal savings rate that would guarantee a process of more accelerated growth in the future. In this context, they emphasized the high priority of investments made in research, technology, and agricultural extension.

18. The Sub-Committee emphasized the importance that export promotion and diversification policy has on the future growth of the Uruguayan economy. The Uruguayan Delegation explained that its Government is conscious of the need to promote export activities, especially by stimulating producers of exportable goods with a high net value added. Through the mini-devaluations mechanism, it is hoped that a favorable competitive level for exports will be assured. There is also a commission studying a system of incentives for non-traditional exports and progress is being achieved in the process of simplifying export procedures. The Government intends to review the tax system for meat exports."

It is the Mission's opinion that the objectives of the proposed Loan are fully consistent with the recommendations of the last CIAP review of Uruguay.

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x Informe Final del Sub-Comité del CIAP sobre Uruguay, Wash. D.C. 23-26 October, 1973.

PART V - PROJECT ANALYSIS

A. Institutional Analysis

1. GOU Organizations

The following are brief descriptions of the responsibilities and functional areas of operation of the various GOU Ministries, agencies and institutions which will be involved in the implementation of the project.

a. Ministry of Industry and Energy

The Ministry of Industry and Energy (MIE) has responsibility for national industrial policy, energy sources, and tourism, and for development activities in these areas. Its responsibilities include the areas of geological surveys, registry of oil wells and mines, industrial research and experimentation, industrial information and evaluations, and the mails. In addition, it seeks to stimulate employment and the application of new techniques in the industrial sector, and maintains relations on behalf of the Government with international organizations in its areas of responsibility.

Within the MIE, the Laboratorio de Análisis y Ensayos (LAE) is responsible for quality control of export products. The LAE is funded entirely by the private sector, and at present works principally in leather, agricultural and fishery products, although it plans to expand its functions to include poultry feed and fodder. Also under MIE is the National Industrial Productivity Center which provides assistance to private sector firms in specific technical industrial questions. More information on the Center is provided below. Another MIE agency, the Unidad Asesora, will be the main implementing agency for the loan project and is also described below.

b. Ministry of Agriculture and Fisheries

The Ministry of Agriculture and Fisheries (MAP) is responsible for elaborating and implementing national policy in the agriculture, livestock and fisheries area. Its responsibilities include the conservation and improvement of soils, irrigation and drainage; land tenancy and exploitation; administration of national parks; sanitary controls affecting crops; livestock and fish; and markets and prices paid for agricultural products. In addition, it has responsibility for agricultural and livestock research; registration of agricultural cooperatives; regulation of meat-packing houses; and cooperating in the social and cultural development of rural workers. The Ministry also maintains relations on behalf of the Government with international organizations in its areas of responsibility.

Sub-project proposals of a particularly agricultural nature, such as those for financing a farm machinery service project, will be referred to the appropriate MAP office as part of the sub-project appraisal process under the project.

c. Ministry of Economy and Finance

The Ministry of Economy and Finance has overall responsibility for the elaboration, coordination and implementation of economic, financial and commercial planning and policy in Uruguay. It manages the monetary system, exchange rates, foreign exchange holdings, foreign investments, and the public debt. It has responsibility for regulating commercial enterprises, expropriations, internal and external trade including customs operations, and weights and measures. In addition, it has responsibility for expansion of exports and encouragement of import substitution, as well as price controls for all products at any stage of their production, and stimulation of employment and the application of new commercial techniques.

The General Directorate of Foreign Trade (DGCE) is the agency within the Ministry of Economy and Finance which is responsible for implementing GOU foreign trade policy. It is charged with advising and making information available on all aspects of foreign trade and with coordinating foreign trade matters. The Directorate advises domestic producers and exporters about foreign markets for their products and on trading procedures.

d. Central Bank

The Central Bank issues national currency, regulates the domestic financial system, and formulates the annual monetary program of the Government. In addition, it administers the country's international reserves, controls foreign exchange rates, and controls the transfer of capital into and out of the country. The Central Bank can make international financial agreements and is the bank of deposit for all funds from foreign or international organizations and institutions.

The Central Bank will act as the GOU financial agent for the project.

e. Unidad Asesora

The Unidad Asesora de Promoción Industrial (Unidad Asesora) was established as an agency within the Ministry of Industry and Energy by the Industrial Promotion Law of September 1974 to evaluate industrial project proposals for the purpose of determining their qualifications under the Law for special credit assistance and tax exemptions. To qualify for these benefits, a project must be declared by the Unidad Asesora to be "in the national interest". The Unidad's declaration includes recommendations on the extent of the benefits and credit for which the applying enterprise should qualify, and must be approved by the Minister of Industry. In its project assessment, the Unidad Asesora can request and utilize the services of the various departments and technical agencies within the MIE and can consult with the Ministry of Economy and Finance, the Office of Planning and Budget (OPP) and other Ministries involved in the subject matter of a particular proposal to assist in their evaluation. OPP concurrence must be received if the declaration of national interest applies to more than one specific industrial project.

The Unidad Asesora is composed of two units. The main assessment unit, Unidad Asesora de Promoción Industrial, is responsible for recommending declarations of national interest and is comprised of three experienced professional engineers. The second unit, a staff support body, is the Unidad de Assistencia Technica para el Desarrollo Industrial, comprised of three business administration professionals and two economists. In addition, the Unidad has delegates from OPP, the Ministry of Economy and Finance, the Central Bank, the BOR, and the Banco Hipotecario del Uruguay, with whom it consults concerning proposals of interest to these organizations. Also, the MIE is receiving technical assistance for the Unidad Asesora from four UNIDO foreign technicians funded by the UNDP to help in establishing industrial project identification, evaluation, and follow-up methodologies and criteria for establishing mechanisms for generating and promoting industrial projects with special emphasis on assisting entrepreneurs with project ideas in any stage of elaboration to complete analyses and studies required to qualify for assistance or declarations of national interest.

f. Office of Planning and Budget

The Office of Planning and Budget (OPP) is an agency directly responsible to the Presidency, which assists in the formulation of national development plans, policies and programs and advises on public sector budgetary matters. It assists in the formulation of economic development plans, projects and seeks sources of financing for these plans, coordinates all efforts to increase national production, and coordinates arrangements for external technical and financial assistance with international organizations and foreign governments. OPP assists in making projections for the national budget and advises on the formulation of the annual budgets of State-owned industrial and commercial entities. OPP approval is required for all loans to the GOU by foreign governments, international agencies, or foreign banks.

The Office is headed by a Director appointed by the President of Uruguay, and is divided into three divisions: Planning, Budget, and Auxiliary Services (administration). The Planning Division is charged with analysis, programming, evaluation and coordination of public sector investment projects, and coordinates and directs all foreign technical assistance. In the industry sector, OPP evaluates sector plans and programs, and provides technical assistance in the organization and implementation of industrial plans. In agriculture, the Office distributes basic statistics on production and prices, and assists the MAP in the evaluation of agricultural development projects. In addition, the OPP conducts a wide range of studies in the area of foreign commerce, including market studies, integration studies, and studies on foreign trade duties and taxes. It also oversees import and export prices, as well as customs duties.

The Industrial Section of OPP's Planning Division received sub-project requests and conducts analysis of these proposals in preparation for financing under the Federal German Republic's small and medium industry loan (see Part IV., C.4).

In actual operations, in order to determine whether a project submitted to it for evaluation meets all criteria for project approval, the Unidad can and does rely on established sources of technical expertise principally within three other GOU agencies as appropriate: the National Industrial Productivity Center, the IAE and the DGCE.

The Unidad Asesora in actual practice frequently enlists the assistance of the Productivity Center for project evaluation when appropriate in accordance with the nature of the project. The Center has had ample experience in all phases of project evaluation at actual business or enterprise levels. In the past, it had been composed of both private and public support, but is now largely government funded, and had gained substantial practical experience working for and with actual operational businesses. The Center's intensive involvement with private sector firms has enabled it to develop a pragmatic approach to project diagnosis and recommendations which are generally tempered with private sector points of view (i.e., pragmatic options) well considered in final recommendations.

Under the "PL-480" pre-export financing fund operated by the Central Bank through the commercial banks, a pre- requisite condition for any firm desiring financing under that mechanism is to have had his proposal evaluated and certified by the Center prior to its being submitted to a bank for initial processing. This pre-export financing mechanism has functioned well and enjoys a substantial respect from members of both the government and private sector (banking as well as business) communities. In large measure, much credit for that success relates to the efficient and effective project analysis and evaluations performed by the Center in that program. The Center has capacity to respond to additional requests from the Unidad Asesora for technical or other reviews of feasibility study or market study nature, and is expected to function as well under this program as in the PL-480 program in those capacities. The Center is the beneficiary of a UNDP assistance program under which it can request the services of technical experts to assist it in performing studies in areas in which it is not fully qualified. The Center has made effective use of this service in the past and will do so in the future for any projects submitted to it by the Unidad Asesora requiring such special review capabilities.

The IAE functions as the country's center for quality control of export products. Given the proposed project's heavy emphasis on export production, the Unidad Asesora is expected to make much use of the general and specific services available from this entity. Among the functions of the IAE is the categorization of Uruguayan food production under worldwide international standards. The LAE is particularly active at present in instituting use of these standards for the export food products area. The LAE categorizes and registers national products and certifies shipments to be of specified quality, an essential requirement for production for export markets. In addition, the ATL also performs on site factory checks for grade and standards control. Although the current standards being applied are less than the highest (due only to the nature of the imperfect or low quality raw materials many firms must use) the LAE has a reputation for strict application of those standards in force. The LAE has good equipment, and more than five years experience in the standards area.

Specific ways in which the LAE is expected to provide essential support services to the Unidad Asesora include, for example, an analysis of the quality of raw materials or actual production to be directed to export or internal markets to insure that the assumptions of a sub-project regarding potential market penetration are production projections and reasonable. With the strong emphasis on export production in this Program, much use is expected to be made of the LAE's services by the Unidad Asesora during sub-project evaluation.

As with the Center for Productivity, the LAE has a strong private sector orientation, with several members of its board of Directors being representatives from the business community. The mixture of private and public officials guiding its efforts has worked harmoniously.

Both the Center and the LAE are working at less than full capacity, and requests the Unidad Asesora may direct to them for assistance will be easily handled. All of the entities mentioned are under the direction of the MIE. Because of this, they can be expected to cooperate and coordinate their activities closely to support mutual programs and interests.

A third source of technical assistance to the Unidad Asesora for project evaluation will be the DGCE, an office which handles export promotion and development activities for the GOU. This office is currently providing services to the private sector among which are so called "sector studies" of regional markets which provide business with valuable non-product specific, market information. Also, under the DGCE program, private entrepreneurs' can request that specific market studies be performed by the DGCE. If capable, the DGCE performs the study itself. Otherwise the DGCE can request the UNDP technical assistance in carrying out highly technical or specific work. It is expected that this latter service capability will be of significant assistance to proposed agri-industrial projects which will plan to enter export markets.

Given the capabilities of these specialized GOU agencies, and the fact that they each have capacity to provide additional services to the Unidad Asesora, the Project Committee's review concluded that specific strengthening of the Unidad's staff in the special technical skills represented in the agencies described is not required to for project implementation.

Further, the UNDP assistance program which will run through February of 1977 will provide a continuous and reliable guidance and support to the Unidad Asesora in developing and improving all phases of its operations.

Nonetheless, as the Project Committee's success in rapidly identifying potentially eligible sub-projects attests, there exists a substantial demand for financing of the nature proposed within the agri-industry sub-sector. When program implementation begins, there will be numerous and frequent sub-project submissions received and to be processed by the Unidad Asesora. In order to handle that increased demand and workload, augmentation of the Unidad Asesora's basic appraisal staff will be necessary.

The Unidad's present staff is comprised of professionals qualified within three main areas:engineering, business administration and economics. It is likely that, with the increased demands for financing to be processed as a result of the AID and IBRD loans, the Unidad's staff will have to increase by from 60 to 100 percent with the expansion composed primarily of the engineering and economic skills to increase project review and appraisal capacity. As noted in earlier Sections of this paper, the IBRD which also intends to work with the Unidad Asesora, will make available up to US$ 500,000 under its Industry Sector Loan for technical assistance to the GOU to increase the capacity of the Unidad Asesora to handle increased workload. More specific estimates regarding numbers of personnel to be added may be determined in the analysis to be undertaken by the GOU and the IBRD appraisal team of the Unidad Asesora beginning June 15. The results of that review, subject to further refinement, will serve as the basis for the GOU submission to AID, as a condition precedent to disbursement of AID Loan funds, of a plan for increasing the capacity of the Unidad Asesora to manage the project.

Additionally, as described in Part V, Section B, below, the Project Committee recommends that the plan to be submitted by the Unidad Asesora incorporate provision for the full time technical services of an agri-industry advisor experienced in food processing activities to support program implementation efforts specifically in regard to management, technical, and marketing advisory assistance. Recommended specific duties and personnel specifications are also detailed in Part V, Section B, below.

In order to assist the GOU to acquire the services of such an expert during the project period, the Project Committee recommends that up to US$ 150,000 of Loan funds be eligible for use by the GOU for that purpose.

B. Agri-Industrial Sub-Sector Assessment and Demand Analysis

1. Summary and Conclusions

1. There is a large unrealized potential for agricultural production in Uruguay. Less than 1% of the agricultural land is used for fruit and vegetable growing and there are obvious opportunities for expansion.

2. There are many small farms (56,000) under 100 hectares on which live 212,000 people. The smaller farms in this group - 50 hectares and less - grow most of the fruit and vegetables.The larger farms in this group - 50 to 100 hectares - account for most of the milk production and field crops.

3. Although Uruguay is virtually self-sufficient with respect to food production and is presently exporting significant quantities of non-traditional foodstuffs, there is considerable scope for improvement in production efficiency at the farm level.

4. The potential for a significant contribution to the world food needs, particularly to neighboring countries, by the production of agricultural surpluses, is very evident. *

5. To realize this potential it is necessary to increase agricultural output by:

(1) improved productivity per unit and lower unit cost;
(2) expanded areas of production;
(3) improved quality standards and uniformity of production.

The constraints identified are: small farms, poor farmers lacking in capital, poorly mechanized farms, motivation for increasing production is lacking as is an organized marketing capacity.

6. Steps are being taken by fruit and vegetable processors to encourage increased production under contracts supplying technical field services, seeds, fertilizers, etc. (Rio Claro); and by the dairy industries improving milk handling and instituting a bonus system for dairy farmers (CONAPROLE).

7. Fruit exports have increased dramatically from US$ 749,000 in 1970 to US$3,440,000 in 1974, and there is much opportunity to quickly increase output by better orchard management and improved agricultural techniques.

8. Packaging materials are in adequate supply to support the existing processing industries but are expensive and there are some qualify deficiencies.

9. Some reinforcement in managerial and technical functions probably will be required to support an expanding food processing industry. No labor problems are anticipated.

* An illustration of potential for marketing increased exports is contained in the fruit marketing analysis performed for the FY 1975 Agricultural Cooperative Development Loan to Uruguay, which indicates significant capability to expand efforts to Brazil.

10. Most fruit and vegetable processing plants are poorly equipped and in need of rehabilitation, some of which is already underway: CONAPROLE dairy plants are excellent in all respects; many other food processors of various types are well equipped.

11. Fruit and vegetable processors are in need of investment programs to improve capacity, efficiency and quality, and to be in better position to increase exports and absorb greater quantities of agricultural raw material. There is much scope for increasing fresh fruit and vegetable and dairy products exports, particularly to Brazil and other neighboring countries.

12. Products developed for export should fit within the framework of the recommended criteria.

13. This proposed loan program will provide funds for needed investments in existing and new facilities, providing Uruguay with a more efficient and more productive food processing industry which could quickly generate additional exports and better supply the domestic market.

14. The loan program should be supported by technical assistance in the areas of vegetable and fruit growing, dairy farming, food processing, and marketing.

The Mission in consultation with the GOU and the private sector has identified 37 illustrative agri-industrial project proposals which are annexed. These proposals have been developed by both cooperatives and private firms and are in various stages of development, from planning proposals to projects that have been submitted to the Unidad Asesora for approval. (See Annex G, Exhibit 1).

Cost information is estimated and based upon the most recent data available at this time. Final costs cannot be determined until proforma invoices are provided based upon exact specifications and delivery schedules. However, present estimates of the total dollar value of capital goods imports, including technical services, for the proposals identified is US$ 13,525,000. The total estimated local currency required by these projects, expressed in dollars, is US$13,091,000. Total investments for these illustrative projects, expressed in dollars, is US$ 26,616,000.

Of the 37 identified proposals, 34 are located in the interior of Uruguay, and 3 are located in Montevideo. The breakdown by commodity or activity is:

Vegetable Processing	8
Fruit Processing	9
Dairy Processing	13
Box Manufacture	2
Can Fabrication	1
Livestock Feed	2
Other Foods	2
	37

This preliminary study definitely demonstrates that there is a need for additional or improved agri-industrial activities that involve food processing and are export-oriented. It is evident that each proposal identified will require additional in-depth study and updated information before the feasibility and both the dollar and local cost financing can be fixed with any degree of accuracy. It is certain that additional projects, better designed, will be forthcoming once a system for submitting these projects for approval and financing has been implemented. Also, local capability for developing proposals, including feasibility studies and financial analysis, has been identified which will greatly improve the planning and implementation of new agri-business proposals.

It is clear that further marketing studies will have to be developed both for internal sales and export opportunities. This must include the continued development of grades and standards to meet specific market outlets, plus packaging and product presentation that will respond to market needs.

It should be pointed out that the non-availability of medium and long-term credit and the scarcity of foreign exchange available for the importation of capital goods has inhibited project development by interested investors. Only recently, with the liberalization of foreign exchange for imports and the proposed bilateral credit agreements with Brazil and Argentina, have developed investment projects received attention.

The illustrative projects outlined above are all within the criteria guidelines developed for export product strategy (see page 77). These proposals:

1. Are based on agricultural raw materials that have been traditionally produced in reasonable volume;

2. utilize minimum packaging costs and complexity;

3. utilize uncomplicated technology;

4 maximize the utilization of existing facilities:

5. are complimentary to existing facilities;

6. are designed for uncomplicated marketing;

7. operate within the limitations of their specific geographic areas; and

8. are complimentary to the domestic market.

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7. Raw Material Supply

The total farm area of Uruguay comprises 16.5 million hectares. This land is divided into 77,000 farm units; 56,000 of these units (73% of the total number) are less than 100 hectares in size, and represent only 7.4% of the total farm area. The remaining 92.6% of total farm area representing 27% of total farm units, is devoted almost entirely to grazing and the growing of field crops.

The following table demonstrates the land use of a typical small farm.

TYPICAL SMALL FARM (LESS THAN 100 HECTS.) LAND USE

Grazing*	60%	(mostly over 50 ha. in size)
Field Crops	20%	(grains, oil seeds, sugar beets, etc.)
Vegetables	10%	(mostly under 50 ha. in size)
Fruits	4%	
Vineyards	3%	
Miscellaneous	3%	

* Includes about 4,600 dairy farms.

Slightly less than 1% of the total agricultural land is devoted to fruit and vegetable production.

At the time of the 1970 agricultural census, the total population of Uruguay was 2.9 million people. Only 318,000 people, 11% of the total population, lived on farms, and 212,000 people or 67% of the total farm population, lived on farms of less than 100 hectares in size. This small population and a highly fragmented farm structure manages to feed the total population, supply raw materials to food processors and for export.

Uruguay, with the highest percentage of productive land of any country in Latin America, has a large unrealized potential in agricultural production. Nevertheless, Uruguay is virtually self-sufficient with respect to food and fibre production, with the exception of a few tropical grown crops which cannot be produced here such as coffee, bananas, etc. The potential for a significant contribution to the world food needs, particularly to neighboring countries, by the production of exportable surpluses is very evident.

In the area of fruit and vegetable and milk production, there is scope for considerable improvement in production efficiency. IATA research has demonstrated that milk production per hectare can be increased as much as three times with better pasture and herd management. An ADELATEC study in 1971 emphasized that Uruguay possesses one of the best zones for citrus production in South America, but it has not developed its production with either the volume or the efficiency that is required to export more effectively. The export of vegetables could be increased considerably, but an organized marketing capacity is lacking.

Because of climate, quality of soil, and proximity to the major market of Montevideo, most of the fruit and vegetables are grown in the southern section of the country, with the exception of citrus, which is primarily grown in the north-west corner. Most of the fruits and vegetables are grown on farms of less than 50 hectares in size, and a considerable number of these are less than 10 hectares. These small farms are lacking in mechanization. The economic equation of hand-labor vs. machines leads to resistance on the part of growers towards mechanization because of low labor-cost and the high cost of farm machines and fuel.

Despite the constraints as evidenced from the above, the total population is being adequately supplied with a balanced and nutritious diet of fruits, vegetables and other foodstuffs, exports are being accomplished in increasing volume and progress is being made.

There is undoubtedly much scope for more production of all kinds of agricultural products, and there appears to be an excellent opportunity to rapidly generate increased exports from the low present base. The three things needed to expand agricultural output are:

1. improved productivity per unit and lower unit costs;
2. expanded areas of production;
3. improved quality standards and uniformity of production.

The low yields and correspondingly high costs put Uruguay in an unfavorable position relative to its principal competitor, Argentina, and present a serious handicap to the fruit processing industry.

At least one processor, the Rio Claro factory, is already taking positive steps in this regard. This small factory has increased its production of tomatoes dramatically in the past two years, from 479 tons in 1972, to 2,523 tons in 1974. They now deal with about 500 very small farmers, and are assisting the farmers by providing field supervision and technical assistance, providing seed and sometimes fertilizers. Last year their yields were reasonable at 15 tons per hectare, which compares favorably with the nationwide average of 7,000 kilos per hectare. They have been selective with their growers and have weeded out those who proved to be unreliable, and they have a good reputation with growers, particularly because they pay on time. They expect to improve yields rapidly over the next few years, to at least the 30 ton per hectare level, with a corresponding improvement in quality. They deal with the growers on a contract basis, guaranteeing to take the farmers' full output and thus providing the needed incentive.

Apparently the practice of dealing on a contractual basis has not always worked as well as it does for Rio Claro. Other companies have experienced difficulties with farmers not adhering to their part of the contract, and the farmers in turn accusing some processors of being unfair in the execution of their part of the contract. It does appear that there is need for improved integrity on both sides. Better processor-grower relations and adherence to guarantees particularly with respect to payment would encourage growers to do a better job.

With respect to fruit, according to data provided by the Oficina de Programación y Política Agropecuaria, the export of fresh fruits including citrus has increased dramatically in the past five year period. In 1970, total exports amounted to US$749000 increasing to US$3,440,000 in 1974, an increase of 460%.

Much improvement can be accomplished merely by better orchard management and the application of improved horticultural techniques. As an example of what might be accomplished, an Israeli technical mission recently developed a comprehensive proposal involving a combination of technical assistance, capital investments and market surveys. From schedules given in their report, they anticipate increasing the yield of peaches, apples, pears, from the present level of about 7 tons per hectare by 70% in five years and more than double in ten years. By a combination of rehabilitating existing orchards and establishing new orchards, they anticipate a substantial increase in fresh fruit exports, paralleling the increase in production.

Although these figures are only forecasts of what this Mission believed could be accomplished, the figures are indicative of the scope of opportunities that exist.

Another need of the fruit producers, and this is true of the citrus industry as well, is the need for processing outlets for second grade produce that is still of reasonable quality but below export grade. These fruits could be processed into such by-products as fruit pulps, concentrated fruit pulp, fruit juices, marmelades, oil extraction, etc.

Cheese and other dairy products seem to be natural exports for this cattle raising country. But the raw milk supply and quality problem must be solved at the farm level. The level of supply limits the production of all dairy products, particularly exportable cheese and casein. The quality of the milk is inferior bacteriologically. Incoming raw milk to the processing plants has a bacteria count ranging from 13 to 16 million bacteria per cubic cm. Even with this high level of contamination, CONAPROLE, the largest milk processor in Uruguay, claim to control their pasteurized milk at about 50,000 bacteria count.

However, the exceedingly high bacteria content of raw milk limits the production of the types of cheeses that can be manufactured by CONAPROLE to one type, Sbrinz . With better quality milk, cheese production could be diversified into other types. Almost all of the Sbrinz production is exported to Buenos Aires and Brazil. However, the quantity of cheese output is restricted by the milk volume problem. At present time the cheese plant operates only 7 months of the year. Without the milk volume limitation, production could take place five more months annually, resulting in at least a 70% increase of output and corresponding exports.

Despite the supply problem, CONAPROLE is making an investment of US$1.2 million for a new powdered milk plant with a capacity of 200,000 liters of raw milk per day, which is planned to be in operation 2 years from now. The executives of CONAPROLE advised they were taking steps to correct their supply and quality problems, such as:

1. Constructing central receiving stations to collect and cool raw milk more quickly.

2. Institute a bonus system for growers based on quality.

3. Improve milk handling throughout the system.

It might also be desirable for CONAPROLE to invest in a technical assistance team of practical operating dairy technicians working at the farm level. Much could be accomplished in a relatively short period of time if the proper approach can be ascertained and some of the elementary aspects of the problem could be corrected.

Packaging Materials

The most important packaging material for the food processing industry is sanitary tin cans. There are three can making plants in the country, which is ample capacity in relation to the present size of the processing industry. One of these is a plant recently acquired by the Cariboni group. This plant had gone bankrupt and has not operated for the past five years. The equipment is presently being overhauled and the efficiency of this plant will be largely determined by the thoroughness of the renovation and the company's ability to recruit a team of good can making operators and mechanics.

The second company, Lostorto, operates a plant with very old, low speed equipment, but they are presently formulating a program of modernization involving an estimated investment in the order of $200,000. Each of the plants has a completely equipped lithographing installation and they do all of their own tin plate lithography and lacquering.

It is important to note that none of the plants is equipped with automatic can testers. This is a serious, although not a vital deficiency. The purpose of the automatic can tester is to eliminate the defective cans which then are never delivered to the processor. These are cans with fabrication defects or a pinhole in the tin plate. Since cans that should have been rejected will be delivered to the processor who has no means of eliminating them, they will be filled with product with resulting spoilage. Not only this is costly, but it is damaging to the reputation of the processor, brand, and the industry overall. It can be particularly embarrasing if a high number of spoiled cans are found in an export shipment. Can testers are quite expensive pieces of machinery and undoubtedly this is the reason why they are not used. They can only be justified on the basis of quality.

Since these plants use Canadian or U.S. tin plate the likelihood of more than a very rare pinhole is negligible and fabricating defects are by far the most likely cause of spoilage.

Cans are expensive and the unit cost is stated to be about double the U.S. cost. However this is very typical of can costs throughout Latin America.

Glass bottles and jars are available but the supply is limited with regard to size and shape. The selection of closures is also limited to rather old fashioned types. Because neither the jar nor the closure is manufactured to very close tolerances, this sometimes results in an inadequate seal.

Labels are available in reasonable quality, but these too are reported to be very expensive.

Corrugated cartons are not widely used and it was reported that these are prohibitively expensive and poor in quality. Most of the product for the domestic market is packed in wooden trays or open top wooden cases which are returnable. Many export packs are shipped in wooden crates.

Packaging costs, availability, and quality will have an important bearing on product strategy for export. For example, fresh fruit exports require a minimum of packaging, canned fruit in syrup requires the most expensive packaging, and fruit pulp in bulk packs would be intermediate in packaging cost.

4. Personnel

The caliber of managerial and technical staff of course varies considerably with the size and complexity of the respective industries. Sufficient skills probably exist to cope with the present levels of activities. Under intensified activity levels, the following areas would probably prove to be deficient and in need of reinforcement:

Planning
Product Research and Development
Agricultural Research and Development
Quality Control
Cost Control
Marketing

The factories are accustomed to operating with an excessive amount of hand labor. There should be a gradual transition to more mechanization and to accomplish this smoothly will require attention to personnel relations, personnel training, etc. The various skills required for more sophisticated processing and operating methods will need to be developed concurrent with the more advanced installations.

The level of education in Uruguay is generally higher than most other Latin American countries, indicating that no greater personnel problems should be encountered as the agri-business enterprises develop in size and complexity than would be encountered in any other part of Latin America.

5. Food Processing Facilities

The Exhibit below details the existing food processing businesses in Uruguay of all kinds except meat packers and processors.

It will be noted that there are 69 establishments devoted to fruit and vegetable processing, fruit and vegetable packing, and dairy products.

These range in size and complexity from very small, primitive type operations, such as the Rio Claro tomato products plant, to modern, sophisticated installations such as the CONAPROLE milk processing plant in Montevideo, and the cheese factory located near Villa Rodriguez. (The notes covering an inspection of seven of these plants are included in Annex G, Exhibit 2).

FOOD PROCESSING BUSINESSES IN URUGUAY

Sources: Indice Industrial del Uruguay
Oficina de Programación y Política Agropecuaria
Centro National de Tecnología y Productividad Industrial

Fruit and Vegetable Processors	35
Fresh Fruit Packers and Graders	5
Flour Mills	51
Edible Oil Manufacturers	11
Sugar Refineries and Related Manufacturers	5
Rice Processors	4
Dairy Producers and Icecream Manufacturers	29
Spices, Mayonnaise, Sauces & Mustard Mfrs.	26
Biscuits and Cookies Manufacturers	15
Popcorn, Candy and Related Lines Mfrs.	44
Oat and Other Meals, Baking Powder, Instant Desserts, and Fecula Manufacturers	25
Noodles and Spaghetti Manufacturers	98
Poultry Processors	10
Honey producers	6
Barley Producers	3
Beer and Malt Manufacturers	3
Fruit Juice Manufacturers	4
Soft Drinks Manufacturers	7
Wineries	80
Vinegar Manufacturers	6
Bakeries	280
Fish, Seafood and Fishmeal Producers	9
Coffee, Cocoa and Peanuts Processors	38
	794

The fruit and vegetable canners and processors are operating with old, mostly obsolete equipment, with excessive use of hand labor. The two plants reputed to be the best in the country do not have even labelling machines of any kind, and are hand-labelling each individual can and jar. The Sauce factory, which accounts for 35% of all fruit and vegetable processing in the country, provided us with a percentage breakdown of cost of a typical product - the 800 gram size of canned peaches in syrup - as under:

Peaches	19%
Syrup	10%
Can, label and case	32%
Labor and Social Benefits	21%
Other Inputs and Overhead	18%
	100%

The labor content is quite high, at least double what would be expected in a reasonably efficient operation. The plants visited, and probably the rest as well, could certainly benefit from an investment program for the purpose of improving capacity, efficiency and quality and correcting services deficiencies. In many instances, the investment needs are relatively minor and immediate improvements could be expected. It is imperative for these improvements to be made if Uruguay is to have a food processing industry capable of absorbing greater quantities of agricultural raw materials. This in turn would provide the needed incentive for growers to produce in greater quantity, would supply the domestic and export markets more effectively, and make a greater contribution to the overall economy.

Nevertheless, these factories are turning out a surprising number of canned and processed food products. The Sauce plant is already exporting US$1,000,000 worth of products annually as compared with domestic sales of US$800,000. Although the management of Sauce identified two relatively minor items of equipment which they believe would be required to increase their efficiency and capacity, a comprehensive plan to upgrade the facilities does not exist. One should be prepared and implemented to avoid the pitfalls of a piecemeal investment approach. A systematic highly selective investment program could assist materially in the generation of greater exports.

The Rio Claro plant has already developed a comprehensive program and is in process of implementing it. They are remodeling part of their building, and have purchased two complete new lines; one including a double effect evaporator for the concentration of tomato paste, and the other a fruit processing line to make fruit concentrates and jams.

In all of the fruit and vegetable canning plants, processing and export marketing technical assistance is required.

Two plants manufacturing a fairly broad line of dry foodstuffs were visited. One, Standard Brands, is producing the usual line of Standard Brands products and the installation is typical of their plants in Latin America. Export opportunities appear limited for their products, but they are planning some export of their Royal line to Standard Brands in Brazil. The Molino Puritas plant is an interesting example of the old family style entrepreneur. They are already exporting some products and with a modest investment of US$25,000 they could increase their export of oatmeal considerably. This factory is in good condition, and is well equipped and maintained.

The CONAPROLE milk processing plant in Montevideo is quite large and with very modern equipment installations. One of their products, Dulce de Leche, is unique to Uruguay and Argentina. The product has not as yet been exported but it is the type of product that possibly could be promoted in a country such as Brazil. Certain technical difficulties will have to be overcome, but this is possible. The CONAPROLE cheese factory is probably the most modern in the country and virtually a showpiece with respect to the buildings and equipment. Almost all the cheese being produced there is exported but production in both plants is limited because of the supply and quality of milk.

Although most of the plant layouts (except CONAPROLE) could be considerably improved and much of the equipment should be replaced, such a program of complete overhaul andmodernization would probably not be economically feasible. Nevertheless, by careful analysis many investments could be identified which would yield satisfactory returns and promptly increase exports. The layouts could be improved in stages over a period of time when the general health of the industry has benefitted from improvements in cost and capacity.

The vegetable and fruit processing industry would benefit considerably by more examples of the type of entrepreneurship as demonstrated by Dr. Egon Sudy's proposed project to establish dehydration facilities. As described in the notes in Annex G, this project has been well researched in all aspects and should be a very successful one. Assuming it is successful it could serve as a good example to others as to how to approach an investment program.

6. Export Product Strategy

From an examination of the conditions and resources of the food processing industry in Uruguay, a list of criteria has emerged for the selection of export products. The products most likely to succeed in the export market should fit within the framework of the following recommended criteria:

1. Normal agricultural raw material should be utilized, which has been traditionally produced in reasonable volume. Avoid the more exotic items as strawberries, pineapples, mushrooms, etc.

2. Minimum packaging cost and packaging complexity.

3. Uncomplicated technology.

4. Maximize utilization of existing facilities.

5. Complement existing facilities

6. Uncomplicated marketing.

7. Examine the limitations which exist in almost every area, and operate within them.

8. Compliments the domestic market

From this criteria, an individual product strategy should be decided. For example, assuming a fresh fruit is available in quantity for exports, the fruit could be exported in at least four different forms as detailed below:

1. Fresh fruit export. Simple washing, grading, inspection and packaging operation; requires cool storage and well organized logistics from packing plant to consumers; uncomplicated marketing; immediate consumption of product.

2. Fruit pulps or fruit concentrates in bulk packs. More expensive equipment needed; expensive packaging; severe competition; direct sales to customer; industrial use.

3. Canned fruit in syrup - Consumer sizes. Expensive equipment or expensive hand operations; more expensive packaging; severe competition; complex distribution and branded product marketing; delayed consumption.

4. Frozen product. Highly specialized production, packaging, storage, and shipping facilities required; specialized distribution channels; high spoilage risk.

From the above, it would appear alternatives 1 and 2 provide the best opportunities for success and alternative 4 is no doubt out of the question, at least at the present time.

For products where a specific market exists, such as identified in the proposal for dehydrated onions, it would obviously not be necessary to go through such an exercise, but for most fruits and vegetables, more than one alternative export product will be possible.

Products with Most Likely Export Potential

1. Fresh fruit and vegetables.

2. Fruit pulps and concentrates in bulk.

3. Dairy products: cheese, casein, butter.

4. Dehydrated vegetables.

5. Miscellaneous dry foodstuffs based on cereals.

6. Selected canned fruits and vegetables.

7. Agri-Industry Advisor

It appears to be highly desirable to support this loan with management, technical and marketing advisory assistance.

The smaller businessmen and entrepreneurs will need managerial assistance to help them think through their project ideas, guide them through the preparation of feasibility analysis, and the preparation of the loan presentation papers, etc. Most of the food processing industry particularly fruit and vegetable processors are in need of technical help. The need for marketing guidance emerged from almost every discussion.

This leads to the concept of establishing the position of the Agri-Industry Advisor, probably on the staff of the Unidad Asesora.

The duties of the advisor would include:

- Work with loan prospects to assist them with preliminary evaluation of suggested investments.

- Guide the clients through the necessary steps required to complete their loan applications, including:

  - market appraisal and proposed marketing strategy
  - sales forecasts
  - cost and profit projections
  - determination of adequate raw material availability
  - facilities design
  - estimated capital needs and timing
  - technical and managerial capability requirements
  - other relevant elements.

- Guide the clients in the preparation of the feasibility studies and other material required by the loan application and review process.

- Assist the clients in the execution of the projects through start up by assuring they are coping with each stage successfully.

- Actively seek out new loan prospects.

- Help to develop and maintain good client relationships.

The personnel specification for this job would include:

- A food technologist or industrial engineer (an MBA would be helpful).
- Good broad experience background in the food processing industry.
- About 40 years of age and mature personality.
- Analytical and objective - ability to quickly get to the nucleus of problems.
- Ability to work with people at all levels of management, from farmers to general managers of corporations.

C. Financial Evaluation

1. Financial Plan

Under the proposed Program, an Agri-Industrial Development Fund will be established in the Central Bank with an initial capitalization level of US$7.25 million in dollars and peso equivalents. The Central Bank will serve as fiscal agent for the operations of the Fund, in coordination with the Unidad Asesora and Mixed Commission, the operational and approving agents for the Program. After sub-projects are processed, reviewed and approved, both dollar and local financing requirements approved for financing will be met from the resources of the Fund.

The AID contribution will be up to US$5.0 million.

The GOU contribution will be not less than US$2.25 million in peso equivalent, equal to 31 percent of the capitalization of the Fund.

In addition, sub-borrower contributions to total project costs are estimated at US$2.75 million is peso equivalent.

Funds from other sources in support of approved sub-projects (including loans to sub-borrowers from commercial banks, suppliers' credits) are estimated to amount to US$2.5 million.

Total project resources are displayed below.

Project Financial Plan

	US$	Pesos
Agri-Industrial Development Fund		
AID contribution	US$5	
GOU counterpart		US$2.25 in peso equivalents
Total Fund	US$ 7.25 million	
Sub-borrower investments (estimated)	US$ 2.75 million	
Other contribution,(commercial banks, etc.)	US$ 2.5 million	
Estimated Total Project Contributions	US$12.5 million	

Dollar resources of the Fund will finance the procurement of capital goods for fixed investment (machinery, equipment, spare parts) as well as services for feasibility studies and technical assistance requirements of sub-projects from Code 941 countries. Working capital requirements for essential raw or intermediate stage processed materials (tinplate, other packaging materials) unavailable locally but determined to be critical to operation of an approved sub-project will also be eligible for financing from Code 941 countries. Sub-loan terms for a package of capital goods procurement, plant installation and other technical assistance services will range from three to ten years maturity and may include a grace period; terms for eligible working capital requirements will not exceed two years, and will be based on recommendations set forth in the sub-project's feasibility study and other analysis and recommendation for approval by the Unidad Asesora. Terms for individual feasibility studies, market studies, etc., for which an entrepreneur requests financing prior to full project elaboration and sub-loan request will be up to three years with the specific period of financing to be recommended by the Unidad Asesora.

Local currency from the Fund will finance procurement of capital goods machinery and equipment of national origin as well as plant construction or acquisition costs as determined necessary by supporting feasibility studies. Locally available technical assistance may also be procured with peso resources, as appropriate. Working capital requirements for locally available raw materials may also be eligible for peso financing as supported by feasibility studies and reviewed by the Unidad Asesora.

2. Interest Rates and Conditions of Sub-loans

A specific interest rate (or rates) for sub-loans has not been determined as yet. Discussions between the Project Committee and the GOU established agreement on the concept of what the interest rate to the end-user should be comprised of, but more intensive analysis than could be performed prior to submission of this document is required to establish the final rate. The GOU has agreed to undertake this intensive analysis and will submit the results of that review to AID for approval in satisfaction of a recommended condition precedent to disbursement of loan funds. The GOU will be assisted in performing the required analysis by the efforts of the IBRD Industry Sector Loan appraisal team, due in Montevideo on June 23, which will be examining the same subject prior to recommending sub-loan interest rates for that credit (both the AID and IBRD loans will, as noted earlier, utilize the same institutional and financial mechanism for project implementation).

The recommended terms from AID to the GOU are two percent during a ten-year grace period and three percent thereafter. The Central Bank, which will serve as the fiscal agent for the Fund to be established, has indicated no charges need to be added to this basic cost for its services, which will be limited to basic financial management and banking functions. Neither will a percentage rate be added to the basic rate for the review and appraisal services of the Unidad Asesora. A charge for the commercial banks' participation in the Program within the range of 1.5-2.0 percent, in real terms, was considered by all private and public sources contacted to be desirable and adequate to motivate and offer incentives to commercial banks to actively participate in the Program, while offering a fair return from that participation. However, the more precise or exact determination of the most appropriate interest rate within the range requires a form of sensitivity analysis, probably best effected through a complete or valid sample survey of the banking community.

An additional factor in the consideration of the proper sub-loan interest rate relates to the degree to which all sub-loans under the Program will be readjustable. GOU economic policies are firm in their intent to remove inefficient subsidies to the private sector, particularly in regard to monetary policy. Therefore, the GOU agrees that all sub-loans under the Program, to include both the dollar and local currency elements, should be able to be readjustable up to 100 percent. The GOU suggests that the most reliable available index for such readjustment is the Montevideo cost-of-living index. A question in this regard concerns the potential influence such fully adjustable loans, as a condition of the Program, could have on the intermediate target group of entrepreneurs who are expected to respond with requests to the Program for project financing. Given Uruguay's second trauma inflation and substantial world inflation as well, current expectations among entrepreneurs may be that such conditions will persist for the near to medium term. Thus, consideration will be given to the desirability of conditioning the loans on less than full readjustability in order to pass on to the sub-borrower the major burdens of the devaluation risks while providing him with a ceiling limitation to that exposure. The major consideration involved relates to the ability or inability of an entrepreneur to determine within acceptable limits what certain costs of his proposed project, over which he can exert little or no control, will be and whether his contemplated investment decision therefore merits further study at a given time. If, for example, readjustability was limited to no higher than "X" percent of the increase in the cost-of-living index, adjusted semi-annually, with uncompensated-for rises in the index deferred until subsequent periods when the rise was less than the maximum (i.e., accrued over time) such a limitation would provide a form of guarantee against unpredictable swings in costs during the particularly critical start-up period for businesses. Under this approach, the GOU could agree to bear a portion of the devaluation risk unilaterally and unconditionally, or sub-loan interest rates could include a margin to the GOU fund as compensation for conditioning loans on less than full readjustability.

Under AID Loan-022 for Capital Goods Imports, all AID dollar loans were repayable in pesos readjusted to dollar debt, with full devaluation risk borne by the sub-borrower. Peso reflows from these sub-loans are being relent with adjustability limited to a maximum of 17.5 percent every six months (35 percent per year). In retrospect, this percentage was insufficient to cover the effects of inflation adequately, given the rates of inflation over the past years (1970 - 20.9 percent; 1971 - 35.7 percent; 1972 - 94.7 percent; 1973 - 77.5 percent; 1974 - 107.3 percent; 1975 - through April - 18.9 percent). (The GOU projection for 1975 is 50 percent.)

An essential difference between the L-022 Project and the proposed Program is that, under L-022, single unit procurement of a capital good or

as an official bank and as a depository and intermediary for state funds. Under present circumstances, the BOR would possess a major financial advantage as a participating intermediary in the proposed agri-industrial program in addition to its dominance within the commercial banking structure as a whole because of its size and numerous branch offices. Since a major objective of the proposed loan program is to enlist the active participation of all the country's private commercial banks in order to foster the widest possible interest in the program on the part of potential entrepreneurs or entrepreneurial groups, project negotiations with the GOU focused on resolving this issue to ensure that all commercial banks were treated equally under the Program. In addition, the major incidence of such a tax falls on the borrower directly, since it is passed on to him by the commercial banks, thus serving to increase the costs of borrowed funds and total project requirements, and therefore acting as a constraint to entrepreneurial initiative.

The inefficiency and undesirability of the banking tax is currently widely recognized. Negotiations with GOU representatives included the AID requirement as a condition for the contemplated assistance that the banking tax be removed, at least to the effect that all sub-loans under this Program will be exonerated from this tax. This condition would also be a requirement of the proposed IBRD assistance for its Industry Sector Loan. GOU officials concurred with this request and indicated that one means of effecting it would be to include an appropriate provision in the proposed legislation on monetary readjustment currently before the <u>Consejo de Estado.</u> Whatever means is selected, exoneration of this tax on activities of this Program is a recommended condition precedent to disbursement, fully agreed to by GOU officials.

(This same tax was an issue during negotiations regarding the AID Capital Goods Imports Loan - L-022, in 1969. Rescindment of the tax was desired then also but, due to the more tenuous political situation at that time, it was decided that the issue could not be confronted. It is indeed an indication of the changes currently underway in Uruguay that GOU officials are now confident that amending the tax provision can be effected without political problems.)

(Professor Harberger reviewed this and other Uruguayan value-added taxes in a monograph in September, 1974. His argument and suggestion that the elimination of the banking activities tax should have the first priority in review of the value-added system were probably instrumental in marshalling GOU opinion in favor of dealing with this issue.)

4. <u>Credit Guaranty Arrangements</u>

A characteristic of the commercial banking system in Uruguay, as in all of Latin America, is the extent of guaranties and collateral required of sub-borrowers. In most cases, all except those involving the most widely known and established borrowers, collateral requirements typically range from 200 to 300 percent of the value of the sub-loan requested. Where possible, compensating deposit balance arrangements may be worked out which reduce the amount of collateral required, but also involve a cost to the sub-borrower. While these large collateral requirements are partially explainable in terms of commercial banks' concerns regarding the repayment prospects of requested loans, particularly during periods of high inflation, a more basic answer concerns the very superficial loan review performed by the banks with little or no attention given to the proposed project itself in terms of its ability to generate revenues to repay the sub-loan.

Under the contemplated Program, which will utilize the commercial banking system as the "outreach" of the Agri-Industrial Development Fund, maintenance of the existing collateral procedures would effectively reduce the expected intermediate target group only to those possessing significant fixed assets, an undesirable effect since newly formed entrepreneurial groups, organizations, or cooperatives would be unlikely to be eligible for sub-loans.

Agencies of the GOU involved in the project are in agreement with this position and the need to design an element of this Program to deal with it. Two proposals have been discussed with the GOU which potentially will resolve the problem. One involves a credit insurance policy, and the other a guaranty arrangement.

Under the credit insurance proposal, a participating commercial bank would be able to obtain, for a premium, a credit insurance policy from the Central Bank which would cover a portion, to be determined, of the commercial risk of sub-loans, thus enabling the commercial bank to reduce its collateral requirements to sub-borrowers. The premium to be paid by the commercial bank would, of course, be passed on to the sub-borrower. In order to implement this type of mechanism, an intensive analysis of likely and typical prospective projects under this Program would have to be performed, as well as an actuarial review of the risks of default to be faced. As there is no significant body of development lending experience in Uruguay, analysis would likely be based on experiences within several similar Latin countries. Once the actuarial likelihood of risk is established, the extent of coverage judged necessary to encourage commercial banks to reduce collateral requirements would have to be set and a fee for the credit insurance determined. To underwrite the insurance, the Central Bank would set aside or earmark a portion of its reserves (reserves to insurance ratio would be determined on the basis of examining loan default histories as indicated earlier), to cover possible or probable commercial bank losses.

Under the credit guaranty arrangement scheme, a slightly different approach is considered, wherein the mechanism proposed would operate similarly to that of the Productive Credit Guaranty Program (Moss Amendment to the FAA). In this approach, the Central Bank would share the commercial risk on approved sub-loans with the commercial bank assuming, for example, 25 percent or more of the "front end" of the risk, and the Central Bank bearing the majority (up to 75 percent) or the remaining portion. In the event of default by the sub-borrower, the commercial bank would be responsible for and interested in (indeed, have a major stake in) attempting to recover its portion of the loan. Such a sharing of the responsibility could induce the commercial banks to reduce current collateral requirements to more reasonable levels and would maintain commercial banks' interest in loan monitoring and follow-up. A fee for this risk-sharing arrangement would also be charged by the Central Bank in order to capitalize a small fund over time to cover potential losses.

Each of these concepts has been discussed with officials in both the public and private sector, in banking as well as in business, and the idea was determined to be highly desirable. The IBRD also is in agreement with the need for such programs. GOU officials have agreed to the USAID negotiating position that an intensive analysis and a plan for reducing collateral requirements of commercial banks participating in this Program, using these recommended or other approaches, will be included as a condition precedent to disbursement of loan funds. Whichever of the two approaches are chosen by the GOU for study, the USAID plans on requesting the TDY assistance of experts from AID/W, OPIC or other international agencies to assist the GOU and Mission personnel if the credit insurance mechanism is selected, or former OPIC personnel familiar with the Moss Amendment program if the guaranty sharing scheme is opted for.

With regard to the guaranty arrangement, the Mission understands that with the transfer of the Productive Credit Guaranty Program authority from OPIC to AID, AID/W intends to explore and consider alternative uses of both the guaranty authority for productive credit purposes and the OPIC-designed model of the PCGP itself in order to expand the potential benefits of such a program to small and medium farmers. The a plication of the proposed guaranty scheme in this loan, based on the experiences of the OPIC model to date, would appear to be most appropriate in this light. GOU officials have indicated substantial interest in the guaranty scheme, in recognition of the need to provide for the legitimate concerns of the commercial banks under this Program, as an essential step in working through banking and private sector businesses to bring benefits to the target troup.

Therefore, the Mission intends to attach highest priority to a request for OPIC and/or AID/W assistance in the analysis and elaboration of either mechanism selected.

5. Flow of Funds - Disbursements

Analysis of potentially eligible sub-projects identified during project development (Annex G) and discussions with the Unidad Asesora indicate that the total resources of the Fund will be disbursed within the three-year life-of-project period. The estimated disbursement schedule (for combined dollar and peso resources) is as follows:

Source	1st Yr.	2nd Yr.	3rd Yr.	Total	
AID (US$)	.55 m	1.7 m	2.75m	5.0 m	69%
GOU (US$ equivalent)	.25 m	1.15m	.85m	2.25m	31%
Total	.8 m	2.85m	3.6 m	7.25m	100%

First year disbursements will be modest, given the need for the Unidad Asesora and the Mixed Commission to work into the expanded functions and responsibilities each will have under the Program. Project approvals will increase significantly in the second year, and all dollar funds are expected to be committed by the third year. Also, analysis of those projects under consideration by the Unidad Asesora which were accompanied by completed feasibility studies indicates that from five to eight months will be the average time between commitment and disbursement of funds for capital goods procurement, given special fabrication requirements and past experience with such procurement. This consideration also bears on the modest first-year disbursement projection.

GOU counterpart contributions may exceed the US$2.25 million minimum. The breakdown of estimated dollar versus local currency requirements contained in the list of illustrative projects suggests an average 50/50 split between these. While a portion of estimated local currency requirements of potential sub-projects may be available locally (e.g., working capital from commercial banks) most sub-project requirements will be for medium to longer term purposes. In order to ensure that sufficient pesos are available to meet demand, the GOU has indicated it will agree to consult with AID jointly and regularly on this issue for the purpose of determining peso requirements of the Program. Such joint reviews would be held every six months or other regular period as necessary.

A probable source of such additional pesos as required may be reflows from loans under the IBRD credits. A large portion of that loan (US$20.0 million) will disburse rapidly, generating rapid and more than sufficient availabilities for the GOU to draw upon for this purpose.

6. Repayment Capacity

The loan will be made directly to the GOU. Eligible sub-projects to be promoted and assisted involve activities which should make significant contributions to the internal economic growth of the country over time through increasing internal production, efficiency, employment, internal demand, and foreign exchange earnings. In this latter area alone, the combined effects of projected sub-projects should provide significant support to continuing efforts to improve Uruguay's foreign exchange and general balance of trade situation.

In view of the improved economic and fiscal policies of the GOU economic team and the overall prospects for regaining control over inflation and the economy in general as shown by the GOU's commitment to the requirements of the IMF Standby arrangement and other policies, the near and medium-term outlook for Uruguay can be considered bright. Taken together, the prospects for repayment of this loan are quite reasonable. Moreover, the GOU has a fine record in repayment of AID loans.

D. Environmental Impact

Potentially undesirable effects of this project on the environment are expected to be minimal. Industry activities to be financed will be small and medium-sized with the majority to be located in rural areas. Many sub-projects will involve active direct or indirect management of fields under production and technology to be applied (e.g. leveling and improving of farm lands) is expected to be beneficial rather than harmful to the environment. Nonetheless, it is possible that an activity requesting financing may not have adequately considered such environmental effects and to ensure that adequate consideration is given, Implementation Letter N° 1 will specify this as a requirement of the sub-project appraisal review responsibilities of the Unidad Asesora.

E. Role of Women

A study recently concluded by the Mission on female labor force participation in Uruguay permits an estimation of the effects of the Loan on women's participation in the project.

The occupational distribution of working women (as of the last available published data, from the census of 1963) shows that more than 80% of the female labor force is employed in occupations in which women are over-represented. In these occupations, the percentage of women employed is higher than their representation in the total labor force (25%); women workers are apparently specifically sought for these jobs, and do not seem to be interchangeable with male workers. Thus, any economic activity that increases the demand for workers in these "feminine" occupations would be equivalent to an increased demand for woman workers.

The proposed Loan would increase economic activity and thus demand for labor in at least the following areas: food processing, the production of capital goods, capital construction, financial services and technical assistance.

1. Food Processing.

The census classification Bottlers and Packers is 69.2% female. Workers in Paper Production are 53% female, and, by sector, 46% of the workers in the Bottling and Conservation of Fruits and Vegetables are female. Increase in activity in the processing of food products would expand the demand for workers in these occupations, and disproportionately increase the demand for female workers.

2. Locally made Capital Goods.

Women are under-represented in occupations having to do with the production of machinery, and increase in activity in this area would not affect many directly.

3. Financial Services.

Women's representation in banking sector is also below their overall representation in the labor force. They are over-represented, however, in the support occupations such as typing, steneography, operators of office machinery, in which demand would increase as a result of the increased paper work generated by applications for Loan funds.

4. Civil Construction.

Few women are employed in this area, except, again, as office workers.

5. Technical Assistance.

Women are under-represented in all professions except the health, teaching and artistic professions, as well as at the higher levels of government service. Therefore, an increased demand for experts is unlikely to affect the demand for women in the labor force.

It is more difficult to estimate the effect of the proposed Loan on women insofar as they are members of the target group of small and medium farmers. There are no figures available on the ownership of farms by sex: though there are some women farm owners (usually widows or daughters), the overwhelming majority of farm owners are men. Women would benefit as members of the target group primarily as spouses.

Virtually no women are employed in farming or crop cultivation except as they provide uncompensated labor on family farms. Increased prosperity on these farms, however -- the source of most of the fruit and vegetable production of the country -- would increase the standard of living of the family, and therefore benefit the women.

The recent AID study found that despite the highest levels of non-agricultural female labor force participation in Latin America, the potential supply of female labor is larger than the demand. The female population in Uruguay is well educated, and, with low birth rates, is relatively unburdened by health and childcare problems present in populations with high fertility levels. That female labor force participation is not higher is undoubtedly due to the stagnation of the economy, expressed by a lack of demand. Since many women, especially married women, are part of a secondary pool of labor, expansion of economic activity and the generation of new employment opportunities is likely to draw on this secondary labor pool, as well as shifting employed women from domestic service to more productive occupations, and thus utilize what is at present an under-utilized resource.

PART VI - LOAN ADMINISTRATION

A. Implementation Schedule

It is anticipated that the Loan will be authorized by June 30, 1975, and that the Loan Agreement will be signed by August 31, 1975. The IBRD Industry Sector Loan Appraisal Mission will arrive in Montevideo on June 23, 1975 to begin their analysis in preparation for the Bank's Industrial Sector Loan. It is anticipated that the Mission's analysis and recommendations will be completed by July 31, 1975. Those recommendations will include a definitive formula for determining sub-loan interest rates and terms under the IBRD loan, which will be the same as those to be applied under this Project. Between July and October, 1975, the GOU will satisfy the recommended conditions for the IBRD loan, and the Bank loan will be presented to the IBRD Board of Directors for authorization in October. Conditions precedent to disbursements for the proposed AID loan should be met well before the terminal date of December 31, 1975, allowing disbursements for technical assistance to begin late CY 1975 and for capital goods imports to begin subsequently (probably early CY 1976). The following are target terminal dates for the Loan, which are in accordance with the periods permitted under AID Policy Determination 57:

- Terminal date for meeting all conditions precedent to disbursement: December 31, 1975
- Terminal date for issuance of commitment documents: June 30, 1978
- Terminal date for Loan disbursement: December 31, 1978

As the analysis in Part V.B. above has demonstrated, substantial demand for Loan funds, has been identified, and based on discussions regarding projected disbursements with GOU officials, the Mission believes that implementation of this Loan within the prescribed time period is within the capabilities of the Unidad Asesora and the Uruguayan banking and private enterprise sectors.

B. Evaluation Plan

A joint Evaluation Committee will be established within two months after conditions precedent to initial disbursements under the Loan have been met. The Committee shall consist of a representative of the Unidad Asesora, a representative of the Central Bank, a representative of the Office of Planning and Budget (OPP), and representatives of the USAID. A Unidad Asesora representative will be selected Chairman, as it will assume major responsibility for evaluation. Representatives of the Ministry of Economy and Finance and the Ministry of Agriculture and Fisheries, as well as of the commercial banking community, may be invited to attend specific evaluation sessions as appropriate to afford opportunities for comprehensive information on all aspects of project implementation.

Evaluation and reporting of Loan implementation will take four forms:

1. Continual self-evaluation of the Unidad Asesora to examine its review and analysis of sub-project proposals, as well as any problems encountered in the application of the selection criteria agreed upon for this Loan.

2. The Unidad Asesora will submit monthly reports to the USAID which will include a breakdown of sub-projects submitted, approved, in process, and disapproved during the reporting period. Brief summaries of these sub-projects describing the amount of financing requested, the nature of the enterprise requesting credit, the purpose of the sub-loan (expansion, new enterprise, etc.), the volume of projected production and exports, and the nature and extent of the sub-projects' impact on small and medium farmers will be included, as well as the reasons why a sub-project proposal was approved or disapproved for financing under the Loan. These reports will also include the Unidad's record of amount of project funds disbursed or committed (with a breakdown of dollar and local currency disbursements and commitments) during and through the reporting period.

3. Representatives of the Unidad Asesora, and possibly OPP and the Central Bank, will meet with USAID representatives at least every six months for the purpose of determining the projected level of local currency the GOU will make available to the project in the subsequent six-month period. The amount will be based on the number and nature of sub-loan proposals in various stages of analysis and the financial requirements of sub-loans for which approval is anticipated during the following period.

4. Formal evaluation reviews by the Evaluation Committee will take place as required, but at least once a year.

These reviews will examine the projects approved by the Unidad Asesora during the review period; determine the extent to which Loan purposes are being achieved; determine the extent to which Loan outputs are being produced, as measured against indicators established in the Logical Framework; and review problem projects, issues, and any operational difficulties that have been encountered. A final evaluation of overall project success and effectiveness will be conducted at project termination. The results of all reviews will be documented in a report from the Evaluation Committee's Chairman to the Director of the Unidad Asesora and to USAID. Such reports will identify any problems in project implementation, and recommend corrective action(s) to be taken. The Director of the Unidad Asesora will determine the individual(s) responsible for taking such action.

The members of the Evaluation Committee will define the need, if any, of outside assistance (including consulting services or short-term assistance from AID/W) in the evaluation process, and arrange to procure such assistance, if required. AID will bear the cost of any AID/W personnel; Loan funds allocated to technical assistance may be used to procure short-term contract assistance, as appropriate.

C. Disbursement and Procurement Procedures

All funds provided by AID under this Loan will be for foreign exchange costs, principally for capital goods imports, but including up to US$500,000 for foreign technical assistance. Disbursement of Loan funds will be handled through Letters of Commitment procedures. After the initial conditions precedent are met, AID Letters of Commitment will be opened and increased upon requests made by the Unidad Asesora on the basis of foreign exchange requirements of approved sub-projects. Letters of Credit will be issued by the commercial banks or the BOR, in response to sub-borrower needs for approved sub-projects. Procurement will be carried out in accordance with normal AID procedures. Small Business Notification for procurement of imported goods and materials will be made in accordance with AID requirements as modified for ICIs by procedural instructions and guidance.

Commodities eligible for procurement with Loan funds include all capital goods, including spare parts, for the establishment or expansion of agri-industries, as well as essential raw or intermediate materials determined by the technical review of the Unidad Asesora to be an element critical to sub-project establishment which are unavailable locally in quantity or quality required.

Procurement will be from the United States and other eligible countries under Geographic Code 941. Excluded from procurement with Loan funds are POL products, fertilizer, and such other raw material inputs to food-processing enterprises which are available locally.

D. AID Reporting and Monitoring Responsibilities

Primary responsibility for administering the project will belong to the Ministry of Industry and Energy, through the Unidad Asesora. USAID's role is expected to be principally one of monitoring Loan performance, and participation in reviews and evaluations outlined above.

This monitoring will be primarily the responsibility of USAID's Controller and Loan and Program Offices, with the Food and Agriculture Office providing any necessary back-up support. TDY personnel will be requested from AID/W as needed to assist the Mission in review of legal requirements, Loan administration, contracting and procurement implementation. Frequent USAID contact will be maintained with the Unidad Asesora, the OPP, the Central Bank, and the commercial banking sector to assist in carrying out the project purposes.

In the Loan Agreement, AID will reserve the right to review and approve sub-projects using over US$ 350,000 in AID dollar funds, following Unidad Asesora and Mixed Commission review and approval of these sub-projects. Because the analysis of the sub-project will have been completed by the Unidad Asesora and approval granted to the sub-project through the Loan implementation mechanism prior to USAID review, it is not anticipated that major monitoring responsibilities will be involved in this process, if USAID chooses to exercise this option.

Opening and increasing the AID Letter of Commitment used for Loan disbursement will be the responsibility of the Mission Controller. Monthly financial monitoring of disbursements, based on information submitted by the Unidad Asesora, will also be the Controller's responsibility. Letters of Credit, however, will be the responsibility of the individual bank making the sub-loan, and should not require any additional responsibility for USAID.

The USAID will submit to AID/W a monthly summary of Loan implementation progress as part of its regular monthly Loan status report. In addition, following formal evaluation reviews held by the project Evaluation Committee, the Mission will submit the appropriate project appraisal form to AID/W.

For monitoring and evaluation purposes, the Unidad Asesora will provide to USAID monthly reports which include a breakdown of sub-project approval status and project funds committed and disbursed in and through the reporting period. These monthly reports are more fully described in the Evaluation Plan section, above.

E. Conditions and Covenants

The conditions precedent and the covenants to be included in the Loan Agreement have been spelled out in detail in the Summary and Recommendations, Part I, Section J. (Page x).

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SUPPLEMENT 1

ANNEX A

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

(INSTRUCTION: THIS IS AN OPTIONAL FORM WHICH CAN BE USED AS AN AID TO ORGANIZING DATA FOR THE PAR REPORT. IT NEED NOT BE RETAINED OR SUBMITTED.)

Life of Project:
From FY______ to FY______
Total U.S. Funding US$ 5,000,000
Date Prepared: June 6, 1975

Project Title & Number: Agri-Industry Development Loan

PAGE 1

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Program or Sector Goal: The broader objective to which this project contributes:	Measures of Goal Achievement:		Assumptions for achieving goal targets:
1. To promote the development of an agri-industrial infrastructure capable of expanding non-traditional exports, thereby producing	1. a. 1, 6, & 7 new or expanding agri-industrial enterprises producing non-traditional products established in first, second, and third year, respectively.	1. a. Industrial census data; GOU statistics and records.	Present and projected policies and programs affecting prices, imports, exchange rates, credit, taxes, marketing, land use, investments, and technical assistance/extension service will continue to provide incentives for increased investment in agri-industrial enterprises, agricultural production, and non-traditional exports.
		b. Industrial census data; GOU statistics and records.	
2. Increased real foreign exchange earnings, and	b. Exports of non-traditional agri-industrial products increase annually.	c. Trade statistics.	
3. Increased production, employment, and income opportunities for the target group.	c. Relation of agri-industrial exports to total exports increases over 1975 percentage.	d. International agencies' economic reports and surveys (IMF, IBRD, IDB, UNDP, FAO); Embassy economic reports.	
	2. Increased foreign exchange received for Uruguayan exports over 1975 level.	2. Trade statistics.	
	3. a. Measurable increases in small/medium farmer production in target areas.	3. a. Production data; farm surveys.	
	b. Measurable increases in small and medium farmer income by 1978 in target areas.	b. Census data; farm surveys.	
	c. Annual increase in direct and indirect employment in agro-industries.	c. Census data; farm surveys; GOU industrial and employment statistics; industrial surveys.	

AID 1020-28 (7-71)
SUPPLEMENT 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY ________ to FY ________
Total U.S. Funding US$ 5,000,000
Date Prepared: June 6, 1975

Project Title & Number: Agri-Industry Development Loan

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Project Purpose:	Conditions that will indicate purpose has been achieved: End of project status.		Assumptions for achieving purpose:
1. To provide a package of financial and technical services to private entrepreneurs and cooperatives for the successful establishment or expansion of agri-industries (food processing);	1. a. The majority (90%) of private entrepreneur or cooperative sub-projects under the Project are operating reasonably in accordance with their approved development or expansion proposals (in terms of production revenue, and exports). b. 12 to 15 agri-industries have received assistance through Unidad Asesora by 1978.	1. a. Unidad Asesora records and reports; records of agri-industry sub-projects. b. Records of Unidad Asesora. c. Joint interim Project reviews. d. Site visits.	1. a. Conditions in export markets will not disfavor Uruguayan production. b. No major crop failures occur. c. GOU policies will continue to encourage private investment in the industrial sector. d. Demand for the package of financial and technical services is not significantly less than estimated and continues over time. e. Small/medium farmers will respond to those production and marketing alternatives introduced. f. Average sub-project received US$ 500,000 from the Fund.
2. to establish an effective delivery system for these services; and	2. The Unidad Asesora: is employing appraisal banking techniques in project review and processing (in assisting sub-project development); in evaluating project proposals effectively (i.e. defaults and claims on credit insurance fund by commercial banks are below or within acceptable limits, and processes credit applications within reasonable periods of time.	2. Unidad Asesora Records. - Joint interim project reviews. - Final evaluation of loan. - Commercial bank and BOR records. - Central Bank records.	
3. to create new production and marketing alternatives for small and medium farmers through the establishment of viable agri-industrial enterprises.	3. a. N°'s of non-traditional agri-industry enterprises purchasing raw agricultural production from small/medium farmers is increasing annually. b. Increase in production of non-traditional crops in small/medium farm areas.	3. a. Records of agri-industries; Unidad Asesora reports. b. Production data: census data; occupational statistics; farmer surveys; sub-project feasibility studies.	

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Project Title & Number: Agri-Industry Development Loan

Life of Project:
From FY ________ to FY ________
Total U.S. Funding US$ 5,000,000
Date Prepared: June 6, 1975

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Outputs:	Magnitude of Outputs:		Assumptions for achieving outputs:
1. Establishment of an Agro-Industrial Development fund.	1. Fund capitalization is US$7.25 million (= to AID and GOU contribution).	1. Letter of certification from Borrower.	1. None.
2. Expanded and strengthened project appraisal capability of Unidad Asesora.	2. N°s. of positions increased to be according to plan submitted as C.P. to disbursement.	2. and 3. a. Unidad Asesora statement of operating policies and procedures. b. Unidad Asesora reports to USAID. c. Joint reviews.	2. and 3. IBRD and UNDP assistance to Unidad Asesora will be realized.
3. Unidad Asesora review, appraisal, and assistance to sub-project investment proposals (feasibility studies undertaken, technical assistance arranged).	3. Annual N°s. of these services will vary according to demand and nature of sub-project proposals.		
4. Establishment of a credit insurance scheme to induce commercial banks to reduce collateral requirements on sub-loans to borrowers.			

AID 1020-28 (7-71)
SUPPLEMENT 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY ________ to FY ________
Total U.S. Funding US$5,000,000
Date Prepared: June 6, 1975

Project Title & Number: Agri-Industry Development Loan

PAGE 4

NARRATIVE SUMMARY		OBJECTIVELY VERIFIABLE INDICATORS			MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Inputs:		Implementation Target (Type and Quantity)				Assumptions for providing inputs:
1. AID.		1st.Year	2nd.Year	3rd.Year		
a. Capital goods imports	US$4,500,000				USAID Records.	Funds will be available from AID and from GOU budget and roll-overs from AID loan funds.
b. Technical assistance					Progress Reports.	
1.To implementing agency	US$ 150,000				Unidad Asesora Records/Reports.	
2.To sub-projects	US$ 350,000	US$ 550,000	1,700,000	2,750,000		
TOTAL	US$ 5,000,000					
2.GOU Counterpart	US$ 2,250,000	US$ 250,000	1,150,000	850,000		
3. Sub-borrowers Contribution to sub-project investment	US$2,750,000	US$ 300,000	1,075,000	1,375,000		

ANNEX B

CERTIFICATION PURSUANT TO SECTION 611 (e)
of the FAA of 1961, as amended

I, Leonard J. Horwitz, the principal officer of the Agency for International Development in Uruguay, having taken into account, among other things, the maintenance and utilization of projects in Uruguay previously financed or assisted by the United States, do hereby certify that in my judgement the Government of the Oriental Republic of Uruguay has the financial, administrative and human resource-capability to maintain and utilize effectively the funds to be provided by the United States of America under the terms and conditions of the proposed Agri-Industry Development Loan.

This judgement is based primarily on the facts developed in the Capital Assistance Paper for the proposed Loan of US$ 5.0 million which discusses in detail the economic, fiscal, and monetary policies of the Government of the Oriental Republic of Uruguay and the capabilities of the Primary Executing Agency of that Government and determines the manner in which that organization possesses and will develop adequate financial, administrative and human resource capability to utilize and maintain effectively the project.

Leonard J. Horwitz
AID Representative

June 7, 1975

Nov 11

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.

FAA, 1973 - Foreign Assistance Act of 1973.

App. - Foreign Assistance and Related Programs Appropriation Act, 1974.

MMA - Merchant Marine Act of 1936, as amended.

BASIC AUTHORITY

1. *FAA § 103; § 104; § 105; § 106; § 107. Is loan being made*

   a. for agriculture, rural development or nutrition;

   1\. a) The project will provide support to agriculture through promoting agro-industrial food processing projects, which will increase the production, income, and/or employment of small and medium sized farmers in rural areas.

   b. for population planning or health;

   b) N/A

   c. for education, public administration, or human resources development;

   c) N/A

   d. to solve economic and social development problems in fields such as transportation, power, industry, urban development, and export development;

   d) The project supports a program of development and expansion of agro-industry projects which will produce and/or process non-traditional products for export markets.

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e. in support of the general economy of the recipient country or for development programs conducted by private or international organizations.

e. The project will provide support to the economic development programs of the GOU for development of the agro-industry (food production - food processing) sub-sector.

COUNTRY PERFORMANCE

Progress Towards Country Goals

2. *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.

A. 1) The GOU is stimulating expanded food production and marketing by a series of measures including favorable pricing policies, reduction of export taxes, and imposition of land productivity tax to foster better land use and provide incentives for the application of new technology.

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

2) Consistent with the National Development Plan, the GOU is making a determined effort to foster foreign and domestic private enterprise and investment by liberalizing or freeing the paternalistic controls on the private economy, and incentivizing savings and investment through positive foreign investment and industrial promotion laws. The GOU is also maintaining or undertaking sound fiscal, credit, wage and price, and exchange and payment policies which will encourage private enterprise and investment.

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

(3) The private sector is being encouraged to play a more active development role through such measures as industrial promotion laws, tax and price incentives for industrial and agricultural producers, and mechanism for mobilizing domestic savings for development. The GOU actively consults with the private sector on economic policy and the GOU has launched an ambitious program to expand the participation of lower income groups in worthwhile social development activities.

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

(4) a) A series of reform measures being undertaken during 1975 involving fiscal, monetary, credit and commercial policy should serve to reduce the fiscal deficit, stimulate domestic savings and permit an expanded level of public investment.

(b) Diverting such resources for unnecessary military expenditure (See also Item No. 20) and intervention in affairs of other free and independent nations.) (See also Item No. 11)

b) Uruguay is not diverting development resources for unnecessary military expenditures.

(5) 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.

(5) The GOU is carrying out a reform of the costly social security system, is improving its tax collection capability with AID assistance, and through the land productivity tax and colonization program, is endeavoring to improve land use. Uruguay has traditionally respected the rule of law and individual freedoms consistent with public order. It also favors an expanded private sector role in the development process as will be promoted through this project.

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

(6) Uruguay adheres to the principles of the Act of Bogotá and the Charter of Punta del Este.

(7) Attempting to repatriate capital invested in other countries by its own citizens.	(7) Uruguay has recently made a determined effort to provide incentives for repatriating capital invested abroad.
(8) Otherwise responding to the vital economic, political, and social concerns of its people, and demonstrating a clear determination to take effective self-help measures.	(8) The GOU efforts now underway involve fundamental structural reforms, respond to a determination to stabilize the economy and foster growth with equity. Its significant self-help measures have earned the active support of the IMF, IBRD, IDB, AID and other international agencies.
B. Are above factors taken into account in the furnishing of the subject assistance?	B. The above factors have been taken into account in the furnishing of subject assistance.

Treatment of U.S. Citizens by Recipient Country

3. 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?	3. Yes. However, payment is being made on a regular basis of these debts.
4. 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?	4. No.

5.

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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. N/A

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

a. N/A

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

b. N/A

Relations with U.S. Government and Other Nations

6. FAA § 620(a). Does recipient country furnish assistance to Cuba or fail to take appropriate steps to prevent ships or aircraft under its flag from carrying cargoes to or from Cuba?

6. Uruguay does not furnish assistance to Cuba, nor does it allow ships or aircraft under its flag to carry cargoes to or from Cuba.

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7. FAA § 620(b). If assistance is to a government, has the Secretary of State determined that it is not controlled by the international Communist movement?

7. The Secretary of State has determined that Uruguay is not controlled by the international Communist movement.

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

8. The assistance is not directed specifically to enterprises which will compete in the U.S. The primary export markets for these sub-projects will be non-U.S. markets. However, if a problem arises with respect to any proposed sub-project enterprise, it will be handled in accordance with policies in effect at that time.

9. FAA § 620(f). Is recipient country a Communist country?

9. No.

10. FAA § 620(i). Is recipient country in any way involved in (a) subversion of, or military aggression against, the United States or any country receiving U.S. assistance, or (b) the planning of such subversion or aggression?

10. No.

11. 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?

11. No.

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12. FAA § 620(l). If the country has failed to institute the investment guaranty program for the specific risks of expropriation, inconvertibility or confiscation, has the A.I.D. administration within the past year considered denying assistance to such government for this reason?	12. Uruguay is now considering an OPIC investment guarantee agreement.
13. FAA § 620(n). 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?	13. Uruguay does not permit trade with North Viet-Nam.
14. 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?	14. Uruguay is not in default on the payment of interest or principal of any A.I.D. loan covered by this Act.
15. FAA § 620(t). Has the country severed diplomatic relations with the United States? If so, have they been resumed and have new bilateral assistance agreements been negotiated and entered into since such resumption?	15. Not applicable. Uruguay has consistently maintained diplomatic relations with the United States.
16. FAA § 620(u). What is the payment status of the country's U.N. obligations? If the country is in arrears, were such arrearages taken into account by the A.I.D. Administrator in determining the current A.I.D. Operational Year Budget?	16. Uruguay is not in arrears on its U.N. assessment.

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17. FAA § 481. Has the government of recipient country failed to take adequate steps to prevent narcotic drugs and other controlled substances (as defined by the Comprehensive Drug Abuse Prevention and Control Act of 1970) produced or processed, in whole or in part, in such country, or transported through such country, from being sold illegally within the jurisdiction of such country to U.S. Government personnel or their dependents, or from entering the U.S. unlawfully?

17. No. Uruguay has provided exemplary cooperation with U.S. authorities in control of international narcotics traffic.

18. FAA, 1973 § 29. If (a) military base is located in recipient country, and was constructed or is being maintained or operated with funds furnished by U.S., and (b) U.S. personnel carry out military operations from such base, has the President determined that the government of recipient country has authorized regular access to U.S. correspondents to such base?

18. Not applicable.

Military Expenditures

19. 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 is to be coordinated with the Bureau for Program and Policy Coordination, Regional Coordinators and Military Assistance Staff (PPC/RC).)

19. Uruguay maintains a modest military establishment.

a) 15 - 20% of the country's budget goes for military expenditures.
b) Foreign exchange expenditures for military equipment are minimal.
c) Uruguay has not purchased sophisticated weapons systems.

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CONDITIONS OF THE LOAN

General Soundness

20. FAA § 201(d). Information and conclusion on reasonableness and legality (under laws of country and the United States) of lending and relending terms of the loan.

20. Lending and relending terms are legal and reasonable under both U.S. and Uruguayan law.

21. 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?

21. The activity is considered to be economically and technically sound. An application for this loan is attached to this document. Detailed discussions before and after receipt of the application with the Borrower and executing agencies, major summaries of which are included in the project analysis section of this document, give sufficient information and assurance that the funds will be used in an economically and technically sound manner.

22. FAA § 251(b). Information and conclusion on capacity of the country to repay the loan, including reasonableness of repayment prospects.

22. It has been concluded that the Borrower, the Government of Uruguay, has the capacity to repay the loan based on the analysis presented in the attached project appraisal, and there is reasonable assurance of repayment.

23. FAA § 251(b). Information and conclusion on availability of financing from other free-world sources, including private sources within the United States.

23. Financing for this project is not available from other free-world sources, including private sources within the U.S., at a reasonable cost.

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24. *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 United States of the assistance?

24. a) The financial plan necessary to carry out the assistance has been prepared.

b) Yes. Cost to the U.S. for the assistance has been estimated.

25. *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 purpose of loan?

25. Other than the normal legislative approval for the loan, no further legislative action is required.

26. *FAA § 611(e).* If loan is for Capital Assistance, and all U.S. assistance to project now exceeds $1 million, has Mission Director certified the country's capability effectively to maintain and utilize the project?

26. Yes, see Annex A. for the Mission Director's Certification.

Loan's Relationship to Achievement of Country and Regional Goals

27. *FAA § 207; § 251(a); § 113.* 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;

27. The loan will emphasize: (a) private sector industry development, (b) cooperate with private sector initiatives to increase the production of food in Uruguay, (c) produce training benefits for employees and laborers associated with sub-projects developed, (d) contribute to improved health of the target group by making possible increases in incomes, and (e) strengthen the overall industry sector, (f) creation of jobs in agro-industrial food processing activities which will generate sub-stantial employment opportunities for women.

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(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; or
(f) integrating women into the recipient country's national economy.

28. FAA § 209. Is project susceptible of execution as part of regional project? If so why is project not so executed?

28. The project is not susceptible to execution as part of a regional project.

29. 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.

29. The project is consistent with the objectives of other developmental activities of the U.S. Government in Uruguay. It will contribute to the economic development of Uruguay by increasing foreign exchange earnings and helping to build an agro-industry base, and by increasing the incomes of small farmers.

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

30. The project to be financed will contribute to the achievement of self-sustaining economic growth through productive investment in activities for which Uruguay possesses relative comparative advantages, which will increase the generation of foreign exchange earnings.

31. 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.

31. Not applicable.

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AID 1240-2 (5-74)

32. FAA § 251(c); § 111. Information and conclusion on use of loan to assist in promoting the cooperative movement in Latin America.

32. It is contemplated that Uruguayan cooperatives will propose sub-projects for financing under this loan.

33. 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.

33. The last CIAP review (October 1973) emphasized the high priority of investments made in the Agricultural Sector.

34. 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.

34. The loan will directly contribute to assuring maximum participation in the task of economic development through the development of greater numbers of agro-industrial activities involving substantial private sector participation overall.

35. 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.

35. The type of program proposed has been frequently and variously cited as a missing element in Uruguay, and reflects a cooperative approach with the country's resources in economic development, and will contribute to an overall increase in self-government ability.

AID 1240-2 (5-74)

36. 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.

36. a) Yes (agro-industrial products.
b) Yes, directly.
c) Yes.
d) N/A
e) Yes, agro-industry.
f) Not applicable.

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

37. Not applicable.

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

38. 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. The loan will have a small positive effect on the U.S. economy through financing U.S. equipment and services, but will have no impact on areas of substantial labor surplus. The assistance is furnished in a manner likely to generate increased trade purchases from the U.S, thus positively affecting the U.S. B.O.P.

39. 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.

39. All of the funds under this loan will go directly to private enterprise through intermediate credit institutions to finance procurement from private sources.

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40. 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).	40. Through improving economic and financial stability in the country, the loan may encourage increased U.S. private trade investment, and services flows to Uruguay.
41. 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?	41. Certain engineering or professional services to be financed under the project may be provided by U.S. firms or their affiliates.
42. FAA § 602. Information and conclusion whether U.S. small business will participate equitably in the furnishing of goods and services financed by the loan;	42. Yes, the Loan Agreement or Implementation Letters will so provide as appropriate.
43. FAA § 620(h). Will the loan promote or assist the foreign aid projects or activities of the Communist-Bloc countries?	43. No.
44. 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	44. All technical assistance will be procured from private enterprise.

whether they are particularly suitable, are not competitive with private enterprise, and can be made available without undue interference with domestic programs.

Loan's Compliance with Specific Requirements

45. FAA § 110(a); § 208(e). Has the recipient country provided assurances that it will provide at least 25% of the costs of the program, project, or activity with respect to which the Loan is to be made?

45. Yes.

46. FAA § 112. Will loan be used to finance police training or related program in recipient country?

46. No.

47. FAA § 114. Will loan be used to pay for performance of abortions or to motivate or coerce persons to practice abortions?

47. No.

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

48. Yes.

49. FAA § 604(a). Will all commodity procurement financed under the loan be from the United States except as otherwise determined by the President?

49. Any commodities procured with loan funds will have their source and origin in the U.S. and Geographic Code 941 countries.

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

50. No bulk procurement is contemplated under this project.

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AID 1240-2 (5-74)

51. FAA § 604(d). If the cooperating country discriminates against U.S. marine insurance companies, will loan agreement require that marine insurance be placed in the United States on commodities financed by the loan?	51. The Mission is not aware of any discriminations against U.S. marine insurance companies by Uruguay. The Mission expects that the major portion, if not all, marine insurance for products purchased under this loan will be purchased in the U.S.
52. FAA § 604(e). If offshore 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?	52. Not applicable.
53. FAA § 604(f). If loan finances a commodity import program, will arrangements be made for supplier certification to A.I.D. and A.I.D. approval of commodity as eligible and suitable?	53. The loan will not finance a commodity import program.
54. 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.	54. U.S. Government excess property will be used to the extent feasible. The loan will finance private sector projects and no U.S. government excess property use is anticipated.
55. 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?	55. Not applicable.

AID 1240-2 (5-74)

56. FAA § 611(c). If contracts for construction are to be financed, what provision will be made that they be let on a competitive basis to maximum extent practicable?	56. A.I.D. procurement and contracting procedures will be followed.
57. 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 United States are utilized to meet the cost of contractual and other services.	57. The U.S. will finance all foreign exchange costs of the project and the borrower and sub-borrower will finance local costs. No U.S. owned foreign currency is available for this project.
58. App. § 113. Will any of loan funds be used to acquire currency of recipient country from non-U.S. Treasury sources when excess currency of that country is on deposit in U.S. Treasury?	58. No.
59. FAA § 612(d). Does the United States own excess foreign currency and, if so, what arrangements have been made for its release?	59. No.
60. FAA § 620(g). What provision is there against use of subject assistance to compensate owners for expropriated or nationalized property?	60. The Loan Agreement will not allow funds to be used for this purpose.

AID 1240-2 (5-74)

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

61. N/A.

62. 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?

62. No.

63. App. § 103. Will any loan funds be used to pay pensions, etc., for military personnel?

63. No.

64. App. § 105. If loan is for capital project, is there provision for A.I.D. approval of all contractors and contract terms?

64. Yes. This provision will be included in the Loan Agreement or Implementation Letters.

65. App. § 107. Will any loan funds be used to pay UN assessments?

65. No.

66. App. § 109. Compliance with regulations on employment of U.S. and local personnel. (A.I.D. Regulation 7).

66. Yes, it will be required through Implementation Letter.

AID 1240-2 (5-74)

67. App. § 110. Will any of loan funds be used to carry out provisions of FAA §§ 209(d) and 251(h)?

67. No.

68. App. § 114. Describe how the Committee on Appropriations of the Senate and House have been or will be notified concerning the activity, program, project, country, or other operation to be financed by the Loan.

68. The proposed Loan was included as a shelf loan in the FY75 Congressional Presentation. The Congress will be notified before any FY 75 funds are authorized.

69. App. § 601. Will any loan funds be used for publicity or propaganda purposes within the United States not authorized by the Congress?

69. No.

70. MMA § 901.b; FAA § 640C.

(a) Compliance with requirement that at least 50 per centum of the gross tonnage of commodities (computed separately for dry bulk carriers, dry cargo liners, and tankers) financed with funds made available under this loan shall be transported on privately owned U.S.-flag commercial vessels to the extent that such vessels are available at fair and reasonable rates.

70. This provision will be included in the Loan Agreement.

(b) Will grant be made to loan recipient to pay all or any portion of such differential as may exist between U.S. and foreign-flag vessel rates?

b) No.

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ANNEX D

DRAFT LOAN AUTHORIZATION

Provided from: FAA Section 103 ("Food and Nutrition")

Uruguay: Agri-Industry Development Loan

Pursuant to the authority vested in the Deputy U.S. Coordinator, Alliance for Progress, Agency for International Development ("AID") by the Foreign Assistance Act of 1961, as amended, and the delegations of authority issued thereunder, I hereby authorize the establishment of a Loan ("Loan") pursuant to Section 103 of said act and the Alliance for Progress to the Government of the Oriental Republic of Uruguay ("Borrower") of not to exceed US$5.0 million to assist in financing the dollar costs of a program ("Program") to provide medium and long term financing and technical assistance for the development and expansion of agri-industrial and related enterprises in Uruguay. An amount not to exceed US$500,000 may be used for feasibility studies and technical assistance. The Loan shall be subject to the following terms and conditions:

1. Interest and Terms of Repayment

Borrower shall repay the Loan to the Agency for International Development within forty (40) years from the first disbursement under the Loan, including a grace period of not to exceed ten (10) years, with interest at the rate of two (2) percent per annum during the grace period and three (3) percent per annum thereafter on the outstanding disbursed balance of the Loan and unpaid interest.

2. Other Terms and Conditions

a. Goods, services (except for ocean shipping and marine insurance financed under the Loan) shall have their source and origin in Uruguay and countries included in AID Geographic Code 941. Marine insurance may be financed under the Loan only if it is obtained on a competitive basis and any claims thereunder are payable in freely convertible currencies. Ocean shipping financed under the Loan shall be procured in any country included in AID Geographic Code 941.

b. Conditions Precedent to Initial Disbursement for Dollar Costs of Technical Assistance to the Borrower.

Prior to the first disbursement or to the issuance of the first letter of commitment document under the Loan for eligible technical assistance to the Borrower, the Borrower shall, except as AID may otherwise agree in writing, furnish to AID, in form and substance satisfactory to AID, the following:

1. Evidence of the establishment by the Central Bank of a special fund for the purpose of administering the AID Loan and the Government of Uruguay counterpart resource contribution to the Project.

2. Evidence that it has authorized the Unidad Asesora of the Ministry of Industry and Energy to serve as the technical review group and principal executing agency for the administration of this Project.

3. Evidence of the establishment and responsibilities of a Special Commission whose functions will include the approval of sub-projects for financing with the resources of the Program.

4. Copies of:

(a) the approved operating policies of the Unidad Asesora;

(b) the approved organization and staffing pattern of the Unidad Asesora;

(c) an approved plan for carrying out objective and comprehensive reviews and appraisals of sub-projects submitted to the Unidad Asesora under the Project;

(d) a statement setting forth the standards and procedures which will be followed in approving and monitoring sub-loans and in providing, or facilitating the provision of, technical assistance to sub-borrowers;

(e) a plan for strengthening the professional and technical capacity of the Unidad Asesora in regard to project review, appraisal and monitoring, and the provision of technical assistance to projects in areas such as export promotion and export market development, and providing for the inclusion of an agri-industry advisor(s) to promote and assist agri-industrial enterprises in identifying and preparing sub-projects for financing.

c. Conditons Precedent to Subsequent Disbursement of Loan Funds.

Prior to the first disbursement or the issuance of the first letter of commitment document under the Loan, for purposes other than technical assistance to the Borrower itself, the Borrower shall, except as AID may otherwise agree in writing, furnish in form and substance satisfactory to AID, the following:

1. Evidence that the tax on banking activities ("Impuesto Unico") will not be applied to any transactions financed under this Program.

2. A Central Bank circular, describing the guidelines and regulations for utilizing the resources of the Project.

3. A proposal, including a time-phased implementation plan, for the establishment of a credit insurance fund or guaranty arrangement, to be administered by the Central Bank, to protect commercial banks against a portion of commercial financing risks involved in sub-borrowing.

4. A statement of the interest rate policy to be utilized under the Project in determining interest rate charges to sub-borrowers for approved sub-loans, including criteria for determining periods of amortization and grace, and the indexing system and the manner in which it will be utilized for readjustment of the outstanding principal amounts of sub-loans approved under this Project.

d. Covenants

1. The Borrower covenants that all commercial banks will have equal opportunity to participate in the Program, and that all commercial banks so participating in the Program will be treated equally with respect to all administrative procedures of the Program.

2. The Borrower covenants that the Central Bank circulars and guidelines regarding the implementation of this Project will not be changed without prior consultation and approval of AID.

3. The Borrower covenants that its contribution to this Project will be equal to no less than 30% of the costs of the Project, as described more fully in the Project Description - Annex A to this Agreement - and that it will make available in a timely manner the local currency for the requirements of the sub-projects approved for financing. The Borrower further covenants to meet jointly with representatives of AID once every six months, or more frequently as AID and the Borrower may jointly agree in writing, for the purpose of determining the projected levels of local currency the Borrower will make available to the Project in the subsequent period.

4. The Borrower covenants that all future reflows from this Loan will be allocated to finance local costs of future agri-industrial projects.

5. The Borrower covenants that in implementing this Loan, special priority and preference will be given to those agri-industrial sub-projects which maximize the benefits to small and medium farmers involved in the production of raw agricultural inputs.

6. The Borrower covenants that all sub-projects approved by the Special Commission which would utilize in the aggregate over $350,000 in A.I.D. funds will be submitted to A.I.D. for review and approval.

ANNEX E

TRANSLATION

Letter N° 114/75

28 February, 1975

Director
Agency for International Development

Dear Sir:

On behalf of the Government of Uruguay, I have the pleasure of confirming the request for financial assistance to the agro-industrial sector originally presented for a capital goods loan.

The Office of Budget and Planning has for some time determined the need for external financing to equip with modern machinery the existing or future enterprises that process food products for export with the purpose of promoting the establishment of new enterprises, increasing the production, and making them more competitive with foreign enterprise. The loan would include, among other elements, funds to finance feasibility studies, funds to finance the import of capital goods and the necessary raw materials, as well as funds to finance technical assistance for agro-industries to be developed with the purpose of eventaully incorporating new technologies applied to processing techniques and quality control.

The Government of Uruguay will provide the necessary internal credits for the working capital of those enterprises which will benefit from the program.

We have estimated the need for external financing in 10 million dollars which will be divided between the different components of the program in accordance with the results obtained from the studies being undertaken by the Office of Budget and Planning.

As you are aware, the Government is elaborating a macro-economic program which will enable the negotiation of a stand-by agreement with the FMI. The purposes of the loan being requested conform with the framework of the program as well as with the present Plan Nacional de Desarrollo.

Yours sincerely,

Ing. Q. Juan Jose Anichini
Director
Office of Budget and Planning

ANNEX B

Nota Nº 114/75

Presidencia de la República
Oficina de Planeamiento y Presupuesto
Dirección

AÑO DE LA ORIENTALIDAD

Montevideo, 28 de febrero de 1975.-

Sr. Director
de la Agencia para el Desarrollo
Internacional (A.I.D.)
PRESENTE.-

De mi mayor consideración:

Tengo el agrado de confirmar, en nombre del Gobierno, la solicitud de asistencia financiera al Sector agro-industrial originalmente presentada para un préstamo de bienes de capital.-

De tiempo atrás la Oficina de Planeamiento y Presupuesto ha determinado la necesidad de financiación externa para equipar con moderna maquinaria a las existentes o futuras empresas que procesan productos alimenticios para la exportación con el propósito de fomentar el establecimiento de nuevas empresas, incrementar la producción y hacerlas más competitivas en el exterior. El préstamo incluiría, entre otros elementos, fondos para financiar estudios de factibilidad, fondos para financiar la importación de bienes de capital y materias primas necesarias, así como también fondos para financiar asistencia técnica a las agro-industrias a ser desarrolladas con el fin de propender a la incorporación de nuevas tecnologías aplicadas a las técnicas de procesamiento y control de calidad.-

El Gobierno uruguayo proveerá los créditos internos necesarios para el capital de trabajo de las empresas beneficiarias del programa.-

Estimamos la necesidad de financiación externa en 10 millones de dólares que se discriminaría entre los distintos elementos del programa de acuerdo con los resultados de estudios que la Oficina de Planeamiento y Presupuesto está llevando a cabo.-

Como es de su conocimiento, el Gobierno está estructurando un programa macro-económico que posibilite la concertación de un acuerdo Stand-by con el F.M.I. Los propósitos del préstamo que se solicita encuadran perfectamente dentro de dicho programa así como dentro del Plan Nacional de Desarrollo vigente.-

Reitero al señor Director las expresiones de mi consideración.-

Ing. Qu. Juan José Arichini
Director

/rpc

ANNEX E

AÑO DE LA ORIENTALIDAD

Presidencia de la República
Oficina de Planeamiento y Presupuesto
Dirección

Nota Nº 205/75

Montevideo, junio 6 de 1975

Sr. Leonard J.Horwitz
Director
Agencia para el Desarrollo Internacional
Montevideo, Uruguay

De mi mayor consideración:

En nuestra nota Nº114/75 del 28 de febrero del año en curso, tuve el agrado de confirmar, en nombre de nuestro Gobierno, la solicitud de asistencia financiera cursada a la Agencia para el Desarrollo Internacional (AID) del Gobierno de los Estados Unidos de América,por un monto de diez millones de dólares, para apoyar un programa de desarrollo agro-industrial principalmente dirigido al sector de procesamiento de alimentos.

Por la presente, tengo igualmente el agrado de confirmar que el Gobierno de la República O. del Uruguay proveerá los créditos internos necesarios para cubrir las necesidades domésticas de financiación de las actividades agro-industriales que se llevarán a cabo en el propuesto programa, por un monto no menor al equivalente en pesos a cuatro millones cuatrocientos mil dólares. Estos créditos, que se suman al préstamo de la AID, para financiar bienes y servicios dentro de los márgenes de elegibilidad, estarán disponibles para financiar los costos en pesos de los equipos elegibles fabricados localmente, así como solventar los gastos de construcción y de compra de plantas industriales, la adquisición de materias primas, y la demanda de capital de giro para aquellas actividades colaterales para las cuales no hay disponibilidad de financiación a través

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de las vías ordinarias. Cualquier otra contribución en pesos que deba hacer el Gobierno del Uruguay destinada a llenar las necesidades del programa, será subsiguientemente determinada en forma conjunta por la AID y nuestra Oficina.

Atentamente,

Ing. Juan José Anichini
Director

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TRANSLATION

ANNEX E

Letter N° 205/75

Montevideo, June 6, 1975

Mr. Leonard J. Horwitz
Director
Agency for International Development
Montevideo, Uruguay

Dear Sir:

In our letter N° 114/75, dated 28 February, 1975 I had the pleasure of confirming on behalf of our Government, the request for financial assistance presented to the Agency for International Development (A.I.D.) of the Government of the United States of America, for the amount of $ 10 million dollars to support an agro-industrial development program principally directed toward the food-processing sector.

I am also pleased to confirm that the Government of Uruguay will provide the necessary internal credits to cover the domestic necessities of financing of the agro-industrial activities that will be carried out in the proposed program, for an amount of not less than the equivalent in pesos of $4.4 million dollars. These credits, to be added to the AID loan to finance goods and services within the eligibility margins, will be available to finance the costs in pesos of locally manufactured eligible equipment, as well as to settle the construction costs and purchase of industrial plants, the acquisition of raw materials and the demand for working capital for those collateral activities for which there is no financing available through the normal channels. Any other contribution in pesos to be made by the Government of Uruguay destined to fulfill the needs of the program, will be further agreed upon between A.I.D. and our Office.

Yours sincerely,

Ing. Juan José Anichini
Director
Office of Budget and Planning

ANNEX F

DRAFT ANNEX A - (PROJECT DESCRIPTION) - TO LOAN AGREEMENT

The Project

The goal of the project is to create an agri-industrial infrastructure capable of expanding non-traditional exports, thereby contributing to a diversification of agricultural production, increased foreign exchange earnings and increased production, employment and income opportunities for the target group.

As used in this project, agri-industry refers to all aspects of food production, processing, storage, distribution and marketing activities, and related activities directly supportive of these, such as those providing necessary agricultural and non-agricultural inputs, e.g., seeds, packaging materials, agricultural machinery and land development and management services critical to improved functioning of the target enterprises.

Purposes of the project are: (1) to provide a package of financial and technical services to private entrepreneurs and cooperatives for the establishment or expansion of agri-industries (food processing); (2) to help establish an effective delivery system for these services; and (3) to stimulate new production and marketing alternatives for small and medium farmers through the establishment of viable agri-industrial enterprises.

The project involves the establishment of an agri-industrial development fund within the Central Bank of Uruguay and the institutional development of a special mechanism within the Ministry of Industry and Energy - the Unidad Asesora - to evaluate project proposals and channel medium-term credit through the commercial banks to the private sector. The contribution of AID will be up to US$5.0 million and the contribution of the Government of Uruguay will be at least US$2.25 million in peso equivalent. The dollar resources of the Fund will provide foreign exchange for capital goods imports, essential raw material working capital requirements (e.g., tin plate for processing plants) and related technical assistance in support of new or existing export-oriented food processing industries and related service industries. The GOU counterpart funds will finance local costs for civil construction, purchase of existing plant facilities, locally-made capital goods, working capital requirements, feasibility studies and technical assistance. As part of its counterpart contribution, the Borrower will establish an industrial credit insurance fund or guaranty arrangement to be administered by the Central Bank to protect commercial banks against a portion of commercial financing risks involved in sub-borrowing, as a means of reducing existing excessive collateral requirements.

The ultimate intended beneficiary of the project is the small and medium farmer who is the principal producer of non-traditional export crops and who will be stimulated to new production and marketing activities by the establishment, expansion or modernization of agri-industrial enterprises. The initial and intermediary beneficiaries will be the private enterpreneurs and cooperatives who will invest in and operate these agri-industrial enterprises. The productive sectors of the economy as a whole will also benefit from the creation of an intermediate financing mechanism for channeling credit and technical assistance to viable development projects.

In order to be eligible for financing under this project, sub-projects must meet the following selection criteria:

1. Target Group - The sub-project must have a significant impact, in terms of increased employment, increased production or marketing opportunities, and/or increased income benefits, to small and medium farmers in Uruguay. The description of the target group will be refined in quantitative terms (i.e. income levels and number of hectares farmers) by the Unidad Asesora in the course of developing plans, standards and procedures for project review and appraisal, in accordance with Conditions Precedent to this loan. Potential sources of relevant data for determining quantitative definitions of the target group may be found in early result of (a) the May, 1975 Agricultural Census and (b) data to be developed on similar target groups under the IATA and CALFORU projects.

2. Characteristics of the enterprise - Priority consideration will be given to sub-projects which (a) utilize normal agricultural raw material which has been produced or has potential for increased production; (b) involve minimum packaging costs and complexity; (c) utilize uncomplicated technology; (d) maximize utilization of existing facilities; (e) complement existing facilities; (f) involve uncomplicated marketing; (g) operate effectively within existing limitations; and (h) complement the domestic market. In addition, enterprises financed under the project must not receive excessive protection, must exhibit good management, must be solvent according to normal commercial bank or Bank of the Republic standards, and must have an internal rate or return of at least 10%.

3. Export orientation - Sub-projects chosen for financing should be export-oriented in one of the following ways: (a) actual production is substantially export-oriented; (b) present production is only export-oriented to a minor degree, but prospects for increased exports are good; (c) interesting export prospects exist if equipment is modernized; and (d) new enterprises whose production will be principally export-oriented either at the outset or after filling an existing domestic demand.

4. Excluded enterprises - The following types of enterprises will be excluded from financing under the project: (a) meat or meat-packing facilities; (b) fisheries or fish processing activities; (c) textile manufacture; (d) shoe manufacture; (e) leather or leather products processing; (f) manufacture or marketing of alcoholic beverage; (g) wool processing or manufacture; (h) those which involve purchase of property owned by the GOU or any instrumentality thereof.

Up to US$350,000 of the AID loan may be utilized by the Borrower to provide technical assistance to sub-borrowers for conducting feasibility studies for prospective sub-projects and for assisting sub-borrowers in setting up new, or expanding and modernizing existing, agri-industries. Up to US$150,000 of the AID loan will be available for technical assistance to the implementing agency itself for the purpose of strengthening the advisory capacity of the implementing unit in agri-industry (food processing) project development. An expert in the food processing area will provide essential guidance and support to entrepreneurs with technical, marketing and managerial assistance in any or all phases of project identification and development including, e.g., working with potential project sponsors and assisting in preliminary evaluation of suggested investments; guiding project sponsors through the required steps of loan application-processing, guiding clients in preparation of feasibility study and market study terms of reference, etc., and assistance to project sponsors in the execution of projects through start-up periods.

IMPLEMENTATION SCHEDULE

The Loan will be authorized by June 30, 1975, and the Loan Agreement should be signed by August 31, 1975. All conditions precedent to disbursement must be met before December 31, 1975.

- Terminal date for meeting all conditions precedent to disbursement: December 31, 1975
- Terminal date for issuance of commitment documents: June 30, 1978
- Terminal date for loan disbursement: December 31, 1978

Disbursement Table

Source	1976	1977	1978	Total	Percentage
1. AID (Million US$)	.55	1.7	2.75	5.0	69%
2. GOU-pesos (Millions US$ equivalent)	.25	1.15	.85	2.25	31%
TOTAL (millions US$)	.8	2.85	3.6	7.25	100%

A N N E X G

Illustrative Lists of Projects

Exhibit I - Agri-Business Opportunities

Exhibit II - Notes of visitations and meetings

AGRI-BUSINESS OPPORTUNITIES

DESCRIPTION	Project Status				Investment			Investment Lead Time				Export LeadTime			COMMENTS
	Plan. Proposal	Pre-feasibility	Feasibility	Submitted to U.A.	Dollars (000)	Pesos Expressed in dollars (000)	Total Expressed in dollars (000)	To 1 Year	1-2 Years	2-3 Years	3-5 Years	1-2 Years	2-4 Years	5 Plus Years	
1. Cooperative located in Bella Union. Vegetable grading, packing and canning.	x				300	450	750		x				x		Potential for increased vegetable production in this area is good. Due to longer growing season off-season exports have possibilities. Will need marking assistance
2. Group from San Javier interested in processing vegetables	x				350	400	750		x				x		Not now a major vegetable area. Has potential in soil and climate. Initial markets will be cities nearby. some export possibilities to Argentina.
3. Company in Tacuarembo Vegetable grading and Packing.	x				400	400	800		x				x		Local markets available for table vegetables. Melons could be expanded for export.

AGRI-BUSINESS OPPORTUNITIES

DESCRIPTION	Project Status: Plan. Proposal	Project Status: Pre-feasibility	Project Status: Feasibility	Project Status: Submitted to U.A.	Investment: Dollars (000)	Investment: Pesos Expressed in dollars (000)	Investment: Total Expressed in dollars (000)	Investment Lead Time: To 1 Year	Investment Lead Time: 1-2 Years	Investment Lead Time: 2-3 Years	Investment Lead Time: 3-5 Years	Export Lead Time: 1-2 Years	Export Lead Time: 2-4 Years	Export Lead Time: 5 Plus Years	COMMENTS
4. Company in Salto Potato dehydrading plant.				x	570	286	856		x				x		Potatoes have relative short harvest season and inadequate cold storage. Plant could sell for local consumption during off-season. Export possibility to Brazil for dehydrated potatoes.
5. Sudy y Cia S.A. in Canelones - dehydrating vegetables, principally onions for export.				x	100	315	415		x				x		Located in major production area. Near export port of Montevideo. Now exporting to assured market. Project well researched
6. Company SAIM located in Montevideo - Vegetable oil extracting plant.				x	1000	1800	2800		x				x		Upgrading equipment for oil extraction - Soybeans, Peanuts and Sunflower.
7. National Citrus Commission - Montevideo.	x				400	500	900		x				x		To provide adequate citrus cold storage at the port of Montevideo. Cooperative operated.

AGRI-BUSINESS OPPORTUNITIES

DESCRIPTION	Project Status: Plan. Proposal	Project Status: Pre-feasibility	Project Status: Feasibility	Project Status: Submitted to U.A.	Investment: Dollars (000)	Investment: Pesos Expressed in dollars (000)	Investment: Total Expressed in dollars (000)	Investment Lead Time: To 1 Year	Investment Lead Time: 1-2 Years	Investment Lead Time: 2-3 Years	Investment Lead Time: 3-5 Years	Export Lead Time: 1-2 Years	Export Lead Time: 2-4 Years	Export Lead Time: 5 Plus Years	COMMENTS
8. Cooperative at San Ramon - Fruit and Vegetable processing		x			1750	1250	3000		x				x		Manufacture of tomato paste Apple pulp and grape juice.
9. Cooperative CALFORU Located in Canelones - canning plant	x				100	100	200		x				x		Now operates 2 cold storage facilities. Installing 2 packing lines and doubling present cold storage. Want to process 2nd grade and surplus production.
10. Company Ponny in Salto - Citrus processing.		x			200	100	300		x				x		Citrus juice extracting and canning equipment for export.
11. Cooperative located in Colonia Berreta, Fruit and Vegetable processing		x			300	200	500		x				x		Preparation and cooking line for fruits and vegetables.
12. Company ICUSA in Soriano, Fruit and vegetable canning.				x	1735	1540	3275		x				x		Preparation and cooking line for fruits and vegetables, including pulps and concentrates. Proposal includes auxuallary equipment such as cans which may not be feasible.

AGRI-BUSINESS OPPORTUNITIES

DESCRIPTION	Project Status: Plan. Proposal	Project Status: Pre-feasibility	Project Status: Feasibility	Project Status: Submitted to U.A.	Investment: Dollars (000)	Investment: Pesos Expressed in dollars (000)	Investment: Total Expressed in dollars (000)	Investment Lead Time: To 1 Year	Investment Lead Time: 1-2 Years	Investment Lead Time: 2-3 Years	Investment Lead Time: 3-5 Years	Export Lead Time: 1-2 Years	Export Lead Time: 2-4 Years	Export Lead Time: 5 Plus Years	COMMENTS
13. Company MASSARO in Canelones, fruit and vegetable processing.				x	700	1000	1700		x				x		Processing 2nd grade apples, Peaches, Quince, and Pears. Packing, Pulp and cold Storage 70,000 box capacity.
14. Company CALCAR in Carmelo, Dairy processing Cheese.		x			200	100	300		x				x		Has contract to export cheese to Brazil, Needs new eqqipment Used technical assistance from Brazil.
15. Company CAPROLET in Tarariras. Cheese plant.		x			320	100	420		x				x		Same as above.
16. Company Industrias Lacteas Fray Bentos in Fray Bentos. Cheese manufacture.		x			230	175	405		x				x		Same as above.
17. Company PILI located in Paysandu, Cheese plant				x	120	-	120		x				x		Process commercial grade milk into cheese and casein.

AGRI-BUSINESS OPPORTUNITIES

DESCRIPTION	Project Status				Investment			Investment Lead Time				Export Lead Time			COMMENTS
	Plan, Proposal	Pre-feasibility	Feasibility	Submitted to U.A.	Dollars (000)	Pesos Expressed in dollars (000)	Total Expressed in dollars (000)	To 1 Year	1-2 Years	2-3 Years	3-5 Years	1-2 Years	2-4 Years	5 Plus Years	
18. Cooperative CONAPROLE located in Florida. Dairy processing				x	1000	580	1580		x				x		Process excess production into powdered milk. Largest Co-op in Uruguay.
19. Cooperative located in Artigas. Process fresh milk and cheese.		x			225	275	500		x				x		Area needs quality fresh milk. Cheese exports to Brazil.
20. Cooperative located in Quebracho. Process fresh milk and cheese.		x			300	200	500		x				x		Same as above.
21. Community of Fray Bentos. Fresh milk and cheese.		x			300	200	500		x				x		Same as above.
22. Cooperative located in Tacaurembo, dairy processing.		x			300	200	500		x				x		Process some fresh milk for local consumption, but mostly cheese for Brazil.
23. Company COLEME in Melo. Dairy processing.		x			200	100	300		x				x		Old plant, now exports cheese to Brazil. Needs new equipment.

AGRI-BUSINESS OPPORTUNITIES

DESCRIPTION	Project Status: Plan, Proposal	Project Status: Pre-feasibility	Project Status: Feasibility	Project Status: Submitted to U.A.	Investment: Dollars (000)	Investment: Pesos Expressed in dollars (000)	Investment: Total Expressed in dollars (000)	Investment Lead Time: To 1 Year	Investment Lead Time: 1-2 Years	Investment Lead Time: 2-3 Years	Investment Lead Time: 3-5 Years	Export Lead Time: 1-2 Years	Export Lead Time: 2-4 Years	Export Lead Time: 5 Plus Years	COMMENTS
24. Private company ILSA Dairy processing.				x	515	1185	1700		x				x		Cheese and casein manufacture location to be determined.
25. Company CAMPICHUELO, S.A. in Salto. Box manufacture.				x	100	-	100		x				x		Manufacture wooden field and export boxes principally for citrus.
26. Company FUCCARO in Paysandu. Box manufacture	x				150	150	300		x				x		Same as above.
27. Company LOSTORTO in Montevideo, can fabricators.		x			100	100	200		x				x		Replacing obselete machinery.
28. Company located in Rio Negro. Livestock Feed.				x	500	700	1200		x				x		Alfalfa dehydration plant for poultry feeds. Local demand good.
29. Company LETAMENDIA in Paysandu, poultry processors.		x			400	600	1000		x				x		New enterprise to process eggs, specifically powdered eggs.

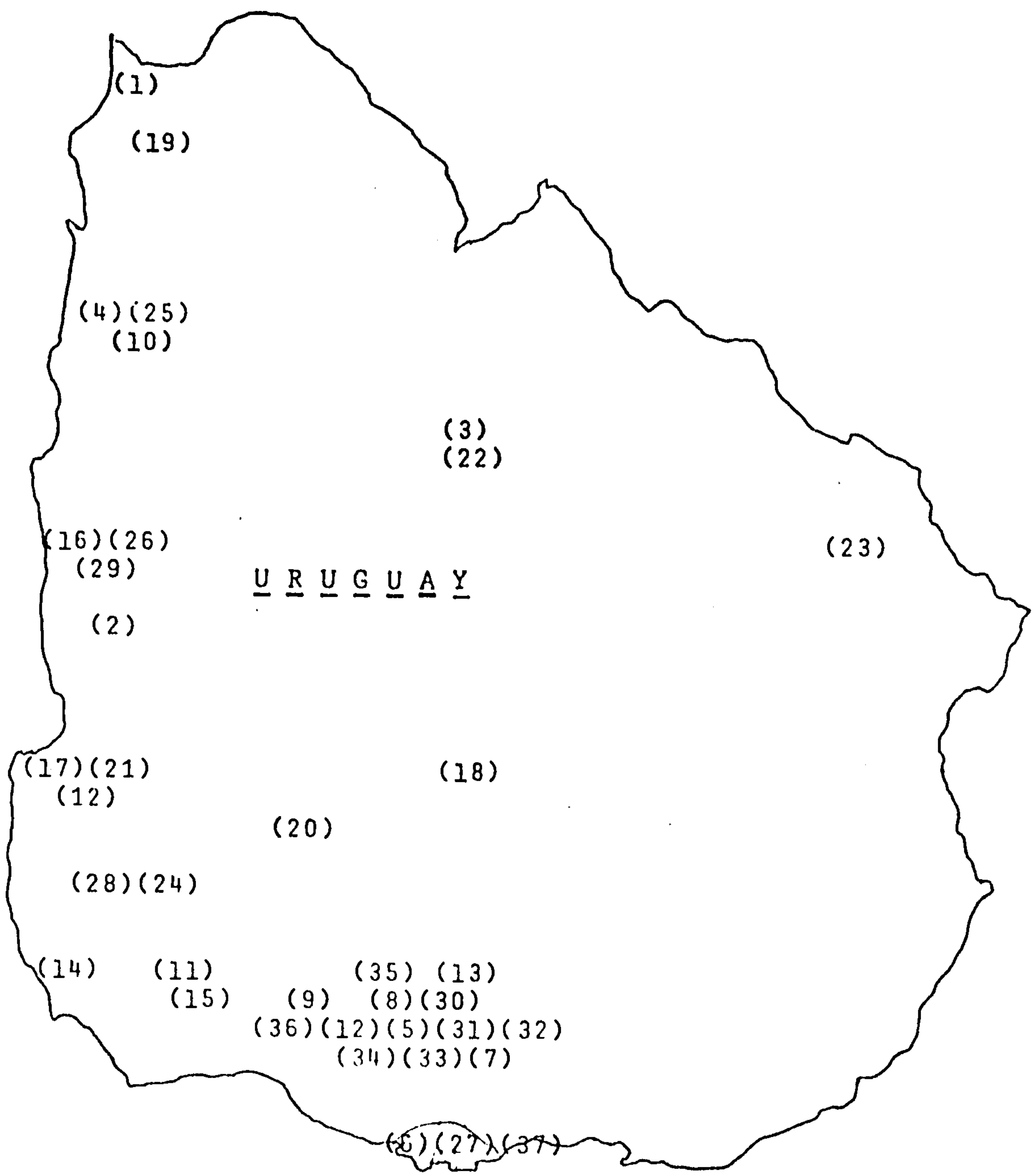
AGRI-BUSINESS OPPORTUNITIES

DESCRIPTION	Project Status: Plan. Proposal	Project Status: Pre-feasibility	Project Status: Feasibility	Project Status: Submitted to U.A.	Investment: Dollars (000)	Investment: Pesos Expressed in dollars (000)	Investment: Total Expressed in dollars (000)	Investment Lead Time: To 1 Year	Investment Lead Time: 1-2 Years	Investment Lead Time: 2-3 Years	Investment Lead Time: 3-5 Years	Export Lead Time: 1-2 Years	Export Lead Time: 2-4 Years	Export Lead Time: 5 Plus Years	COMMENTS
30. Company MOLINO PURITOS Dry Foodstuffs located in Montevideo.		x			25	25	25		x			x			New packaging machine for oatmeal and similar products for consumer packs.
31. Company SAUCE located in Canelones. Fruit and vegetable processors.		x			30	15	45	x				x			Pulp cooler and cooling tunnel to increase export capacity and quality.
32. Company SAUCE located in Canelones. Fruit and vegetable processors:		x			250	50	300		x				x		Replace obselete machinery to increase capacity and efficiency
33. Company Bennet and Brandon, fruit and vegetable processors		x			80	20	100		x				x		Same as above.
34. Cooperative CONEPROLE Dairy processors.	x				25		25	x					x		Marketing assistance to help develop "Dulce de Leche" as an export item for Brazil.

AGRI-BUSINESS OPPORTUNITIES

DESCRIPTION	Project Status: Plan. Proposal	Project Status: Pre-feasibility	Project Status: Feasibility	Project Status: Submitted to U.A.	Investment: Dollars (000)	Investment: Pesos Expressed in dollars (000)	Investment: Total Expressed in dollars (000)	Investment Lead Time: To 1 Year	Investment Lead Time: 1-2 Years	Investment Lead Time: 2-3 Years	Investment Lead Time: 3-5 Years	Export Lead Time: 1-2 Years	Export Lead Time: 2-4 Years	Export Lead Time: 5 Plus Years	COMMENTS
35. Cooperative CONEPROLE Dairy processors.	x				200		200	x					x		Technical Assistance to milk producers to increase volume and improve quality. A basic need.
36. Company RIO CLARO in Canelones. Fruit and vegetable processors.	x				25		25	x				x			Technical assistance for a new tomato and fruit concentrate installation. Has export markets.
37. The National Citrus Commission.	x				25		25	x					x		Technical assistance needed to determine if an existing citrus juice concentrate plant can be purchased and operated economically. Plant not now successful.
TOTALS FOR THE 37 ILLUSTRATIVE PROPOSALS					13,525	13,091	26,616								

GEOGRAPHIC LOCATION OF ILLUSTRATIVE AGRI-BUSINESS PROPOSALS



COMMENTS REGARDING DEMAND ANALYSIS

1. The saturation piont might be reached in certain catagories which would effect timing of implementing some of the proposed projects.

2. Priorities will have to be assigned by the Unidad Asesora and approvals granted on a very selective basis to minimize the possibility of duplication and to avied the construction of excess capacity. Also, it must be determined that the raw material input will be assured in adequate volume and quality.

3. Although no better information is presently available it appears the capital costs of some projects may have been over estimated by the propeser.

ANNEX G

EXHIBIT II

INDEX

NOTES OF VISITATIONS AND MEETINGS

No. 1

May 28, 1975

Meeting with Dr. Chester W. Hitz and Dr. Ronald Morse

The discussion with these two professors on loan here from Penn State University was entirely centered on the growing of fruits and vegetables.

Labor cost is low but is getting higher. Stoop labor is still available. There is a resistance on the part of growers to mechanization because of low labor cost and high fuel costs. The economic equation of hand-labor versus machines is quite different in this country.

Most tomatoes are grown in the area of Canelones. The growers, although poor, are receptive to change and to instruction. They do need financing. They can get seed and some fertilizers but not many can afford equipment. If the growers have an assured market they could improve their output and motivation no end. Tomatoes yield only about 7,000 kilos per hectare and cost is about double the USA cost per ton. The Roma variety has been successfully introduced and there is no reason why peeled tomatoes could not be produced in quantity. There are no irrigation systems; each farm provides its own irrigation from his own source, usually a well, and of course this is quite expensive. Irrigation is only applied as needed in the event of a long dry period.

The export routine demanded by the Government is restrictive and it is almost impossible to handle fresh vegetables under this system.

In order to establish smooth and continuous exports, for example from Uruguay to Brazil, on a regular basis it would be necessary to cut through this Government red tape.

They believe there is a good opportunity for dehydrated onions within the market in Europe. Good yields of onions are obtainable and with some technical help this could be a good project.

Fruits generally are grown in the south with the exception of citrus, which is primarily grown in the north-west corner of the country. Uruguay has a physical advantage over Argentina for export to Brazil. Argentine fruit production is located in the far west region near the Andes so their transportation distance to the Brazilian market is about double the distance from Uruguay.

Uruguay is already exporting fresh peaches and apples and the CALFORU loan will aid with washing, grading, waxing, pre-cooling and cold storage facilities. However, it is necessary to provide processing outlets for second quality fruit which does not lend itself to export. This second quality fruit could be used for fruit pulps, fruit nectars or diced for fruit cocktails. There is need to improve the productivity of existing fruit orchards and to accelerate new plantations.

They believe there is much scope for more production of any kind of agricultural produce. The sophistication level of the growers varies considerably. With respect to vegetables the fresh market growers are the most sophisticated whereas those that provide produce to the processors are at the lowest sophistication level.

The same applies to fruit growers but not to quite the same degree. Since fruit orchards vary in size from 10 acres to 700 acres, it is obvious that there are varying levels of sophistication.

There are no standards for fresh produce and this is a real need.

The three things needed to be done to improve agricultural output of fruit are:

1. Improve productivity per unit and lower unit costs.
2. Expand areas of production.
3. Improve quality standards and uniformity of production.

Government incentives are being investigated and a land-tax based on land usage and production is being considered. This should be done here and also credit should be given to orchard growers who invest in new orchards in as much as these investments have a 4 year dormant period. With respect to fresh fruits, Uruguay's main advantage is its location to the Brazilian market. The main disadvantage is the intense competition from Argentina. Our yields are lower and our costs are higher.

There should be a cohesive attack on exports in conjunction with the CALFORU loan. The CALFORU loan is providing the additional processing facilities needed and this loan could aid in providing some agricultural and marketing technical assistance. There is some question about the acceptance and efficacy of contracting for crops with growers. From past experience it appears that there is need for improvement of integrity at both ends of the contract.

Conclusion

There is much scope for increasing production and exports. Need processing outlets for second grade produce and streamlined export logistics. Need technical assistance at the "grass roots" level both in agriculture and marketing.

No. 2

May 29, 1975

Meeting with Mr. Jorge Saxel

Mr. Jaime Barceló and I met with Mr. Jorge Saxel, President of the National Plan for Citrus, which is under the Ministry of Agriculture and Fisheries.

Mr. Saxel described the areas of citrus growing being mostly in Salto and Paysandú with some minor acreage near Rivera. There are also some significant orchards near Montevideo growing lemons and Valencia oranges. Last year 833,000 cases (16,000 tons) of citrus were exported. This represents about 33% of the total crop of 50,000 tons. 90% of these exports originated from the Salto and Paysandú orchards. The major export market is Holland and some product is exported to France, Germany, England and Scandinavia.

They have received an IDB Loan of 3 million dollars plus local money equivalent to 2 million dollars and this totals 5 million dollar loan, which is being used to: (1) rehabilitate existing orchards and increase unit production; (2) establish new plantations to the extent of 1,000 hectares; (3) construct an additional packing plant in Salto in coordination with CALFORU.

He believes one of the primary needs of the citrus export industry is a cold store at the Montevideo port area. They are now using small stores in various places and this is inefficient, cumbersome and costly. The new store at the port area should be run by the citrus growers in some way and not the port authority or other organizations.

Three juice plants are in existance. One plant at Salto and one plant at Paysandú are merely juice extractors and their product is preserved by the addition of sulphur dioxide or sodium benzoate. All of the Paysandú product is exported mostly to France.

A third factory which exists in Salto is presently for sale. It is not associated with any growers and therefore has not been getting sufficient raw material and is not functioning successfully. This is a frozen concentrate plant. Saxel would like to have a feasibility study made regarding the possibility of purchasing this plant for a cooperative with the product to be exported. This could be a technical assistance project under this new Loan Agreement.

Another problem of the citrus industry is the lack of outlets for second quality fruit. There should be some solution to this problem such as marmelade processing, oil extraction, animal feed, etc.

> Note: The waste skins and fiber from the existing extracting plants are not being utilized. This material when dehydrated makes excellent animal food and could be an important supplemental food for dairy farms during winter months. An economic study might be revealing but Saxel believes present production is too low.

N° 3

May 29, 1975

Meeting with Ing. Alba of CALFORU

Mr. Jaime Barceló and I met with Ing. Alba who represents the CALFORU organization, a buying, packing and export service to fruit growers. They have already been meeting with processors to make arrangements for the disposal of non-perfect fruit. In general the growers are not happy with processors because of failure to keep promises. CALFORU is handling the cooperation, and in effect absorbing the shock, between growers and the processors. The concept is that one organization, CALFORU, will handle all matters pertaining to the producer, the producer's relationships with processors, and the export of the producer's fruit, which is presently oriented towards Brazil only. They claim to have all of the export expertise they need. The new plants are going to be located west and north-west of Montevideo.

With regard to expansion of field production they are still concerned with present production and believe much more fruit is available than has been marketed. An oversupply depresses profitability at the present time. The real need for the fruit industry is the packing and cold storage units which will be provided shortly.

Although Brazil is the main export target a second regional possibility is the Middle East. They do not plan to expand their activities to include vegetables. There are 10,000 vegetables growers in the area and he claims it would be too difficult a task to sort out the growers and determine which to include in the cooperatives. Mostly however, they are negative to this idea because they are unsure of their market. Although they are extremely sure of their ability to handle the export of fruits they would need marketing assistance to develop vegetable exports which he agrees would be a help to small and medium sized producers.

All of us met with a large group representing a fruit-growers association. They had conceived a rather grandiose project to establish new orchards on a large scale - up to 1,000 hectares - partially financed by a company known as INDUCOA located in Spain which would provide 2 million trees with financing over a 4 year period. There was much discussion on technical and political aspects of the project but it became evident that they had not really thought through the economic equations even on a rough preliminary basis. They felt they would need financing to the tune of 35 million dollars which would break down to about 70,000 dollars per hectare at the 500 hectare level and on the surface this is obviously far and above the economical limit for an agriculture venture. Although it is extremely doubtful if this project would be economically feasible based on the numbers stated, they agreed to work through their figures and advise us by Friday evening.

They did have some other ideas including a 500 hectare cooperative for the growing of tomatoes together with a processing plant. We provided them with data sheets and asked them to return these with the required information as soon as possible.

No. 4

May 23, 1975

Bennet and Brandon Food Processing Factory at Colón (Frigorífico)

The group making this visit comprise the following:

- Mr. Juan C. Crespi, AID
- Mr. Milton Torres, Frigorífico
- Miss Mónica Francois, Frigorífico
- Ing. José Madariaga, Ministry of Industry
- Miss Beatriz Levrero, Ministry of Industry
- Mr. Daniel Iglesias, Frigorífico

This is a small plant equipped in rather primitive fashion. The operation is limited only to simple canning. At the peak of the season about seven hundred people are employed making numerous products including: canned peaches, pears and apricots all packed in sweet syrup, various marmelades including stawberry, quince, pear and orange, canned vegetables including canned peas, corn, pimientos and peeled whole tomatoes. We did not attempt to list all of the products produced at this factory as the Frigorífico Company in total packs several hundred different items at its various factories.

The equipment is quite old and the processing depends largely on hand operations, even including hand labelling of individual cans.

It is evident that there is considerable scope for methods improvement and an investment in relatively inexpensive equipment such as preparation equipment and the more simple types of mechanical labellers could effect substantial economies.

Production is mostly for the local market but some packs are made for export. Fruit pulps packed in 5 kg. cans, 6 cans/wooden crate, are sold to Chile and Argentina.

The whole peeled tomatoes are packed from the Roma variety which has recently been introduced and is now established with the growers. With some slight quality improvements peeled tomatoes could be an important export item.

A large quantity of scrap production piled outside the factory was noted. There were many swollen cans due to bacterial action and the fault was attributed to be the quality of the cans themselves, some of which are imported from Argentina.

The company does not provide crop financing but sometimes does provide the seed. Farmers secure some financing through the Government bank. This processor pays his farmers within 30 to 90 days after receipt of the raw material. The factory's production is financed "anyway possible". They do receive some export credits from the Banco de la República. They claim to have good relations with growers and deal with both individuals and cooperatives.

With respect to expanded exports they believe they could export marmelades to England, but they need to improve their capacity and production facilities. They also believe they could export greater quantities of fruit pulps to Brazil but would need better preparation equipment and more processing equipment generally.

Although this factory is anything but modern the buildings are maintained in fair condition with reasonable sanitation.

In summary, export possibilities would be peeled tomatoes (a new item), marmelade to England (a new item), and increased volume of quince pulp and apple cubes.

An investment in the order of $50,000 to $100,000 would probably be required to increase capacity, efficiency and quality.

From an engineering survey made by a Mr. Basso and Engineer Myer, dated April 1975, the following points have been noted:

- the amount of raw material processed in 1974 was 1,846 tons comprised mostly of peaches, 654 tons; apples, 556 tons; corn, 226 tons; and pears, 219 tons. Only 48 tons of tomatoes were processed.

- This production resulted in exports to the extent of $219,000, the balance being sold in the domestic market. The raw material is supplied by approximately 100 growers.

- Water of top quality is obtained through the OSE system, but their reticulation system needs improvement and there is no system for the recuperation and recycling of water.

- The electrical and steam installations are adequate for the existing capacity of the plant. Cold storage facilities do not exist. Lavatories and toilets facilities for employees are inadequate. There is no laboratory and quality control is exercised from the central laboratory of the company at the other factory called "Sauce". There is a reasonable maintenance shop with good equipment

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Conclusion

With a modest investment of $50,000 to $100,000 this factory should be able to increase exports considerably. Would need tighter quality control and export marketing assistance.

No. 5

May 23, 1975

Sauce Factory (Frigorífico), located approximately 28 kilometers north of Montevideo

The same group that visited the Bennet and Brandon factory also visited this plant. Relative to Bennet and Brandon, this is a much larger plant and better equipped.

Here exists an adequate quality control laboratory supervised by a qualified food technologist which conducts all of the quality control tests for this plant as well as the Bennet & Brandon plant. Although better equipped than the other plant, including a rotary coil single effect evaporator, most of the operations from preparation through labelling and packing are accomplished by hand. There are numerous opportunities in all phases of the operation for efficiency improvements.

Nevertheless, a considerable export has already been achieved. A large quantity of apple and peach pulp packed in plastic bags of 40 kilos each has been packed for export to Brazil. The plastic bag in turn is placed inside an open top wooden crate. This is an expensive package as the wooden crate is non returnable and costs about 80 US cents. Next year, they plan to pack this product in 20 kilograms square cans. This will be hotfilled and self-sterilizing, eliminating the need for the current use of SO_2 as a preservative. The fruit pulp can then be used for reprocessing into a greater variety of products including baby foods and the product would have better market acceptance particularly in Europe.

This plant manufactures vinegar and processes pickled cucumbers, onions, carrots and cauliflour. Much of the pickled product is exported to Brazil in a rather interesting fashion. A large heavy plastic container resembling an oversize milk can with a capacity of approximately 60 gallons is imported from Brazil, filled with the pickled products and exported back to Brazil.

The rotary coil evaporator can concentrate tomato paste to 32% and they claim to have produced paste of export quality with low mold count. (However they do not check for insect fragment count and therefore it is not known whether the tomato paste would meet U.S. standards in this respect).

Some fruit pulps are packed in 5 kg. cans and stack cooled by the old fashioned method of merely spraying the stacked cans with cold water. There is no other cooling equipment.

They claim to have good relations with their raw materials suppliers and believe that the production of fruits and vegetables is adequate to meet their requirements. They could increase their exports but they need the following:

1) Export financing;
2) A pulp cooler costing $20,000 to $30,000 which would increase volume 50% and improve quality considerably;
3) A fourteen meter long cooling tunnel to cool square cans for the European export at a cost of $15,000.

From the engineering report previously referred to (in the Bennet & Brandon Memo), the following information has been noted:

- In 1974, the total raw material processed amounted to 4,782 tons, comprising principally quince, 1,733 tons; apples, 1,039 tons; peaches, 731 tons; and sweet corn, 262 tons. Only 230 tons of tomatoes were processed.

- Exports amounted to $1,075,000 and domestic sales were $809,000.

- With respect to services the water is obtained from an adjacent reservoir. The water is filtered and chloronated before being used in the plant. There are some defects in the system which should be corrected. The electrical installation is considered to be inadequate and substantial improvements should be made. Some improvements are required to be made to the steam generation plant. There is no effective treatment of boiler water and there are some other technical deficiencies that should be corrected.

- The buildings themselves are in good condition and amenities for employees are adequate.

- At the height of the season, this plant employs about 500 workers and they seem to have a good technical and supervisory staff.

Conclusion

Here is a facility already earning over $1,000,000 in export income despite a number of obvious inefficiencies. To correct these inefficiencies, improve capacity and provide the necessary services improvements would probably require an investment in the order of $200,000 to $300,000. Significant improvements can be made by the installation of inexpensive labor saving devises. A comprehensive plan to upgrade the facilities should be prepared and implemented. Increased exports should result. Export marketing assistance would help to accelerate sales.

N° 6

May 29, 1975

Río Claro Factory

Mr. Quesada, President of the Company, Mr. Leiferman, and Ing. Torriglia, a consulting specialist in meat and fruit processing, together with Mr. Jaime Barceló and I, visited the Río Claro plant which is located about an hour's drive along the south-east coast, near the town of Atlántida.

Last year this small factory processed 2,500 tons of tomatoes and they are planning a crop of 20,000 tons for the coming season. Whether they will expand their plantings to this extent will depend upon the Governments prompt action to approve the import of equipment which was ordered last year. These negotiations for import permits have been continuing since last September but still have not been finalized.

The seedlings must be planted by the end of June and available for transplant during the period August-September. The harvest period begins about the first week of January and continues through March. In the event of exceptionally good weather, the harvest can be extended through part of April.

They deal with 500 farmers who put about 2½ to 3 hectares each in tomato crop. Irrigation is primitive and used only if it is needed because of a long drought. They operate under a contract and seed is provided by the company. Yields have not been very good - at 15 tons per hectare - but they expect to build this rapidly to the 30 ton level. These farms are operated on a family basis and this is encouraged as is maximized the use of family resources.

They pay the equivalent of $ 80 dollars per metric ton for tomatoes, provide field supervision, provide seed and sometimes fertilizers, insecticides, etc. The growers obtain some credits from the Banco de la República. They admit their quality could be better and this is being worked on. Their farmers are reliable as the unreliable ones have been weeded out over the past few years. The company has a good reputation with growers particularly because they pay on time. Growers are not very well mechanized.

Duties are high for imported equipment, however, a farmer owning common equipment such as a tractor will rent it to others for the heavy work and many of the farmers will use animals for light field work.

Sales are made through wholesalers and up to now all of the output has been sold on a domestic market. However, with the new equipment, they plan to export 2,000 tons per year of 32% tomato paste. Their target markets are Carribean countries and northern South American countries particularly Venezuela. They are also considering the possibility of tomato paste for England.

The tonnage of tomatoes processed has increased dramatically in the last two years. In 1970 they produced 487 tons, 1971 - 258 tons, 1972 - 479 tons, 1973 - 2,451 tons, 1974 - 2,523 tons. The reason given for the big increase from 1972 to 1973 was that they decided to go ahead with greater vigour.

Fruit is handled in 22 Kg. boxes delivered to the factory by truck. The growers are scattered over a large area to a maximum radius of 25 miles.

They were very concerned with Government red tape and all kinds of approvals needed to get import permits for vital equipment. They claim the reason for the long delays can mostly be attributed to poorly qualified people in positions of responsibility and lack of decision because of fear of taking responsibility. They started negotiation in September last year for two lines of equipment to make tomato paste and fruit pulps and fruit products but have not yet received the necessary approvals.

90% of their past production has been Pulpa de Tomate which is a crude product containing seeds and skins of the tomatoes and which is packed in various sizes of glass bottles.

Last year they packed 200,000 cans of peeled whole tomatoes but they have experienced a very serious problem because of a failure of the can. They claim the can company, Companía de Envases, used the wrong lacquer for the internal coating with resulting failures amounting to a $50,000 dollar loss to the company.

The can company is unwilling to listen to their claim. Even more important, possibly, the health department of Food and Beverage Inspection in Montevideo blames the factory for this problem and they are threatening fines and confiscation of the product. No final action has yet been determined, but this is an interesting point and we would certainly like to know what the final outcome turns out to be. If the canner can prove the cause of the failure, and this is a relatively simple thing to determine, then any ethical can company would compensate the processor. If this is not the case in Uruguay, it leaves the processor without any recourse and he is accepting the full product risk and accepting full responsibility for any failures on the part of the can manufacturer. This risk is aggravated by the lack of testing machines at the can plants.

Pulpa de Tomate is a simple product. The pulp is heated to 90°C filled into pre-heated glass jars, capped, and sterilized at 85°C for 36 minutes on a conveyor pasteurizer. It is then stored until labelled. All labelling is done by hand.

Some very simple machines could increase the efficiency of this operation considerably. The $1\frac{1}{2}$ Kg. size is now packed 6 bottles into a very light paper case. Any degree of rough handling could result in excessive damage. They claim no problem thus far and they have been using this method of packing for the past two months. Other products are packed in returnable wooden trays or returnable wooden crates. They claim the use of corrugated cartons was out of the question with respect to both price and quality. Next year they plan to pack tomato paste in 10 pound round cans, 6 cases per wooden box. Alternatively, they may be able to import cardboard boxes from Argentina under bond for re-export.

The new processing line will handle 200 tons of tomatoes in 24 hours and contains a continuous double effect evaporator and all ancilliary equipment. The second line which has been purchased is a complete fruit-pulp concentrate and jam line which will be able to handle 50 tons of fruit per day. They believe this will help them to maximize plant utilization as some fruits, principally quince, are harvested after the tomato season ends. They have already made contacts with nearby orchards and expect to be able to utilize 2nd grade fruits from these orchards.

They obtain their employees from nearby farms and communities. They have experienced no labor problems and they repeated that they have a good reputation with both growers and employees. Their new building program starts next week in anticipation that they will ultimately receive the equipment now on order. A new boiler is under construction to replace the existing obsolete unit.

They stated their additional needs as being (1) a good resident technical supervisor, and (2) guidance in export marketing.

This company is taking a major step and is converting an extremely primitive operation to one which should be as modern as any in Uruguay. This is a courageous group. Since Ing. Torriglia is planning to visit the United States in the near future, I suggested he write to Mr. Raymond Good, President of the H.J. Heinz Company to seek permission to visit some Heinz plants in California. He was particularly interested in better methods of raw material handling, which I described to him, but which he could see in actual operation at those factories.

Summary

An outstanding example of what can be done to boost exports! Need technical and marketing help. This could be a real winner.

No. 7

May 30, 1975

CONAPROLE

Messrs. Barceló, Jones, Ricardo Inciarte and I, visited the CONAPROLE milk processing plant which is one of ten plants owned and operated by this cooperative. The company employs in total approximately 2,000 employees and there are 2,300 milk producers in the co-op.

This plant is all that a dairy plant should be with clean buildings, sparkling clean stainless steel equipment, and a variety of products being made including pasteurized milk, cream, butter, icecream and dulce de leche.

This latter item is a unique product to Uruguay and Argentina. It is not now exported but they believe it could be. The product contains 70% total solids, has a high sugar content, some fat, is tasty and nutritious. The product particularly appeals to children. The product as now made has about a 3 month shelf-life. After this time it is inclined to crystalize. They believe however, that this characteristic can be overcome by special processing methods. This could be a significant export item to Brazil, but would require a good marketing effort (could this be provided under the technical assistance part of our loan program).

Their major problem is one of volume and quality of supply. The quality of the milk received with respect to bacterial content is extremely poor. The plate count of incoming milk is around 13 to 16 million per c.c. but this is controlled, so they claim, to 50 thousand after pasteurization.

Here is a progressive company with significant organizational strengths and first class facilities. In addition to the existing plants they have purchased a new milk dehydrating plant to produce powdered milk with a capacity of 200,000 litres of raw milk per day. 80% of this product is targeted for export to South American countries. The investment will be $1.2 million which is financed from their own resources and the new plant should be in operation two years from now. The new plant will probably be located in the Florida area.

They believe in addition to the dry milk powder that significant export opportunities exist for cheese to Argentina, Mexico and Brazil, for butter oil (anhydrous butter) to Mexico, casein, etc.

Here is an outstanding opportunity to prepare for volume exports by correcting these serious supply problems. Building more factories or expanding facilities would be premature unless the quantity and quality of the milk can be considerably improved.

Idea - organize training centers to instruct the 2,300 producers in the basics of milk production, herd management, very elementary bacteriology, etc.

Another idea - would centralized mechanized milking stations each capable of handling say 200 cows, be a practical solution to eliminate the many small milk sheds which contribute to the high bacteria count? A pilot operation might be feasible and if successful could solve the quality problem by the use of modern techniques. This would be preferable to a difficult educational program for 2,300 producers.

No. 8

May 30, 1975

CONAPROLE - Cheese Factory at Villa Rodriguez

Messrs. Jones, Inciarte and I continued to Villa Rodriguez where we were met by Ing. García, manager of this cheese plant.

It is a very modern plant indeed and seems to have been designed as a show-place. It is equipped with modern stainless steel machinery from Finland, Sweden, Denmark, and some locally made. The factory has a capacity of 260,000 liters daily: 100,000 liters are for cheese, 80,000 for casein and the other 80,000 are shipped as whole milk to Montevideo for packing and distribution as pasteurized milk.

The plant operates at full capacity only four months of the year. If the weather is very favorable, they may get a five-month operation, but normally the capacity operations are during the months of September, October, November and December. The cheese plant operates only seven months of the year, from October through April. It was not operating the day we arrived but they were planning to have a run the following day.

Again the quantity and quality of the raw material was stated as being the limiting factor. All of the cheese is exported and without the milk supply limitation 5 more months of cheese production could take place annually, resulting at lease in a 70% increase in output. They are now manufacturing Sbrinz cheese which they claim is the only kind of cheese possible to be made from this high bacteria milk. With better quality milk, cheese production could be diversified into other types. For this cheese they presently receive a price of $1.60 dollars per kilogram CIF Buenos Aires (and I presume the same price is obtained for that which is exported to Brazil).

Note: The Government pays an incentive of 30% of the FOB price to the exporter. These incentives apply to all non-traditional exports and range from 4 % up to 35%. In this instance the Government incentive apparently is theirprofit because price and production costs are apparently about the same.

If the milk production curve could be lifted to a higher level and the low point of May, June and July flattened out somewhat, the export of dairy products could take a big leap forward. This is one of the best opportunities I have seen in Uruguay for a rapid development of exports. The traditional May, June, July, deficit is not expected this year because milk prices are higher as been prices have declined. The base amount that must be supplied to Montevideo is 500,000 liters a day. After this base supply has been met other products can be manufactured from the remaining milk. The small size of farms limits economic possibilities for improvements but nevertheless a very serious effort to improve herd management and pasture management would pay real dividend

Refer to the report by Dr. Zehren made in 1971.

Note: On the way to this cheese factory - a drive of 80 kilometers -

I had a good chance to look at the countryside. Shortly after leaving the environs of Montevideo, many orchards were in evidence stretching to the horizon on both sides of the road. These were interspersed with various vegetable crops and also numerous vineyards. At about 50 to 60 kilometers from the city of Montevideo the orchards disappeared and became mostly grazing land as we approached the cheese factory. The impression of this very small bit of geography was very favorable and it is evident that this should be a very productive agricultural region.

No. 9

May 28, 1975

Visit to Standard Brands - Mr. Bartó

Jaime Barceló and I met with Mr. Bartó and his production manager who showed us through their plant. This is a typical Standard Brands South American installation. The factory is cluttered as it grew like Topsy but it is in good shape with everything clean and in working order.

Bartó claimed that some sugar is still imported and all of his gelatine is imported. The yeast is produced locally with only a small amount of culture material being imported from the United States periodically.

He is satisfied with his packaging material and they use a large quantity of small paper cartons and plastic envelopes, etc. They sell through wholesalers and supermarkets. In the latter category there are 18 only. 60% of his sales are in Montevideo and they handle sales through distributors in the Interior. Not many export opportunities could be identified but Bartó thought that possibly they might export certain Royal products to Standard Brands in Brazil.

The factory is operating close to capacity now.

He is going to invest about 100,000 dollars in additional equipment. They already have a small amount of land for expansion. Most of the equipment will come from Argentina, Brazil and the U.S.A plus locally manufactured items. They are presently producing almost the full line of Royal products and Fleischman's yeast. They do not produce vinegar which is a fairly standard item with this company in other countries. Their products are all of usual Standard Brand's quality and have high acceptance in this market.

Conclusion

Not much scope for development of exports.

No. 10

May 29, 1975

Molino Puritas

Mr. Barceló and I, met with Mr. Luis Fabini and his three sons who own and operate this company. Their principal production is a line of grain products including avena, completo Puritas, harinas de arroz and others, polenta, copos de maíz, rice and fainá. Other products include some dry soups and dry refrescos.

Avena, packed in 450 gram consumer size utilizing paper and pliofilm packaging, has been exported to Brazil. Perú, Venezuela and Ecuador are on their export schedule for this year. There has been a shortage of oats and they are trying to improve the situation by giving technical assistance to selected oat growers to improve quality, quantity and price. They contract with the grower at a basic price and adjust at the time of delivery Because of a shortage of raw material no product was exported in 1974. However, this year they are planning exports in the order ot 100 to 150 tons per month. Other exports to Brazil are cleaned barley in 50 kilograms sacks, and cleaned rye grass. Last year 60 tons of these products were exported and they expect to reach 250 tons by the end of this year.

They have an excellent well equipped but small factory in "A-1" condition. They make all of their own packages and have a fully equipped printing plant. Each aspect of this little operation gives every indication of agressive and able management. They feel they are now in a good position to enhance exports particularly as two years ago they had to import oats from Argentina to supplement a low local supply. They now anticipate an adequate supply of raw material and also they have a favorable rate of exchange with respect to Argentina.

Their principal need is for one new pliofilm packaging machine costing about $25,000. With this machine they could improve both volume and quality and they believe they could build exports to about $45,000 per month (this seems to be an ambitious number but this is what they stated).

This is the kind of export that should be encouraged as it contains little if any imported components - no cans are used. The advantages are: supply of local raw materials, a price advantage compared with Argentina, a good quality product.

N° 11

May 30, 1975

Sudy & Company

Mr. Ed Lijewski and I, met this morning with Dr. Egon Sudy at breakfast to review with him his proposed project to build a plant to dehydrate vegetables particularly onions and carrots.

He has researched the project in depth in all aspects. He was able to answer instantly all penetrating questions with respect to product specification for various target export markets and technical questions regarding the growing and processing of the vegetables.

Since Dr. Sudy promised to give us a memorandum describing the project this note will be relatively brief.

With respect to market, he has already obtained a cooperation agreement with a firm in England for all production which is planned to be $ 500,000 in export value the first year comprising entirely dehydrated onions, with exports building up to a level of 2 to 5 million dollars annually.

They have researched the varieties of onions and feel reasonably certain they will get onions of the proper quality for dehydration - a high solids variety.

The drying tunnels they would install would not be the direct heat type so they would not encounter the problem of sulfur contamination or contamination by other products of combustion of the fuel.

They would pack the product in 2 plastic bags which in turn would be shipped in corrugated cartons.

They would utilize small farmers with 2 to 3 hectares each in onions and carrots. They would provide the seeds and agree on a contract with the farmer for a fixed price together with an incentive to share in the export profits. They plan to use about 230 farmers to provide the full acreage and they would contract for the full output.

The investment is estimated at $ 200,000.

This is an excellent example of entrepreneurship and new venture organization.

SUDY & CIA. S.A.

SUMMARY

A short, synthetic review of a project regarding dehydration of vegetables.

Sudy & Cia. S. A. is an Uruguayan, 15 years old manufacturing company. Its principal activity is in the field of manufacture, distribution and sale of synthetic detergents, having over 50% market share of these products. The company employs about 200 people and has an annual sales volume of about two million dollars worth of Uruguayan pesos.

About two years ago the company decided to diversify its scope of activity and after a long selecting process established that vegetables dehydration would fullfill the targeted main objectives, namely totally local raw material supply in the form of agricultural produce and the finished goods to be exported almost one hundred percent.

A years long market survey, carried out by the company with its own finantial and human resources, revealed a good and receptive market in the European Common Market area. A manufacturers agent has been designated, the same being an old established and specialized german-dutch firm. Contracts have been signed with substantial quantities of dehydrated onion and carrot as a starting point and purchases in accordance with manufacturing capabilities and volume of output, to be increased gradually in three subsequent steps.

Simultaneously the company carried out a pilot plant size operation, in order to train personnel and to design equipment to quality and production requirements. This stage has been completed, again without any outside technical or finantial assistance. On the agricultural side research has been done and is still on its way, to find the most suitable onion seed, with highest solid content, adequate taste and pungency and highest per acre yield. No previous experience was available in the country, so six different american and european seeds are being tested in field conditions (about 250 hectares) with the company's agricultural engineers and outside government and international expert's assistance. Transplanting seedlings method is used.

Seed is distributed to small farmers, in the Montevideo area within 100 km distance. Individual farmers participate in the programme with one to three hectareas. The contract assures the farmer that the entire crop will be purchaed at a base price, but after export, another premium will be paid to them in accordance with export profit. Such an incentive, which could increase the price received by the farmer to twice the base price, is designed to overcome initial resistance and fear of working with unknown seeds. Cooperative methods of making available to groups of farmers modern planting and harvesting equipment is part of the project.

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A set of figures are enclosed representing a resumé of an eight years proyection, three stage investment to increase plant capacity and the corresponding sales profit and loan amortization figures.

At present, the finantial resources for the plant equipment and buildings for stage one, are being sought and are not available so far.

SUDY & CIA. S.A.
FABRICA DE PRODUCTOS QUIMICOS

SOLICITUD PARA SER TENIDO EN CUENTA EN UN CREDITO EVENTUAL DE AID A LAS AGRO INDUSTRIAS.

DATOS DE LA EMPRESA

A. EMPRESA

SUDY & CIA. S. A.
Empresa existente
Fábrica de productos químicos
Planta : Av. Racine 3000 Carrasco, Oficinas : Buenos Aires 519 - 985240
Capital en proceso de autorización 500 millones
" suscrito 250 millones
" integrado 78 millones

B. REQUERIMIENTOS PREVISTOS

Razón para solicitar crédito :

Ampliación por nueva producción y diversificación.

Requerimiento de Financiación total : En tres etapas, ver planilla adjunta.

C. DATOS TECNICO ECONOMICOS PREVISTOS

Capacidad Propuesta del Proyecto: Valor medio anual US$ 4.386.000.=
Volúmen medio anual : 2.900 ton.
Empleados adicionales requeridos : 100

Ventas previstas - exportaciones : 100%

Principales mercados previstos : Mercado Común Europeo, existe contrato al respecto.

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	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	TOTAL
Dehydrated Vegetables Exports	290	1.100	2.710	3.110	3.510	3.710	3.710	3.710	3.710	3.710	29.270(1)
Natura. Vegetables Processed	2.200	8.100	19.200	21.000	23.700	25.100	25.100	25.100	25.100	25.100	199.700(1)
between	100	370	880	960	1.080	1.140	1.140	1.140	1.140	1.140	
Planted Hás.											
and	120	440	1.050	1.150	1.290	1.370	1.370	1.370	1.370	1.370	
Real FOB value (US$ 1.000)	433	1.648	4.061	4.660	5.259	5.559	5.559	5.559	5.559	5.559	43.856
F.O.B. VALUE DETAILS (thousands of dollars)											
General Cost	484	1.791	4.123	4.316	4.868	5.143	5.143	5.143	5.142	5.141	41.294
(2) Amortization Charge	9	34	68	77	86	91	91	78	40		574
(2) Financial Cost Charge	6	23	44	49	55	57	57	49	25		365
Net Profits	86	376	1.247	1.849	2.091	2.214	2.214	2.235	2.298	2.364	16.974
FOB Value Equivalent	585	2.224	5.482	6.291	7.100	7.505	7.505	7.505	7.505	7.505	59.207
INVESTMENT LOANS (FINANTIAL PLAN)											
Program I	85	95	84	70	56	39	21				
Program II		234	262	230	104	153	108	57			
Program III			255	286	251	211	167	118	62		
Subtotals of debts	85	329	601	586	501	403	296	175	62		
12% Interest	10	40	73	70	59	50	35	21	7		
Subtotals	95	369	674	656	560	453	331	196	69		
Less: Amortization											
Program I		23	24	23	23	23	23				
Program II			64	63	64	64	64	64			
Program III				69	70	70	69	70	69		
Balance	95	346	586	501	403	296	175	62	0		

(1) metric tons
(2) re: Investment loan

N° 12

May 23, 1975

Can-making Plant (Frigorífico)

The same group that visited the frigorífico food processing factories also visited a can-making plant which the company has recently purchased. This was a bankrupt company and the plant has not operated for the past five years. There are five lines comprising mostly Italian made equipment with some rebuilt American equipment interspersed. They expect three of the lines operating at full speed will produce a total of 500 cans per minute. One line producing a six pound can will operate at 100 cans per minute and the 5 gallon square can line will produce 5,000 cans in 8 hours. It is the output from this square can line that "Sauce" plan to use for packing fruit pulps next year.

It is important to note there are no automatic can testers. This means that a higher number of defective cans than normal can be anticipated.

There is a completely equipped lithographing plant and they plan to do all of their own tin plate lithography and lacquering.

They plan to use tin plate from Canada and the United States and use Dewey and Almy imported compound.

They claim to be overhauling each piece of equipment completely and some have already been completed. However, a coat of paint can cover many deficiencies and give the appearance of a good machine. It is a task of considerable magnitude to overhaul all this equipment and do a good job and I would anticipate many and possibly some serious startup difficulties. They will need to hire a team of good technicians and train operators. To minimize start-up problems and costly mistakes it might be advisable for him to hire on a project basis some good can making men from such countries as Mexico, Venezuela, etc.

N° 13

May 30, 1975

Lostorto Industrial y Comercial S.A.

Can Manufacturing Plant

Mr. Barceló and I, visited this plant and were shown through it by the General Manager, Mr. E. Mariani and later were met by the President, Mr. T. Lostorto.

The plant comprises six lines which makes the sanitary can sizes commonly used here and also makes cans for edible oils, biscuits and crackers and lubricants. All of the equipment is very old, slow and organized on a departamental layout in an old fashioned manner. Much handwork is involved, there are no testers. They make a large number of crown caps.

Production is at a low point now, as canning is practically ceased and soft drink and beer consumption has declined.

They use Canadian tinplate (which is a plus). It is a good plant, probably are reliable people, but quality will suffer resulting from equipment age and lack of testers.

They are now looking for good used or rebuilt equipment to replace their old worn out line. I suggested that they should contact the Goetz Machine Company in Australia as a possible source.

Note: There is a third can plant but since the two I visited do not have automatic can testers I presume the third would not have them either. This is a serious although not vital deficiency. During the course of the day on a high speed line an automatic can tester might remove 100 or so defective cans which never are delivered to the processor. These cans are defective in that either the side seam or the double seam has been improperly made or the tinplate contains a pin-hole. Since cans that should have been rejected will now be delivered to the processor who has no means of eliminating them, they will be filled with product with resulting spoilage. Not only this is costly but it is damaging to the reputation of the processor, the brand and the industry overall. Can testers are expensive and undoubtedly this is the reason they are not used.

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N° 14

May 28, 1975

Meeting with Mr. Einoder

Mr. Horwitz and Mr. Ed Lijewski met with Mr. Einoder and I at my hotel for lunch.

Mr. Einoder is an entrepreneural type who has developed a list of 16 possible agro-industrial projects. These are listed below:

1. Fruit and vegetable canning.
2. Dehydration of fruits and vegetables.
3. Tomato paste.
4. Pickles and sauces.
5. Growing of mushrooms.
6. Pork-sausage processing.
7. Organotherapic products (based on packing-plant by-products).
8. Demountable wooden boxes, for export of citrus.
9. Condensed milk and dulce de leche.
10. Cold storage and fruit packing.
11. Concentrated grape-juice (for liquor).
12. Soy bean (production development/oil factory).
13. Textile.
14. Cooked meat agcoop plant.
15. Tripe processing plant.
16. Vacuum packing.

Mr. Einoder agreed to send his engineer to see us to elaborate on certain of the more important projects.

N° 15

May 23, 1975

Visit to the Supermercado Tienda Inglesa

This is considered to be the largest and best supermarket in Uruguay. It is actually a small department store with only about 25% of the floor space devoted to a grocery section.

Since there was almost a complete absence of imported food products, the number of items available for sale was considerably less than might be expected. The presentation of the locally produced products varied from very poor to normal. Edible oils packed in glass bottles are a good example of poor packaging and presentation. The Royal products and Knorr Suiza products are examples of good packaging and presentation. It is evident there is much to be desired with regard to quality of packaging and attention to this important factor could pay dividends for the industry as a whole.

There was a rather impressive display of fresh fruits and vegetables with respect to variety and quality. Compared to fresh products the manufactured items seem to be disproportionally expensive.

N° 16

May 30, 1975

Mercado Modelo

Early this morning, with Delfín Pérez, the chauffeur, I visited the Mercado, to gain an impression of the variety and quality and general availability of fruits and vegetables. The market is in a large building enclosing an area of approximately 100,000 square feet - by rough estimate. The building is shabby, unpainted, rusting with numerous broken windows. Every form of conveyance was in evidence from horse-drawn two-wheel carts to large modern trucks. The drive-ways and parking areas were littered with garbage and manure and the floor of the building was littered with garbage and debris. There was much activity and the whole operation was typical of mercados in many other Central and South American countries.

A good variety of fruits, vegetables and grains was being handled. Of course, the quality varied considerably from fair to excellent. But the overall impression was as of an abundant and good quality raw material supply. Most impressive with respect to quality and size were tomatoes which varied from good to excellent. There were many carrots of very good quality but on the other hand some green peas in pods would be barely salable. Large quantities of apples were available of all qualities but some were well graded, individually wrapped and attractively packed. Citrus also appeared to be of good to excellent quality. The principal produce seen were: citrus, apples, sweet corn, squash, tomatoes, onions, coliflour, lettuce, leeks, carrots, garlic, potatoes, sweet peppers, green peas, parsnips, acelga, and some late season pears. There were also fresh eggs in crates, grains of all kinds in 50 kilo bags and sweet potatoes.

Outside the main building are a number of smaller shops. One that was visited was a wholesaler of cheeses and other dairy products. This shop, which should have been one of the most sanitary of places, was actually the dirtiest place I have seen anywhere. The cheeses were stored all over the place on various filthy shelves and even on boards on the floor. The cheeses were covered with flies and the whole effect was extremely unapetising so that it was very difficult to nibble on the sample of cheese that was offered to us. I had to admit, however, that the cheese did taste good, even though the surroundings were so repulsive.

The Department of Health and Sanitation would be well advised to get the entire Market and these kind of shops cleaned up.

No. 17

June 4, 1975

L. A. E. - Ing. Alfredo Dovat

Mr. Juan Crespi and I visited the LAE laboratories and were met by the Director, Ing. Alfredo Dovat. LAE has developed export standards for a wide rante of products and certificates of quality are issued to exporters by this laboratory. They also control the importation of special items or materials needed to fabricate export products.

The laboratories are very well equipped and are maintained in immaculate condition. There are laboratories for chemical and bacteriological examinations, as well as special purpose labs for the examination of fish, leather and dairy products. They seem to be well staffed and we were introduced to a number of the technicians and department heads.

At our request they had purchased a representative number of products of different brands at random from retail stores in Montevideo. These products were opened and examined organoliptically with the following results:

Canned Peaches in Syrup	- fair - peaches irregular in shape - trimming cuts - too brown in color - syrup was satisfactory.
Canned Crushed Corn	- poor product - most unappetizing appearance.
Canned Green Beans	- poor - earthy odor - whole beans, soft in texture.
Canned Green Peas	- poor product - many hard peas - the liquor was grey and turbid.
Tomato Ketchup	- 14 oz. bottle - with crown cap covered with a dust cap. Product was poor and brown in color - there was oxidized product in the neck of bottle - many specs and lumps - one hair.
Marmalade in 8 oz. jars	- the product was fair - but dark color and overcooked scorched flavor - the package is poor with dirty, partially rusted cap and oxidized product under the rim.

We were very disappointed with the quality of products being sold in the domestic market. LAE presently has no jurisdiction over the domestic market, but Ing. Dovat expects to be given this responsibility in the near future. The domestic market cannot be developed with products of this quality.

LAE is planning to expand their facilities and Ing. Dovat is making a trip to the U.S. within the next two or three months for the purpose of inspecting various laboratories there. I suggested that he should visit the Heinz Co. laboratories in Pittsburgh, Pennsylvania, and told him to whom he should write.

August 1, 1974

IBRD MEMORANDUM - INDUSTRY SECTOR

Current Trends and the Structure of Industry

The level of industrial output in 1972 and 1973 was 6-8% above the 1957 level, indicating an annual increase of less than 0.5% over the last 15 years. The stagnation of the country's industrial sector reflects the fact that while industrialization through import substitution reached its limits decades ago, economic policy has never been reoriented away from that objective. This has been the case despite the fact that there is strong world demand for many manufactured or semi-manufactured agricultural based products which Uruguay is capable of producing and that there is widespread recognition that fundamental changes are required in existing policies affecting industry.

Uruguayan industry is essentially devoted to the production of final consumer goods for the local market. Even among the branches of activity which are generally classified as producing "intermediate" or "capital" goods, a large share is consumer-oriented.1/ Exports probably account for no more than 5% of industrial output. These include wool tops (with very low value added), finished and semi-finished leather, some cement and ceramic items. Nevertheless, in appraising the structure of the sector, in particular the distortions which have resulted from the previous policies, it should be noted that Uruguay, because of its size and particular natural resource endowments, has not witnessed the creation of the larger, grossly inefficient basic or intermediate products industries which have characterized larger developing countries that have pursued such policies. Moreover, the durable

1/ For example in 1968 one half of value added in the chemical industries was accounted for by pharmaceutical and cosmetic preparations.

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INDEX OF VALUE ADDED IN MANUFACTURING BY PRINCIPAL SUB-SECTORS, 1958, 1961, 1965-72

(1961 = 100, based on data at 1961 prices)

	1958	1961	1965	1966	1967	1968	1969	1970	1971	1972
Food	104	100	116	114	106	120	131	137	122	121
Beverages	94	100	100	110	102	109	137	153	155	145
Tobacco	98	100	119	105	109	94	110	133	151	149
Textiles	120	100	113	126	105	111	124	92	74	96
Clothing & Shoes	127	100	128	137	133	145	129	114	108	95
Paper & Paper Products	108	100	148	142	141	141	153	173	198	189
Printing	112	100	102	89	89	102	111	93	107	107
Rubber Products	121	100	68	82	69	58	81	77	69	78
Chemical Products	96	100	94	110	121	103	113	123	135	125
Petroleum & Coal	90	100	118	108	106	106	114	114	117	118
Non-Metallic Minerals	116	100	98	103	101	127	142	156	165	157 a/
Metal Products	104	100	111	74	74	68	71	72	74	71
Electric Machinery & Apparatus	64	100	83	69	63	56	63	59	63	57
Other	90	100	95	76	103	108	93	118	116	115
Total	104	100	106	108	103	108	115	119	117	115 a/

Source: Office of Planning and Budget

a/ Mission estimate

consumer goods industries which have received high protection and whose economic viability is most subject to doubt, do not have large weight either in output or employment in the country.

: STRUCTURE OF INDUSTRIAL PRODUCTION

(in percent of total value added)

	1955	1960	1970
1. Traditional Industries	59.4	51.7	56.5
Food	23.3	19.1	22.5
Beverages	7.7	7.6	11.1
Tobacco	2.5	3.2	3.6
Textiles	15.7	12.7	10.3
Shoes and clothing	4.8	5.3	5.0
Wood and products	2.5	1.5	1.3
Furniture	1.4	1.2	1.2
Leather	1.5	1.1	1.5
2. Intermediate Industries	21.9	29.2	27.2
Paper	0.9	2.0	2.3
Printing	2.6	3.5	2.8
Rubber	1.0	3.5	1.7
Chemicals	5.3	6.1	6.6
Petroleum	5.1	4.8	4.7
Non-metallic minerals	5.5	8.0	7.8
Basic metals	1.5	1.3	1.3
3. Capital Goods	17.6	17.1	13.7
Metal products	4.2	3.4	1.7
Non-electrical machinery	3.6	4.0	2.5
Electric machinery	3.6	[illegible]	3.0
Transport equipment	6.2	5.3	6.5
4. Others	1.1	2.3	2.6
Total:	100.0	100.0	100.0

Source: Office of Planning and Budget

The period of most rapid industrial growth ended in 1957. As the sector experienced difficulties through the decade of the 1960's, an awareness began to emerge of the constraint on economic and industrial development which the import substitution strategy was imposing and that future growth was dependent upon opening the economy and adopting an export initiative ; for a country the size of Uruguay with expectations for rising income, the ratio of exports of goods and services to GNP of 10 percent would have to be raised. A number of measures were taken of limited scope and at various times, with minor impact.

In March 1972 a major revision in exchange rate policy was introduced, attempting to establish a more realistic relationship between the peso and other currencies. This was followed shortly by reintroduction and expansion of an export-incentive program involving tax rebates which had been initiated in 1964. This scheme provides for rebates (reintegros) on the value of exports of non-traditional manufactured products. The percentage returned to the exporter varies by item in accordance with the proportion of value added in production, the use of domestic raw materials or intermediate products and the net foreign exchange earnings. Except for a small number of specific products, the Government has committed itself to maintain the program for at least three years. From mid-1972 through 1973, exports of non-traditional manufactured products have shown considerable increase, particularly in value terms as a result of price increases in world markets. While there are no volume data presently available, a number of enterprises have reported substantial increases in unit sales abroad, in such varied categories as leather products, cement and ceramics, textiles, electronics and manufactured foodstuffs other than meat. This seems to indicate

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that export incentives and realistic exchange rates, coupled with improved overall fiscal and monetary management, could result in a substantial expansion of non-traditional exports.

The failure of industrial activity to grow has resulted in a further increase in unemployment which appears to be most serious in the Department of Montevideo. The decline in employment in that area was concentrated in those branches which supply consumer goods for the local market; the only group to experience any expansion includes leather products which is export-oriented. However, in the secondary urban areas, such as Paysandu, there may have been some offsetting increase in employment. While there are no official data for these areas, a number of factories producing leather and wool products for export reported some expansion in labor force.

EMPLOYMENT IN THE DEPARTMENT OF MONTEVIDEO, BY PRINCIPAL BRANCHES, 1969-1973
(in thousands)

	1969	1970	1971	1972	1973
Food, Beverages and Tobacco	26.4	26.0	26.0	25.6	25.7
Textiles	40.6	43.6	47.4	50.1	41.5
Wood, Cork, Paper, Furniture, Printing and Leather-products	17.5	19.2	18.5	16.2	20.1
Rubber, Chemicals, Petroleum Derivatives, Coal, Ceramics and Glass	28.0	28.9	33.7	28.1	25.9
Metal and Metal Mechanical Products (including Castings, Electric and Non-Electric Machinery and Automobiles)	32.3	37.5	34.4	35.7	30.9
Total	144.8	155.2	160.0	155.7	144.1

Source: Office of Planning and Budget

Prospects for Future Growth

While wool production has been a traditional activity with major importance in the total exports of Uruguay, its impact on the industrial sector has been limited as most of the trade has taken place in wool with little local processing. World market conditions for this product have varied sharply in the last 15 years but the potential for increasing the local value added through the export of wool products is basically independent of those trends, originating in the tendency of the developed countries, which are the principal consumers, to shift from producing to importing items with relatively large labor inputs, such as textiles and clothing.

In 1973, Uruguayan exports of woollen yarn and textiles amounted to some US$4.5 million as compared to US$1.5 million in 1972; more than half of the increase appears to be the result of price increases. For 1974, these exports are expected to rise to about US$8 million, the markets including the United States and South Africa; for the year, little change in prices is expected. Most of this output comes from a few large enterprises which have been able to modernize a considerable proportion of their equipment. In general, the firms producing these items have obsolete machinery and substantial modernization, as well as rationalization, would be required for an expanded export effort. One area which could experience particular growth is trade in woollen-synthetic mixtures for which existing capacity is rather limited.

Exports of woollen clothing remain relatively modest, almost US$400,000 in 1973; but this is expected to rise to almost US$2 million in 1974, largely from one firm which is concentrating on external marketing. There has been considerable buying interest from the US, Canada, Australia and even Japan for these products, particularly for men, and the mass retail establishments in those countries indicate that a growing proportion of their requirements for inexpensive ready-made clothing will be imported. While the extremely high labor content of such products might tend to favor buying from the countries of the Far East with low wage levels, Uruguayan advantage in having its own supply of woollen cloth appears to be offsetting this factor, at least partially.

Even more significant under existing conditions is the possibility for expanding leather products exports including clothing and accessories such as belts and ladies' handbags. In 1973, these exports amounted to slightly under US$5 million as compared to US$2 million in 1972; price increases appear to have accounted for less than half of the increment with the volume apparently almost doubling. Exports in 1974 are expected to reach US$8-10 million as a result of both volume and price increases. Employment requirements vary among the individual products but a representative leather clothing firm producing US$1 million in exports would employ 200 persons and would require US$100-150 thousand in equipment (all values in 1973 prices). Uruguayan exports of these items are a very small share of world trade; for example, U.S. imports of leather clothing, handbags and accessories in 1973 exceeded US$250 million and the only significant import from Uruguay was US$3 million in men's clothing.

Shoe exports represent another excellent prospect but in this case the equipment requirements are relatively large and there is need for improving existing technological and marketing know-how. Expansion of this trade is, therefore, expected to take a few years to develop. There have been reports that Brazilian shoe firms are showing interest in establishing various forms of joint ventures for developing exports with Uruguayan enterprises. In addition, a West German firm which has been importing Uruguayan leather for producing shoes is reported to be considering a joint venture to manufacture shoes in Uruguay. This move would be in response to the export incentive policy for leather; under the measures established in mid-1972, the rebate for tanned leather exports will be reduced to zero at the end of June 1974 to encourage exports of further elaborated products which will retain high rebate percentages.

Processed foods also offer considerable export possibilities. The country has a capacity to produce excellent quality temperate zone fruits (e.g. peaches) and vegetables (e.g. tomatoes) which it currently exports in fresh form, mainly to Brazil. Some processing for export is undertaken but a major effort for modernizing and expanding equipment, particularly for the production of pulp, as well as for creating the necessary organization for assuring raw product supplies, is required. One area in which this is already underway is citrus fruits where an IDB loan is providing assistance in mounting an integrated growing and processing program.

Another food category where possibilities exist is fish and shellfish products. In spite of Uruguay's location with a relatively large coastal area, this industry has had minimum development. With high world demand for these items, interest is being shown by importing countries in establishing joint ventures for expanding the fishing fleet and constructing processing facilities, particularly for freezing. A number of specific proposals have been awaiting official approval for a considerable period of time involving investors from Argentina, Brazil, and the United States.

FAO is now engaged in a major oceanographic survey to determine the characteristics of the fish resources in nearby waters as the basis for a more comprehensive development program for this subsector. This study will identify investment requirements both direct for vessels and processing facilities and indirect for port and handling equipment.

Non-metallic minerals present another group of resources which the country contains in relatively abundant quantities. Since 1964 a fairly substantial trade in cement has developed, first with Brazil and more recently, as capacity was expanded, with other nearby countries. This trade is now threatened by the fuel crisis as the wet-process used in cement manufacture requires considerable oil use which will raise cement prices substantially; nevertheless, there are large net foreign exchange earnings in cement exports and whatever measures are taken to reduce petroleum imports should be designed to avoid interfering with production for exports from existing capacity. However, a proposal to expand these installations further needs to be re-evaluated in the light of radically changing price relationships for fuel, cement and equipment required. Within this same sub-sector, tiles, ceramics and glassware are being exported to neighboring countries but there also appear to be possibilities for trade outside the region, particularly for the first item; this would require some modernization of equipment to achieve output of exportable quality. Finally, excellent deposits of marble and black granite are the basis of a modest export activity at the present time. While fuller exploration to determine more precisely the characteristics of the available resources is required before any substantial investment is undertaken, there appears to be the basis for a relatively major export project which could be implemented relatively rapidly.

Although best export opportunities lie with the resource based items, some trade in more advanced manufactures is possible within special bilateral accords and LAFTA concessions. Modest in orders of magnitude, the items concerned nevertheless offer important employment outlets for a country the size of Uruguay. Among the products already being traded are electronic

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equipment and synthetic textile yarns. On the other hand, an interchange of automobile parts within a complementation agreement with Argentina is taking place under such highly protected conditions that the real resource cost to Uruguay appears excessive.

Principal Industrial Policy Issues

The basic elements of an industrial policy for Uruguay would include maintenance of a realistic exchange rate, adoption of measures to channel private savings toward productive investment, reduction of excessive protection, elimination of bureaucratic obstacles to normal business transactions and rationalization of export incentives. The objective would be to use the price system to eliminate current disincentives and to structure appropriate incentives to encourage a better allocation of resources and improve industrial efficiency, both oriented toward raising exports.

In recent years the most important single step which the Government has taken relates to exchange rate policy, the mini-devaluations designed to maintain a realistic parity of the peso with other currencies. As a result of this policy and the system of rebates for exports of manufactured goods, some progress has been achieved in finding markets for the country's non-traditional exports which embrace a wide range of products based on agricultural and non-metallic mineral resources. With continuation of the relevant measures, export of these products could continue to show moderate growth. The main constraint on this expansion seems to lie on the supply side, set by tax and price policies which hinder rationalization and investment in modern equipment. Thus, to take fuller advantage of the opportunities which exist, measures are urgently needed to capture financial resources for long-term investment in industry. At present, enterprises are almost completely dependent upon their own resources to finance local costs for modernization and/or expansion, while Central Bank regulations require that virtually all imported capital equipment must be financed through suppliers' credits. General world market conditions for sales of capital goods, as well as the past repayment experience of Uruguay, have made external creditors wary of providing new loans.

With high and variable rates of inflation, and infrequently adjusted nominal interest rates, real interest rates have varied widely and, over the past two years have been strongly negative. Under these circumstances interest rates do not function to allocate investment according to economic efficiency. Furthermore, negative interest rates discourage holding of savings in financial assets and lead to shortages of credit through the banking system and to scarcity of long-term loan capital. A system of indexing financial transactions to attract funds and to channel these resources to productive investment should, therefore, be adopted. The Government plans to establish a mechanism for indexing some of its obligations. This would tend to channel financial resources to the public sector, possibly at the expense of the already credit-starved industrial sector. In view of the more than a decade of practically zero net investment in industry, it is essential that the funds flow to that sector and to those branches where the economic returns are now so promising. One means to achieve this would be through the establishment of a Development Bank which could apply monetary corrections to both its lending and borrowing. While the Government in principle has committed itself to take this step in the statement of norms to guide its policy actions which was issued last year, it has recently announced its intention to wait a period of two years and to reorganize the Banco de la Republica (BROU) to set up a

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special development division. Aside from the fact that BROU has not, in the past, shown capacity for acting as a development institution, this measure completely ignores the problem of obtaining financial resources.

To ensure that proper use is made of available capital, it is essential that the present tariff and import control systems which provide excessive protection to domestic industry be modified. The tariff actually has two elements: (1) standard rates fixed by law which are relatively modest, and (2) surcharges ("recargos") which are flexible and can vary from 0 to 300 percent in nominal terms. In the past, the overvalued exchange rate tended to reduce the level of effective protection provided by tariffs so that unless these are lowered, the present policy for a more realistic exchange rate can lead to an increase in effective protection. The existing import quota system, of course, provides absolute protection by prohibiting whole range of imports, especially consumer goods.

A more rational system would provide for lowering tariff rates and gradual freeing of imports. Where it is felt necessary to reduce consumption of luxury goods which are normally imported, this can best be achieved through imposing excise taxes which avoid the undesirable effects on resource allocation characteristic of tariffs and controls. While there is concern that reducing protection will lead to the closing down of industries which have benefitted from past policies and to a consequent growth in unemployment, the growth of the export industries which would be encouraged by these measures could be expected to provide alternative job opportunities. The two most inefficient and most highly protected industrial branches, the assembly of automobiles and electric household appliances, employ approximately 5,000 persons, some of whom could be retained as not all of the operations would be abandoned.

From the point of view of employment, the most interesting export possibilities are woollen and leather products. Moreover, both have very low capital requirements and can be expanded relatively rapidly. Production of these items is undertaken by a number of small and medium-sized firms, precisely the type which generally benefits most from financial assistance from official development institutions.

Another element which would favor the growth of these enterprises oriented toward exports is the reduction of the bureaucratic processes which surround all elements of doing business in Uruguay. The management of such firms simply cannot afford the time entailed in meeting current administrative regulations, particularly for exports. In this connection, one example of the difficulties in obtaining administrative reform under current conditions is the delay in revising export documentation requirements. At present, six separate documents are necessary for exporting: in 1973 an inter-ministerial group with the help of a UNDP technical assistance expert revised these procedures and drafted a single document to meet the official needs of the various agencies. This document was to go into use on January 1, 1974 but final approval by one participating institution has not yet been forthcoming and this simple reform remains sidetracked.

August 1, 1974

THE DEVELOPMENT OF MAJOR INDUSTRIAL BRANCHES

1. This Annex provides a description of the major industrial branches, concentrating on their structure and the past policy mix which has served to determine in great part recent events. The principal features of a new policy approach to provide the basis for future expansion are discussed in the text of this Economic Memorandum.

A. Wool Industry

Main Trends in Recent Periods

2. While wool production has been a traditional activity with major importance in the total exports of Uruguay, its impact on the industrial sector has been limited, as most of the trade has taken place in wool with little local processing. The world wool market has experienced sharp fluctuations since the middle of the 1960s which have had important effects on the Uruguayan industry. Present uncertainties in the world wool market pose obstacles to the definition of a development policy designed to increase the importance of the subsector in manufacturing.

3. The decline in the world wool prices which took place in the period 1969-1971 coincided with an increase in demand for beef and Uruguayan sheep producers shifted to raising cattle.1/ After remaining relatively constant since the mid-1950s at about 22-23 million head, the country's sheep population began to fade and by the end of the 1971/72 season it was estimated at 18 million head. During that season, wool production was estimated to be only about 65% to 70% of the average for the previous decade.

4. Prices of wool in world markets began to rise during 1972 and, accompanied by a more realistic price and exchange rate policy adopted by the Uruguayan authorities, this served to renew interest in wool production. While the country's wool clip for the 1972/73 season rose 10%, it was still below earlier levels due to the reduced animal population. However, there was a sharp reduction in sheep slaughtering as producers attempted to rebuild depleted herds. Thus, registered slaughterhouses recorded processing 776,000 sheep in 1971 but only 192,000 in 1972; the 1973 figure may have been even less. Despite the fact that the local wool clip for 1973/74 is expected again to rise about 10% over the previous year, it would still be below the average for the 1960s.

5. As already noted, Uruguayan wool is exported with very little local processing. For many years, the bulk of this trade was in greasy wool, direct

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1/ This tendency has also been noted in other major wool producing countries. See Commonwealth Secretariat, Woollen Textiles, May 1973, Vol. XXVI, No. 5, p. 344.

from clipping, but there has been a tendency to increase the share of wool tops, a crude wool which has undergone scouring and combing or carding. Production of wool tops has thus become an important industrial branch, accounting for about 10% of value added in the entire textile subsector and providing considerable employment.

Table 1: Distribution by Value of Crude Wool Exports
(in percent of total)

	1961	1965	1968	1970	1972	1973
Greasy Wool	66.1	67.3	59.1	55.7	49.1	37.4
Washed Wool	10.8	8.5	6.9	7.9	9.1	21.0
Tops	23.1	24.2	34.0	36.4	41.8	41.6
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: Trade Statistics of the Banco de la Republica

6. Only a small share of the total wool supply is used for yarn and fabric production. Estimates prepared by the Planning and Budget Office (OPP) for 1971 indicate that slightly more than 10% of the clip volume enters into advanced manufacturing, predominantly for the local market. Nevertheless, in recent years there has been relatively large growth in exports of these products and also of woollen clothing.

Situation at the Beginning of 1974

7. The reduced supply of crude wool resulting from the reduction in the sheep population has caused a number of problems within Uruguayan industry. At the beginning of 1972/73 clipping season (October 1972), world market prices had been rising and there was accelerated buying of greasy wool for export from the country in expectation of the reduced clip. In these circumstances, it appeared possible that the local tops industry would not be assured adequate supplies to maintain its production both for exports and for the local market requirements for yarn and fabric output. The Government, therefore, prohibited new export registrations of unprocessed wool mid-way through the season, until the beginning of the new season (October 1973).

8. The 1973/74 clip was initiated under considerable uncertainty. World market prices had declined from the exceptional highs reached in the

middle of 1973 but were still well above the average for the previous season. Buying interest for export continued very high for greasy wool and registrations of export commitments by mid-December amounted to 16.8 million kilos, or about 25% of the expected clip. Considerable interest was reported from new customers, including East European countries, with the traditional buyers (Western Europe and, recently, Japan) showing caution as a result of the sharp change in expectations in those countries following upon the petroleum crisis. In early 1974, the Government acted once more to restrict new commitments for greasy wool exports believing that this was necessary to ensure tops producers of their raw wool supplies. This move was taken precisely at a point when no clear trend was emerging in world wool markets. Japan had increased its exports of tops and there was little interest among major importing countries in additional purchases. Moreover, greasy wool prices had turned downward from the peaks reached in the last half of 1973, but they were only slightly below the average for that year. Thus, Uruguayan wool producers were having difficulties in disposing of their wool and were accumulating large stocks. The Government subsequently rescinded the ban on greasy wool exports.

Long-Term Prospects

9. Developments in the major importing markets of the developed countries during the last two years have suggested a resumption in the growth of demand for wool and its products. While there was some uncertainty about price trends at the beginning of 1974, world demand is expected to remain relatively buoyant. The forecast for average 1974 price is below that of the previous year but much higher than that prevailing in 1972.

10. The present petroleum crisis is characterized by a number of factors which can operate either to support or diminish future demand growth for wool and only time will tell which will predominate. On the one hand, the crisis is expected, at the least, to slow down income growth in the industrialized countries and consequently to reduce consumer demand. On the other hand, rising prices for petroleum will clearly affect the prices for such petrochemicals as the synthetic fibers, thus improving wool's competitive position; moreover, with fuel shortages, there may be preference for woollen garments which are considered to offer more warmth. With this uncertainty, framing a development strategy for the industry in Uruguay is obviously difficult. Nevertheless, even within the existing situation, there appears to be scope for expanding the degree of elaboration of wool exports and consequently increasing the value added and employment in the Uruguayan economy.

11. Among the five major crude wool exporters,[1/] Uruguay has made the most progress in increasing the importance of tops in its trade. The principal exporters of tops, in fact, are the traditional importing and processing countries of Western Europe (and recently Japan) which have long established production relationships within the trade. While such patterns are difficult and slow to change, internal developments in those countries themselves may speed up the process.

1/ The others are Argentina, Australia, New Zealand and South Africa.

12. The situation with regard to yarns and fabrics is much clearer, however. In these cases there exists a substantial world trade in which Uruguay has hardly participated. Moreover, there is a growing tendency for importing woollen garmets by a number of high-wage industrialized countries because of the heavy labor inputs in the production of these items. In the opinion of numerous trade sources in the developed countries, regardless of the trends in overall demand, an increasing proportion of these kinds of finished consumer goods will be purchased in developing countries.

13. Uruguay has had a small, relatively well-developed yarn and fabric industry and has exported in the past good quality products in limited quantities, amounting to about 10% to 15% of production. The output of these products and in particular exports is dominated by four or five large enterprises, two of particular importance, which are integrated producers, starting with the production of tops and then moving into the more advanced products.

14. A study by the Uruguayan Productivity Center (CPU) in early 1971 indicated considerable obsolescence in existing loom capacity, some 60% of the equipment not being considered appropriate for export production. In the case of yarn machinery, the study recommended replacement of 25%; also 10% to 15% would have to be upgraded for use in producing exportable quality products, through improvements or modifications. Total costs for the modernization program recommended by the CPU (which also included some improvements in the wool scouring facilities) were estimated at US$12-14 million. Requirements for the expansion of production facilities were considered minimal, since the industry was estimated to be operating well below capacity, from 50% in the case of fabrics to 60% in the case of yarns. However, the investment program recommended for the industry at that time was largely based on the relatively depressed conditions of world demand in 1971 and will need to be revised in the light of the current situation.

15. Obsolescence of equipment is particularly important for the smaller firms which apparently accounted for a major portion of the underutilized capacity found by the CPU study. Few of these establishments are currently exporting, not being in a position to produce items of quality for sale in the major importing countries. In order to attempt to penetrate external markets, these enterprises would require not only modernization but considerable rationalization of production as well.

16. Other structural deficiencies were also noted in the CPU report. Given the orientation of the industry towards a small local market, the study found a lack of specialization among producers, other than the few enterprises producing only tops for export. Particular emphasis was also given to the question of the adequacy of working capital where the seasonal pattern of supply creates special problems. Thus it was recommended that steps be taken to provide credit facilities which would permit the local industry better access to the wool clip in competition with foreign buyers. Finally, attention

was drawn to the lack of modern marketing know-how and the need to carry out external programs for market development and distribution.

17. A number of measures have been taken by the Government in recent years to assist the development of the industry. In addition to a special tax rebate (re-integro) of 22% which all wool exports other than greasy or washed wool receive, individual products receive a specified proportion related to value added. For example, in the case of woollen fabrics this ratio is 28%, making a total rebate of 50% for the item. Other measures have included special short-term credit lines to local manufacturers for the purchase of raw wool.

18. These specific measures, as well as the general policies to promote exports have served to stimulate modernization programs within the industry. This is particularly true among the larger integrated firms which reported substantial export contracts with production booked through mid-1974. Some expansion is also being implemented, although many producers remain cautious in view of uncertainty over future world demand trends and especially over the ability of the Government to carry out the total revision of general policies which it has promised and which would provide sufficient incentives.

19. A major obstacle to expansion is the shortage of long-term credit and equity capital. For example, the modernization and expansion projects now proposed are to be essentially financed by relatively short-term suppliers' credits and even these are extremely difficult to obtain at this time. For the future, governmental policies designed to improve the flow of long-term capital (for example, the creation of a Development Bank) and to better meet the seasonal pattern of demand for short-term capital are required to supplement the general measures favoring more rational allocation of resources which are already in operation. In addition, external marketing and distribution programs recommended in the CPU study need to be implemented and such cooperative programs within the private sector should be encouraged and promoted by the Government.

20. The growth of an export-oriented woollen garment industry is of particular interest in view of the high level of un- and underemployment and the labor-intensive nature of this operation, with consequent possibilities for expansion of employment opportunities. There has been interest shown in importing Uruguayan clothing by buyers from the United States, Canada, Japan and Australia, and a small amount of export trade has been recorded. This has, however, largely been the response of one Uruguayan firm which has shown willingness to adapt design and production techniques to requirements of those markets. To encourage further expansion of this trade, including stimulating other firms to take advantage of these export opportunities, there is a particular need to reduce bureaucratic procedures affecting enterprises, particularly those which are related to the process of exporting. As most of these firms are small, this administrative burden is a major obstacle to expansion of activity.

B. Leather Industries

Manufacture of Leather

21. One of the few dynamic elements in the Uruguayan economy in the last decade, the leather industry has undergone important structural changes during this period tending to increase the degree of processing within the country. Nevertheless, there remains considerable scope for further development of this branch of activity which would provide both higher foreign exchange earnings as well as employment opportunities. The industry is based on hides both from cattle and sheep, but since the former weighs more heavily in output and trade it will be dealt with in greater detail.

22. As late as 1963 two-thirds of the hides available from slaughtered cattle were exported in crude or unprocessed forms; of the remaining one-third which was processed by the local leather industry, only 20% was exported.1/ Thus, exports of processed leather represented less than 10% of the volume of the total trade in hides and leather, although in value terms it represented some 20%. Moreover, since it is possible to differentiate between finished leather and that which is simply tanned, the former which represents a further processing state accounted for only slightly more than half of the value of those exports in 1963. Finally, exports of finished leather products (shoes, handbags, etc.) were negligible.

23. As compared with a slaughtering capacity in 1963 of about 3 million head (and an actual recorded slaughter of 1.5 million), the leather industry was estimated to have capacity to handle only 800,000 hides for tanning and probably around 600,000 for finishing. The general policies followed through the 1960s had served to discourage the development of an export-oriented industry. This situation, moreover, had "backward" links in that little incentive existed either in cattle raising or in slaughtering to obtain optimum quantity or quality of hide for leather production.

24. A number of measures were taken during the course of the 1960s as well as in more recent years, which have resulted in major shifts in the character of the industry and of its exports. A system of retentions or export taxes on hides was introduced in 1964 and by 1968 exports of tanned or finished leather represented some 75% of the value of trade in hides and leather. At the end of 1968, a system of tax rebates was initiated for these products so that in more recent years exports of unprocessed hides have all but disappeared.

1/ Based on data published by CIDE, the predecessor agency of the Planning and Budget Office.

Table 2: Exports of Hides and Leather
(in millions of US dollars)

	Hides	Leather /a
1963	14.4	3.2
1968	5.6	10.9
1970	4.5	20.0
1971	3.9	17.5
1972	3.5	19.3
1973	3.9	21.3

/a Includes semifinished and finished leather but not leather products.

Source: O.P.P.

25. Moreover, as indicated, leather has been traded in semifinished or tanned forms and in a more advanced finished state. In 1972, the tax rebate for the former was set at one-half (12%) the level of the latter, producing a further shift to exports of more elaborated products. In line with this policy for developing the finished leather industry, the rebate for tanned leather was reduced to 8% in 1973 and will be reduced to zero at the end of June 1974.

26. Industry sources currently estimate that tanning capacity is about 1.15 million hides representing more than twice the 1963 capacity figure. Capacity for producing finished leather appears to be somewhere under one million hides, also representing considerable increase over that which existed ten years ago. No estimate is available on the value of the new investment which was undertaken for this expansion. It is reported that most of this was financed through suppliers' credits, apparently linked to the major importers, such as Western Germany.

27. With the present annual slaughter running about 1.2 million head there is some under-utilization of tanning machinery but finishing equipment is apparently fully utilized. As a result of the policy favoring exports of finished leather over tanned, some modernization is being undertaken of much of the tanning facilities to improve quality while expansion of finishing facilities is also being pushed by a number of enterprises. Nevertheless, should the total cattle slaughter rise substantially in the next few years there would be need to increase not only the finishing capacity but the tanning capacity as well.

28. At the present time, the industry is dominated by three or four large firms, with one accounting for an estimated 80% of exports of finished and semifinished leather. The rest of the enterprises are extremely small and produce primarily for local consumption. A number of them are integrated with shoe production facilities supplying the local market. To produce leather of exportable quality, the smaller entrepreneurs would require both modernization of existing obsolete equipment as well as expansion facilities. Larger plants have other advantages since they permit capture of wastes and recycling of materials otherwise uneconomic.

Leather Products

29. At present it is estimated that about one-third of total available leather is consumed in the domestic market in the form of leather products, such as shoes, belts, handbags, leather clothing and gloves. About 80% of this output in value terms is made up of shoes, but in terms of volume of leather consumed the percentage is about 70%, reflecting largely the higher degree of processing and value added in the production of this item.

30. It has been estimated that there are about 200 shoe producing enterprises in the country, the majority of which are small-scale and almost handicraft in nature. Moreover, with few exceptions, their equipment is obsolete and not capable of producing qualities of export standards. Some 10 to 15 enterprises are considered capable of exporting but since their present output is almost entirely for domestic consumption, they are hindered by excessive diversification of models and the need to adapt styling, sizing and presentation to meet the foreign market requirements.

31. The recent favorable experience of both Argentina and Brazil in expanding shoe exports and the new domestic policies favoring exports have encouraged producers to explore the possibilities of selling in external markets. Moreover, the differential rebate policy has encouraged exports of more processed products. An export association has been formed and is working with various government agencies to obtain technical assistance for both production and marketing. An expert from UNIDO is scheduled to undertake a study during the course of 1974 to analyse the production situation and possible deficiencies. Assistance in marketing is being provided by the UNCTAD/GATT International Trade Center, through its project with the Uruguayan Direction of Foreign Trade.

32. There has been an increase in shoe exports in 1973, which amounted to over US$700,000 as compared to an annual average of about US$200,000 in the period since 1969. A tax rebate of 36% has been particularly important in this development. Nevertheless, the volume involved, of the order of 100,000 to 150,000 pairs, is still extremely small.

33. Current production is estimated at 3 million pairs (leather only). Capacity is estimated at between 4.5 and 5 million pairs (two shifts), but,

as noted, only a small proportion of this is of export quality. A major investment program is needed to replace obsolete equipment to improve the quality of product and to make other adaptations to meet external market requirements. The UNIDO study will examine total investment costs of such a program of modernization. In this connection, there is need to develop these investment programs working closely with importers and distributors in the consuming countries to ensure both adequate access to and appropriate feedback of trends from those markets.

34. It has been reported that the major leather finishing enterprise is now developing a project to establish a large, modern factory for shoe production, in cooperation with West German capital, whose output would be exported to that country. No details are available on the size or timing of this project. The proposal reflects two trends now dominating the structure of world trade--to raise the degree of elaboration to the maximum efficient level in leather producing countries such as Uruguay and to shift away from the production of these labor intensive products in developed countries such as Western Germany. It should also be kept in mind that even under the most optimistic of assumptions Uruguayan shoe exports will represent a small share of world trade in this item. Assuming ten pairs of shoes per hide and annual slaughter of two million head of cattle and assuming no other use for leather, maximum output would amount to 20 million pairs. Total leather shoe imports of the United States in 1973 were 150 million pairs, valued at about US$700 million.1/

35. As regards other leather products, their production is considerably simpler with modest fixed capital needs and quality is more dependent upon labor skills than on the equipment itself. It is, therefore, not surprising that exports of these items, such as leather clothing and ladies handbags, have been able to rise considerably since early 1972 in response to the incentives offered through the tax rebates (36%) and the realistic exchange rate. From a level of US$200,000 in 1969, these exports are estimated to have amounted to over US$5 million in 1973. Much of this expansion reflects a shift from producing for the local market where demand has been extremely low over the last two years but there were also some small equipment imports, permitting a modest increase in capacity. Given the characteristics of production, in particular the high labor - low capital requirements, possibilities for rapid expansion of output and increased employment are promising.

36. As in the case of shoes, production of these items is widely scattered among many small workshops in the Montevideo area, but there are four or five relatively large enterprises which are closely connected with leather finishing companies. In the case of items such as leather handbags or accessories, the required production processes and the characteristics of both the products themselves and the demand do not provide economies of scale. The limits to the size of these enterprises are partly remediable through policy changes. At the present time, the major obstacles to expansion

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1/ Imports from Brazil amounted to 20 million pairs valued at US$80 million.

relate to the difficulties in obtaining working capital, the uncertainty of supply of processed leather, and the burden of administrative red tape necessary to obtain permission to import capital equipment or to take advantage of any of the special facilities for export, including export financing. A few of these firms do appear to have management capabilities for larger scale and with appropriate incentives (in reality, the removal of the disincentives) they could expand.

37. The characteristics of the market for leather clothing presents other problems. An average leather garment requires three square meters or about two-thirds of an entire hide. Moreover, the nature of demand from the retailer for a style of garment, to provide a range of both colors and sizes, particularly for the markets of the developed countries, will require a relatively large scale of production. Thus, access to raw materials and provision of working capital to finance these purchases are extremely important. While credit policies facilitating access to working capital may be of some use, the expansion of these firms may be best obtained through measures to encourage vertical integration with leather processing. This will largely rest on improving the availability of long-term capital funds. Such a development would be consistent with the growth in finishing capacity which, as noted earlier, would be required by the expansion of cattle slaughter. There are some indications that proposals of this type are being considered within the trade. Moreover, at least two of the leather products factories which are presently exporting clothing are already linked to firms specializing in finishing leather.

38. Of particular interest to the development of the leather-clothing industry but of general importance in order to make the entire industry more economic is the need to improve the quality of the hides which are available for processing. It had been earlier noted that prior to the development of a leather processing industry for export, there had existed few incentives to adopt either cattle raising or slaughtering techniques which would maximize both the quality and quantity of hides from a given slaughter. Thus, many hides were covered with owners' brands, bruised by barbed wire or simply poorly stripped from the cattle when slaughtered. With the growth in processing, better quality of hide was required. It was relatively simple to improve the stripping in the slaughterhouses particularly as they themselves were being modernized and improved techniques were being introduced. The problems of the branding marks and bruises have proven much more difficult to solve and continue to plague the processors.1/ Where the hide will be used for products such as shoes or handbags, the damaged part can be generally cut away but this results in a loss of volume of hide to be used and fewer products per unit. For clothing manufacture, however, where a large cut of hide is required, such damages can, in fact, result in the hide being completely unsuitable.

1/ A UNIDO expert has estimated that eliminating the branding would reduce the loss by 30%.

39. There are a number of techniques which can be used to reduce this waste and programs to educate the cattle raisers on these possibilities are extremely useful. For example, in many developed countries, branding of cattle has been discontinued in favor of such measures as ear tagging which do not affect the hides.

C. The Meat Industry

Recent Trends

40. While value added in meat production is a smaller share of gross value of output than in other industries, the sheer volume of slaughtering (some 1.2 million head of cattle per annum in the last two years plus varying quantities of sheep) makes this the largest subsector (at the three digit ISIC level) in the country. The main problems affecting the supply of livestock are discussed in the general chapter of this report. The present discussion will focus only on certain aspects of the capacity of the slaughterhouses and packing plants, particularly as regards beef production.

41. The industry comprises meat packing plants ("frigorificos") and slaughterhouses under the control of the Ministry of Livestock and Agriculture, slaughterhouses controlled by municipal authorities and slaughterhouses in the interior of the country which are authorized but not directly under the control of the local authorities. The frigorificos, accounting for 50% to 60% of output, are equipped for a full cycle of operations, from slaughter to cutting, freezing or chilling. Some also have facilities for preparing special cuts and some for refrigerated storage. The slaughterhouses, however, can only perform that part of the operations and distribute fresh meat for local consumption, many at the retail as well as the wholesale level. Because of the lack of control, information on the operations of the slaughterhouses in the interior of the country is deficient; the agricultural planning unit of the Government (OPYPA) estimates their output at between 450,000 to 580,000 head of cattle per annum in recent years or 30% to 40% of the total slaughter. The relative importance of their operations is closely linked to the official price policy for beef; when prices are set at levels which are not remunerative for cattle producers, there is a tendency to channel supply away from the registered slaughtering facilities, as was the case in 1971 and the first few months of 1972.

Table 3: Distribution of Cattle Slaughter by Facilities
(in percentages)

	1970	1971	1972
Registered Slaughter	68.7	56.9	63.6
"Frigorificos"	62.5	52.7	57.7
Slaughterhouses	6.2	4.2	5.9
Uncontrolled Slaughter	31.3	43.1	36.4
Total	100.0	100.0	100.0

Source: O.P.P.

42. In the last decade, the structure of the frigorificos has undergone major changes as a result of uneconomic levels of operations which led to numerous bankruptcies, as well as of financial difficulties arising from inflation. At present there are 15 such plants currently functioning and many of these (the traditional larger companies) have been in operation for a considerable period of time, for as long as 50 years in some cases. However, some new plants have been established outside Montevideo, based upon existing slaughterhouses, to replace the most obsolete installations which have been abandoned. The frigorificos account for all meat exports (frozen and chilled, beef and mutton) and some of the by-products. In addition, about 30% to 35% of their output has been for local consumption.

43. The capacity of the existing plants has considerably exceeded their output, even in 1970 which represented the peak production year in the last decade. Current capacity is estimated at over two million head per annum.

Table 4: Cattle Slaughter in "Frigorificos"
(in thousands of head)

1967	1968	1969	1970	1971	1972	1973
839.1	919.3	775.1	1,137.6	709.1	728.2	770.1

Source: INAC

44. Only part of this overcapacity is due to the seasonal nature of the animal supply, with the period of heaviest slaughter in the first five months of the year at which time there may be some pressure on facilities. This weakness of the structure of the industry, an underutilized frigorifico capacity, which is export-oriented, alongside a substantial capacity in small slaughterhouses widely scattered in the countryside which are domestic-market oriented, has its origins in the policies in effect during the 1950s and early 1960s. During that period, the Government followed tax, price, exchange rate and labor policies which both discouraged exports and encouraged the establishment of channels to meet local demand outside those subject to government controls.

45. Toward the end of the 1960s, various changes, including the initiation of the Plan Agropecuario, began to be introduced which served to encourage the flow of cattle to the frigorificos. At the same time, the Government moved to make resources available to modernize and improve these installations including, in particular, to finance measures to raise sanitary and hygienic standards. (In 1969 the UK had prohibited meat imports from Uruguay for sanitary reasons.)

46. From mid-1969 to mid-1971, these plants invested the equivalent of US$11 million in such improvements, of which US$3.1 million was in foreign currencies, according to estimates of OPP. In 1970, a loan for US$13.4 million was signed with the IDB to finance modernization programs; local funds required as counterpart were estimated at US$10 million. However, none of this was used in the period through 1973 as the Government continued to make available peso funds to the frigorificos. This policy has been changed and in the last months of 1973, three subloans under the IDB loan had been approved while four more were awaiting approval before the end of the year, representing about US$5 million in commitments.

47. In addition, a study is expected to be completed for the IDB by mid-1974 which will consider a program for refrigerated storage, examining the needs of the industry and the most efficient way to meet those needs through establishing separate storage facilities and/or expanding or establishing such installations in the frigorificos themselves. Preliminary estimates of the foreign currency requirements for this kind of program are in the range of US$10 million. It is also expected that there will be large local currency requirements which could raise problems in view of the persisting liquidity difficulties in the industry.

Future Prospects

48. The modernization and storage programs, as well as the programs for improving livestock pasturage and related feed facilities, should reduce the seasonal pressures on the frigorificos capacity so that these plants could handle an increase in the animal slaughter. Other factors which will affect the volume of exportable supplies include improvement of transport facilities and the level of domestic consumption.

49. On the question of transport, the IDB study mentioned earlier will also consider these difficulties including the possibilities of containerization which is related to cold storage facilities.

50. Within the existing or expected supply of cattle, some attempt is being made to increase foreign exchange earnings by exporting special cuts rather than sides or quarters which make up almost 90% of present exports. Some of the IDB funds are to be used to equip plants for these operations. As regards more processed forms of beef (e.g., canned cooked beef), there have been practically no exports of these items since 1970, and INAC officials have indicated no interest at this time in encouraging any renewal of such operations or establishment of new plants for this purpose.

D. Traditional Consumer Goods Industries for the Domestic Market

51. The traditional consumer goods industries which produce for the domestic market (e.g., non-wood textiles, food excluding meat, beverages and tobacco, furniture) still account for half of total manufacturing output (see Table). These products are not subject to significant economies of scale and, generally speaking, their production can be economically undertaken in a market the size of Uruguay (particularly with its high per capita income).

52. The food industries (excluding meat) are characterized by very low value added, representing a minimum of processing of basic agricultural inputs. Export potential for these items is essentially determined by the relative efficiency of agriculture and, especially in the case of Uruguay, by policies affecting the allocation of agricultural resources among competing products, given external demand. From the point of view of the industrial sector, what is required is appropriate feedback from agriculture, at both the public and private levels, to ensure the availability of manufacturing capacity and of any required complementary inputs to process the expected harvest. In the case of Uruguay, the ability of the industrial sector to respond to developments, either from the side of agricultural production or external demand, is restricted by the mass of governmental controls, in particular those on both imports of capital goods and of intermediate products.

53. As an example, in recent years, there have been excellent fruit harvests but, because of the conditions surrounding the actual harvesting, the magnitudes of the crops are often not fully known until shortly before they are to be marketed. The local canning industry, in order to import the cans required for processing, must apply for import quotas for that purpose and, on occasions, this has been a time-consuming process. Particularly in recent periods of general tightness of supply of those items, this has proven to be a substantial obstacle to taking advantage of the opportunities offered.

54. Most of the food processing enterprises have been in existence for a considerable period of time and there is a large element of obsolescence of equipment. A survey of fruit and vegetable canning plants which OPP conducted in 1971 reported that, of seven facilities accounting for 80% of production in this category, only two had machinery capable of providing export quality products. The Government's development plan foresaw a modest volume of exports of canned fruits (pears and peaches) and vegetables (mainly tomatoes) were considered possible, with a correspondingly modest investment in modernization and new facilities. The principal markets were expected to be the neighboring countries such as Brazil.

55. Up to the present, this trade has not developed even though the supply of raw produce has increased. The fruits have instead been exported in fresh form. This trade amounted to $4 million in 1973 as compared to some US$600-800 thousand per annum in the period 1969 through 1972. In the light of continued excellent demand conditions in world markets, specific measures may be required to assist the development of this industry. Easier access to imported inputs such as cans, as well as to the necessary new equipment, is intimately related to the entire question of import liberalization. Since the industrial processors are mostly independent enterprises buying directly from farmers, there is need to facilitate purchase contracts and similar arrangements ensuring supplies to processors as well as markets to producers; access to credit is particularly critical for this purpose. There may also be scope for helping to establish producers' cooperatives with their own canning facilities. There appear to be a few such cooperatives in existence at present but their equipment is considered among the most obsolete and would require complete replacement.

56. Given the seasonal nature of the harvest, better use of the available processing machinery could be accomplished if cold storage facilities were available to keep the produce until such time as it could be processed. In this connection, the program for expanding cold storage facilities for the meat packing plants is considering the possible use of such space by fruit and vegetable processors.

57. On the marketing side, programs such as those conducted by the Office of Foreign Trade, to supply the industry with detailed information on external market requirements, should be expanded. For example, one processor has already successfully tested exports of fruit pulps which are used for further industrial processing in the importing countries. Since these items have relatively lower can costs per unit than items for household consumption, Uruguayan products dependent upon imported cans have a better competitive position in foreign markets.

58. Finally, it is necessary to take into account the interrelationships between fruit canning agricultural policies affecting other products. For example, most canned fruits for direct consumption require large amounts of sugar for their preparation. In the past local sugar was high-cost, affecting the production costs of the processed products and their competitiveness in world markets.

59. An OPP survey has indicated that of 29 dairy industry plants in operation in 1971, only two had adequate modern equipment to produce within sanitary levels required for export. A small trade has developed in these items, mainly cheese and industrial products for further processing such as casein, the production of which has benefitted from concessions granted by Mexico under LAFTA arrangements. Given current price controls on these products, domestic price policy is extremely important in determining supply and export opportunities should be taken into account in these decisions.

60. A major food product, fish, has been all but ignored for both domestic and external markets. Considerable attention is now being given to proper development of this branch, taking into account the fact that there is broad scope for increasing supplies for the domestic market as Uruguayan per capita consumption at four kilos per annum is extremely low for a country of its income level. Moreover, external demand is exceedingly buoyant at this time. Preliminary studies have indicated excellent fish resources in nearby waters. The FAO is now undertaking a major detailed study to make more precise these opportunities and will provide estimates of investment requirements, both for processing and port infrastructure.

61. An interministerial committee submitted a report in 1972 on the needs for developing the industry which include not only fishing boats but processing plants, refrigerated storage capacity and port facilities as well. While there exist a number of privately-owned firms, at present the largest operation is that controlled by a government agency, SOYP, which includes boats and capacity for freezing and storage. The Government has announced that future development will largely be left in the hands of the private sector. Nevertheless, all investment decisions must be approved by a National Fish Council recently created.

62. While there have been large numbers of investment proposals, the Fish Council has moved very slowly in making its decisions and by the end of 1973 had not yet approved any projects. Among those which are currently being considered are proposals for joint ventures with Uruguayan capital from Argentine, Brazilian, and United States investors. Output will be available for export as well as the domestic market.

63. The non-wool textiles industry is dominated by one large integrated producer, a wholly owned subsidiary of a large U.S. textile producer, which accounts for about 50% of the local supply of cotton, synthetic and mixed yarns and fabrics. There is a large number of small producers providing the balance. The industry has been completely protected in recent years through the import licensing system which has restricted imports of competing products. Domestic prices appear as high as twice the international level for many of these items. But industry sources feel that prices could be reduced and quality improved if manufacturers were permitted access to imports of machinery as much of the existing equipment is obsolete.

64. The industry is unlikely to be a major exporter, particularly in view of the lack of specialization. Some exports have been recorded in recent years but these have been items in short supply in world markets (e.g., cotton, denims, and knits). With a low level of domestic demand, the industry has had capacity available for export contracts. In this connection, there has also developed a small trade with Brazil in synthetic yarns as a result of that country providing special quotas for Uruguayan products. These items enter Brazil with a 10% preference and trade is made possible by a combination of duty-free imports into Uruguay of the inputs and a tax rebate on the exports.

E. Durable Consumer Goods Industries

65. Industries producing durable consumer goods were among the activities which received special stimulus under the import substitution policies followed during the 1940s and 1950s. At the present time, they are generally operating well below capacity and under highly protected conditions. Efficient production of the majority of these items require relatively larger markets than the country can offer, not only under current conditions of stagnation but for the longer term as well. A number of these enterprises have sought to diversify output, manufacturing related products with small equipment additions or adjustments. LAFTA complementation agreements and the bilateral accord with Brazil, as well as the tax rebate incentives, have recently encouraged exports of a few of these items.

66. Among consumer appliances, an exception to the overall pessimistic picture is found in the case of certain electronic components. A modest trade has developed not only within LAFTA but also with some European countries for parts and components for record players, sound systems and television sets. Manufacture of these items requires high labor skills and given the availability of literate and adaptable human resources in the country, their production for export has proven economic under existing conditions. In these instances, since some of the inputs are imported (from LAFTA countries as well as third areas), the tax rebates are generally not large. While this trade will be of small magnitude, the possibilities for employment generation are important for a country the size of Uruguay.

67. Among the industries experiencing the most difficulties at this time is the automobile industry. It should first be noted that new car prices in Uruguay are among the highest in the world; a medium-size passenger vehicle currently sells for approximately $13,000 while the smaller cars sell for about half that price. Imports of new cars are prohibited and the local supply is based on the assembly of imported kits with certain locally produced parts. A study by OPP in 1972 reported ten assembly plants in operation with capacity for about 16,000 vehicles; production in 1971 was less than half of that capacity. It is believed that production rose slightly in 1972 but declined in 1973. In 1971, about a quarter of the kits were imported from Argentina under a complementation agreement within LAFTA. This agreement provides for the

importation of kits from that country and the export of parts from Uruguay for an equivalent value, FOB basis, with preferential tariffs in both countries. When the agreement was initiated, Uruguayan exports had to be equivalent to only 45% of the value of Argentine exports but this percentage was raised over time and for 1974 it must be 100%. Because of the concessions involved, the CIF value of these kits appears to be somewhat higher than from third countries. Moreover, in order for Uruguay to export parts for the equivalent value, it appears that items are being shipped at less than their cost of production with the difference being added to the price of the locally assembled cars and thus, in the final analysis, being passed on to the Uruguayan purchaser. Because of the conditions of the agreement, these exports have been rising and in 1973 amounted to almost $3 million.

68. Under current conditions, the industry is grossly inefficient. During 1974, the Government will undertake a review of the complementation agreement; this may also provide an opportunity to review the industry in general, to examine the real foreign exchange costs to the economy and the costs in fiscal income which is lost due to the inefficiencies.

F. Non-Metallic Minerals - Construction Materials

69. This sector has had a strong growth trend since the mid-1950s. In the early part of the period, this reflected primarily import substitution but, in more recent years, exports have contributed to the expansion. The country appears to be well endowed with the basic sands which are the raw materials for the principal products involved--cement, glass, ceramic wares and tiles, and is in a particularly strong position to supply the neighboring countries.

70. About half of the output of the branch is accounted for by cement and associated products (e.g., cement blocks). There are currently three enterprises producing cement of which two are large scale. One of the latter is state-owned, part of ANCAP, while the other is a subsidiary of a major U.S. corporation and has been in operation for a considerable period of time. In 1973, ANCAP brought into full production its second plant (of 120,000 tons). This expansion was financed by IDB and represented the first stage of a construction program which would eventually reach 270,000 tons. A request for a loan to cover the final stage is now being prepared for submission to IDB.

71. Since 1964, a fairly substantial export trade has taken place with the southern areas of Brazil where there has been a high rate of development. The proximity of the cement plants in northern Uruguay has provided a locational advantage favoring this source over alternative Brazilian sources. In addition, periodically, exports have been shipped to Argentina and Paraguay in response to local shortages. At the end of 1973 large orders were taken for shipment to South Africa so that ANCAP estimated one-third of output was being exported with excellent prospects to maintain this trade. Export commitments and domestic market prospects represented full utilization of existing capacity.

72. As regards ceramic ware, tile, and glass, the same locational factors which have favored exports of cement to Brazil have recently led to exports of these items to that country. In addition, since 1969 there has been substantial trade in the first two products with Argentina and Paraguay. Thus at present these exports amount to about 20% of Uruguayan output. Recent developments in world markets for tiles, particularly the change in the competitive position of Japan, have stimulated interest in purchases from Uruguay and some sales have been made to overseas buyers. While there appears to be at present under-utilization of capacity, expansion of output at competitive prices and export quality would require some modernization of equipment.

73. Within this subsector, the country also appears to have a strong resource base for exploitation of marble and granite for export, although more detailed geologic explorations are required to determine the characteristics and size of the deposits, particularly for marble. As regards black granite, some quarrying is currently taking place, in recent years almost entirely for export, but under primitive conditions producing and shipping only in the form of crude blocks. World market conditions have been favorable for more intensive development of this resource. One enterprise has applied to BROU for financing (through IDB funds) for a modest expansion and modernization program. But in view of present conditions, efforts should be made to promote a broader expansion program including the establishment of polishing facilities. This type of project would best be undertaken with companies experienced in the marketing and distribution of the finished products and could also include international financial assistance.

74. Finally, there are a number of elements of uncertainty now affecting this subsector as it is one of the principal consumers of energy. According to the 1968 census, fuel and lubricants accounted for 18% of the value of total inputs for production of these items, electricity another 6%. While no breakdown is available by specific products, the production of cement is known to have particularly heavy energy requirements. The proposal to expand the cement capacity will have to be re-evaluated in the light of changes in energy prices and in the cost of equipment.

ANNEX I

RESUME OF CAPITAL GOODS IMPORT LOAN 528-L-022

Loan Amount: US$15.0 million authorized; US$13.8 million disbursed.

Borrower: The Government of Uruguay.

Executive Agencies: The Central Bank, an "ad hoc" Inter-ministerial Commission and commercial banks.

Date of Loan Agreement: October 17, 1969.

Date Conditions Precedent to First Disbursement Met: February 20, 1970.

Terminal Disbursement Date (final): December 31, 1974.

Objective: To provide medium-term credit rapidly to the private industrial sector for the purchase of capital goods.

Operating Procedure: The Inter-ministerial Commission reviewed and approved all sub-loan requests; the Central Bank administered the loan; the commercial banks guaranteed the sub-loans and the sub-borrowers assumed the exchange rate risk. The release of the first US$5.0 million was subject to the signing of a formal standby agreement with the IMF and the release of the funds in excess of US$5.0 million was subject to a review of Government of Uruguay's progress in carrying out its economic program and the project.

Historical Events Affecting the Project: The original loan proposed financing for five industrial sectors that had export potential. The major part of AID's lending was intended to modernize and expand Uruguay's 15 major meatpacking plants. Early in 1970, however, the Inter-American Development Bank signed a US$14.2 million loan specifically for the meatpacking industry. Therefore, AID notified the GOU that major expansion and modernization of the meat processing industry would not be eligible for financing under the Capital Goods Import Loan.

Simultaneously, industries were included that met the criteria of import substitution and utilization of materials abundant in Uruguay but not fully exploited. Also, Western Hemisphere (Code 940 Countries) procurement was made eligible under the AID loan. By broadening the eligibility criteria, the effective demand was maintained and by May of 1971, the first tranche of the loan was committed and the GOU requested the opening of the second tranche.

As required by the loan agreement, release of the second tranche was subject to the Borrower's "(a) continuing eligibility and actual drawing under the IMF standby agreement or evidenced that it has taken other steps consistent with its Economic Program acceptable to AID; (b) satisfactory progress in carrying out its Economic Program; (c) satisfactory progress in carrying out the Project; and (d) enactment of legislation to permit commercial banks to make readjustable loans". On October 29, 1971, the Mission, after reviewing the above, recommended the release of the second tranche and AID/W concurred. (See cable MVD 2587, dated October 29, 1971.)

On December 3, 1971, the US$10 million second tranche was released with no major project modifications. From January through June, 1972, sub-loans amounting to US$7.5 million were approved, and, with only US$2.5 million unallocated, Mission encouraged the Inter-ministerial Commission to again give priority to export industries. In October and November of 1972, the remaining US$2.5 million was approved.

In December 1972, the Central Bank established a deadline for the opening of import permits to sub-borrowers. As a result, US$1.5 million was reallocated between January and October 1973 and the loan terminal disbursement date was extended to December 1974 to accommodate the reallocation.

Total disbursements were US$13.8 million. The balance of US$1.2 million was deobligated because the last two sub-loan requests (FIAT and Navegación Atlántida) were originally approved by the Mixed Commission but were not approved by USAID and the remaining funds could not be reprogrammed and disbursement made before the December 31, 1974 loan terminal disbursement date.

Accomplishments: See Attached Tables I through IV.

Table I

SUMMARY OF SUB-LOANS APPROVED

AID LOAN N° 528-L-022

By Banks

Name of Banks	N° of Loans	Total Amount US$	Percentage Total Approved
República O. del Uruguay	167	7.137.164	47.6
Crédito	14	1.640.518	11.0
Comercial	48	1.369.836	9.1
Mercantil y Popular	23	1.068.079	7.1
F. N. C. B.	20	1.041.002	6.9
Holandés Unido	3	399.895	2.7
Francés e Italiano	4	351.929	2.4
Sociedad de Bancos	13	345.716	2.3
Montevideo	11	300.394	2.0
Londres y América del Sud	3	274.316	1.8
Aldave y Martínez	5	223.368	1.5
Palestino	9	179.024	1.2
Pan de Azúcar	5	171.355	1.1
Cobranzas	4	121.695	0.8
Financiero Sudamericano	8	102.234	0.7
U.B.U.R.	6	100.106	0.7
BANFED	2	46.970	0.3
Litoral	3	43.880	0.2
Caja Obrera	1	34.529	0.2
Exprinter Casa Bancaria	1	24.400	0.2
Israelita del Uruguay	1	17.038	0.1
Del Plata	1	6.552	0.1
	352	15.000.000	100.0

Table II

Sub-Loan Repayment Terms

AID LOAN N° 528-L-022

Terms	N° of Sub-Loans	Amount	% of Total
6 months	43	848.143	5.7
1 year	24	1.445.450	9.6
$1\frac{1}{2}$ years	7	94.572	0.6
2 years	4	296.044	2.0
3 years	83	2.044.986	13.6
4 years	17	276.720	1.8
5 years	85	4.867.458	32.5
6 years	43	1.399.851	9.3
7 years	21	843.853	5.6
8 years	3	253.530	.7
10 years	22	2.629.393	17.6
TOTAL	352	$15.000.000	100.0

Summarized Breakdown

6 months to 2 Yrs.	78	2.684.209	17.9
3 to 6 Years	228	8.589.015	57.2
7 to 10 Years	46	3.726.776	24.9
	352	$15.000.000	100.0

Table III

Summary of the Capital Goods Imported

AID LOAN N° 528-L-022

Calendar Years 1970-1974

By Industrial Sectors

Industrial Sectors	N° of Loans	Amount	%
Truck Kits	18	2,150,000	15.99
Transport (Buses, Trucks)	6	1,962,000	14.59
Textile & Clothing	58	1,746,000	12.99
Extractive	32	1,268,000	9,43
Construction	28	1,067,000	7.94
Metallurgic	60	915,000	6.80
Food Processing	17	633,000	4.71
Automotive Industry	12	585,000	4.35
Poultry	13	517,000	3.85
Plastic	12	528,000	3.92
Glass	8	298,000	2.22
Agro-Industry	15	289,000	2.15
Printing	12	282,000	2.10
Meat Packing & Cold Storage	4	270,000	2.01
Fishing	4	141,000	1.04
Fertilizer Preparation	5	131,000	0.97
Electrical & Electronics	12	113,000	0.84
Leather Processing	5	112,000	0.83
Pork	6	90,000	0.67
Paper & Cardboard	4	83,000	0.62
Soft Drink Industry	3	59,000	0.44
Rubber	2	47,000	0.35
Pharmaceutical	5	39,000	0.29
Tobacco	3	35,000	0.26
Soap & Industrial Detergents	3	28,000	0.21
Forestry	1	20,000	0.15
Banking Service	1	19,000	0.14
Sugar	1	19,000	0.14
TOTAL	350	$ 13,446,000	100.00

Table IV

List of Capital Goods Imported

AID LOAN N° 528-L-022

Calendar Years 1970 - 1974

By Type

Type of Items	%
Truck Kits (K.D.)	15.9
Inter-State Buses	13.9
Traxcavators and Loaders	7.7
Diesel Electric Generators	3.7
Fork Lift Trucks (all types)	3.6
Macaroni Production Lines	2.9
Metal Working Machines	3.4
Ind. Sewing Cutting and Processing Machines	3.0
Textile Machinery - (Various Types)	2.7
Plastic Injection Machines, Extruders and related equipment	2.5
Lathes	2.2
Plastic Bag Making Machines	0.9
Spare Parts	1.9
Steam Turbine Generators	1.5
Offset Printing Presses and Access.	1.6
Textile Spinning Frames and similar	1.4
Refrigerating Plants	1.4
Stone Crushers	1.3
Knitting Machines	1.3
Air Compressors	1.3
Mobile Cranes	1.2
Poultry Incubators and Egg Classifiers	1.3
Equip. for Automotive Assembling Plants	1.0
Accounting Machines	Less
Road Rollers	than
Refractory blocks for Furnaces	1%
Freon Compressors	"
Glass Bottle Machines	"
Jigs for Automotive Industry	"
Asphalt Plants	"
Electric Welding Equipment	"
Dehydrating Plants	"
Chicken Feed Processing plant	"
Narrow Fabric Needle Looms	"
Packaging Machines	"
Textile Texturizers	"
Tracklaying Tractors	"
Fish Meal and Oil Plants	"

Type of Item	%
Stone Vibrating Screens	Less than 1%
Gravel Washing Machines and Classifiers	"
Flexographic Printing Machines	"
Nitrogen Generator Plants and Thermos	"
Tire Recapping Plants	"
Battery Plates Automatic Machines	"
Marine Diesel Engines	"
Fruit Packing Plants and Trade Markers	"
Poultry Automatic Feed Lines	"
Cotton Cleaning Machines	"
L.P. Gas Tank Trucks	"
Electric Glass Melting Supplements	"
Black Toppers and Asphalt Laying Machines	"
Ice Making Machines	"
Poultry Slaughtering Plants and Coolers	"
Zipper-making Machines	"
Crankshaft Working Machines	"
Poultry by-products plants	"
Leather Processing and Finishing Machines	"
Industrial Ovens and Furnaces	"
Scrapers	"
Centrifugal Pumps and others	"
Agricultural Power Sprayers	"
Forest Tractors for Lumbering	"
Quary Pneumatic Hammers and other Machs./Accs.	"
Electric Cable winding and working Machines	"
Chicken Depluming Machines	"
Electric motor insulation machines	"
Double-die Strip Feed Presses	"
Bulldozers	"
Glass Making Batchers	"
Grain Dryers	"
Diesel Engines	"
Automatic Metal Sheet Feeders	"
Tablet Compressing Machines	"
Pharmaceutical Homogenizers	"
Tires and Tubes for Quary Tractors	"
Vegetable Slicing Machines and Similar	"
Metal Testing Equipment	"
Wood Working Machines	"
Spectophotometers	"
Electric Controls and Testing Equipment	"
Miscellaneous Printing Equipment	"
Miscellaneous Equipment	"

AGRICULTURAL CREDIT ANALYSIS

Increasing agricultural production through adoption of improved technology and management practices is closely associated with increased capital use; (a) short term or operating capital for increased use of off-farm inputs (fertilizer, labor, herbicides, etc.) and (b) intermediate and long term capital for machinery and improvements.

The main sources of capital in the agricultural sector are: (1) the capital generated during the production process, particularly important in crop production, (2) producer savings, and (3) institutional credit from private and government credit banks. The most important source of agricultural capital is that generated during the production process and producer savings, both of which will increase with the adoption of profitable production and management's practices. Most Uruguayan farms are diversified into several enterprises, each using and producing capital during different production periods of the year. The frequently observed combination of summer and winter crops each assisting in financing the other enterprise is an example. Institutional credit plays an important role in providing supplemental short term production capital and for longer term capital where producer savings are inadequate to cover major investment.

Inflation of Uruguayan magnitude creates serious pressures on any institutionalized credit system. Frequently, the rates of interest, even though high, are less than the rate of inflation.- creating in effect negative interest rates. Under such circumstances, lending agencies soon suffer capital losses if loans are not adjusted for inflation while at the same time providing significant subsidies to their borrowers.

Borrowers have the incentive to obtain the maximum amount of available credit as long as they can locate their excess capital at higher rates of return than the subsidized credit cost. Producers try to minimize their liquidity in order to protect the real value of their assets from the high rate of inflation and use as much credit as possible.

A natural reaction of a credit institution to a negative interest rate condition is to keep the loans as short term as possible. Thus, we find the bulk of the agricultural loans in Uruguay are short term, production loans. There is limited intermediate and long term credit available, as will be pointed out later in this paper.

To analyze the institutional credit situation in Uruguay, it is convenient to divide agricultural credit by source, type (period of loans), and use by enterprise or investment activity.

The Banco de la República (BOR) is the principal government credit institution and is the major supplier of short-term production credit for crops, fruit, vegetable, poultry and swine production (see Annex I, Table I).* The BOR also has limited short-term credit for livestock health costs and sheep shearing

Private banks are major suppliers of short term credit (30 - 120 days) for purchase of livestock (US$ 76.5 million in 1973). This credit is closely associated as financial transaction for rural livestock auction markets and explains why over 90% of the private bank credit was for livestock during the 1971-74 period.

The Plan Agropecuario, supported by IBRD financing, supervises the intermediate term credit (up to a 7-year payment period) for development loans in the livestock sector amounting to about 6 million dollars annually.** These loans are administered through the BOR.

The BOR has credit lines of up to two years for machinery purchase and repairs. BOR credit is available for breeding bulls and rams and dairy cows with terms of up to two years.

No long term credit for land purchase is presently available in Uruguay.

GOU agricultural policy as it relates to rural credit is implemented through the BOR. Due to the importance of this institution in rural credit, a major portion of this section is devoted to the BOR and its specific activities in rural credit.

In the allocation of financial resources for agricultural credit through the BOR the National Planning Office and the Ministry of Economy and Finance establish the global covenants available for allocation. The Ministry of Agriculture sets the priorities for credit financing by crop or commodity. The BOR relates the amounts of financing available to commodity priorities and establishes amounts of credit available for each major commodity. Also, since the BOR operates a continuing agricultural credit program which, through loan repayments produces funds available for relending, these amounts are included as annual lending levels as established.

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* To express current pesos into US$ the following procedure was used in this study: current pesos were deflated by, the cost of living index 1961 = 100. 1961 constant peso values were then converted to US$ by using the 1961 financial exchange rate of 112 pesos to US$ 1.

** This program is supported by loan assistance from the IBRD.

Many of the credit lines are self-sufficient and normally require no additional budgetary allocations. On the other hand, some international agency sponsored credit lines (Plan Agropecuario) have firm host country contributions which do require annual or periodic budgetary support depending upon the demand created by these programs.

The BOR has, in addition to the principal bank and seven branches in Montevideo, 75 field offices or branch banks throughout the country. The banks have, in addition to the regular banking personnel, a staff of 52 agricultural trained field men who work as supervisors of producers' use of the bank credit.

The BOR has historically played a major role in credit supplying approximately US$ 45 million annually during the 1960 - 72 period. Actual credit made available compared to agricultural gross value product (AGVP) is high, averaging 16% (1960 - 72).

BOR credit is high relative to the value of agricultural inputs. BOR credit, after decreasing during the late 1960s, has been increasing in recent years in response to increased credit demand due to more favorable conditions in the agricultural crops sector. In the early 1960s credit was nearly equal or more than the value of agricultural inputs. This period was associated with large crop areas and high capital investment in agricultural machinery.

The level of BOR agricultural production credit used is closely correlated with the amount of crop land planted. An unpublished study by the MAP showed that the area planted to wheat in Uruguay was more a function of climatic conditions and agricultural prices rather than credit availability; a similar relationship pertains to other crops. *

Between 1970 and 1974, the area planted to major crops increased 14% and credit increased 48% indicating that the BOR was very responsive to credit demands during a period of increasingly favorable economic conditions for crop production but with rising production costs. Crops account for about 47% of rural credit, livestock 22%. Wheat and rice are the two most important crops in terms of amount of credit accounting for 31 and 19% respectively of the creditgranted for crop production.

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* MAP/DIEA, an unpublished study on the wheat sector in Uruguay during the 1950-73 period.

BOR production credit loans terms, guarantees, etc. are defined through different credit formulas. These formulas, in addition to specifying credit terms and obligations, also include a "technological package". BOR field men serve as advisors and inspectors to see that these improved practices are followed. The "technological package" concept has had a positive influence on certified seed and fertilizer use.* Although the credit formulas are quite specific a great deal of flexibility exists to modify the formula due to increased cost from inflation or unforeseen problems, such as a pest control cost not included in the formula. Branch directors contact the Montevideo officer who, in turn, consults other branch directors, then a formula modification is relayed back to the branch director who contacts producers and extends more credit.

All crop loans are short-term operating capital loans and are paid at the end of the production cycle: however, special provisions exist in case of crop failure due to climate or pests' problems. Loans can be extended to the next crop year in case of crop failures without being charged additional interest until the credit for the next crop year is extended. This procedure essentially eliminates default in loan payments.

In the past, BOR has had difficulties in getting capital to producers early in the production cycles. To overcome these delays, the BOR has, in the past two years, given credit for early land preparation activities before actual formulas for credit are prepared. This is an attempt to make credit availability more timely and insure that proper production practices are completed.

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* This is based on observation and survey work by the MAP - DIEA division but quantified estimate have not yet been published.

** All payments for slaughter cattle and sheep as well as grains purchased by the government are channeled through the BOR. The BOR thus discounts loan payments before paying market receipts to borrowers.

BOR crop production credit is in general quite liberal covering 80 - 85% of the cash cost of production for those farms qualifying for the full formula. Even in larger farm units, the bank credit covers the seed and fertilizer cost of approximately 50% of the cash costs of production. Credit is made available in specified installments during the production process (land preparation, seeding and crop protection and harvesting costs).

The BOR's interest rates are controlled by law and, for the period of August 1966 to August 1973, ranged between 8.75 and 9.75% annually depending on the line of credit guarantee, etc. In addition as much as 9% annually was charged, for commissions.* If the maximum rate of interest is added to the maximum rate of commission charged the annual real rate of credit cost would be 18.75%, well below the average rate of increases in the cost of living index of 65.4% annually during the 1966-73 period. Only in 1970 when the cost of living index rose 16.4%, was the credit cost positive.

Interest rates were increased to 28% between August 1973 and September 1974, when the rate was raised to 43%. These rates are still well below inflation rate and the BOR is presently in the process of adoption of readjustable production credit. Only with readjustable loans can the bank extend intermediate and long term credit.**

Private banks could not compete with the BOR in the same credit lines at the highly subsidized credit rate. This, in part, explains their concentration on short-term higher cost credit for cattle and sheep associated with auction market intermediation.

BOR credit has, in several aspects, favored the small and medium sized producer. Credit availability is greater per hectare for small farmers as illustrated by the 1974-75 formula for winter crops that grants larger quantities of credit to farms under 500 hectares. Credit formulas in addition exist for major enterprises found on small and medium-sized farms, including sugar beets, dairy, potatoes, poultry, hogs, vegetables, fruits and vineyards.

BOR and the Plan Agropecuario are presently initiating a pilot program for small farms that have critical capital, technology and management problems. This program, now in the final stages of preparation, will include in addition to a number of adjusted credit lines, an intensive technical program including production, economics and financial assistance.

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* Banco Central del Uruguay, Seminario Mercado de Capitales en el Uruguay, Tomo II, Montevideo, 1973, p. 561.

** The decreasing portion of credit available for machinery during 1970-74, in part, reflects the difficulty of extending longer term credit at negative interest rates. (see Table I).

The Plan Agropecuario's credit program is for development of the livestock sector.* The most important lines of supervised credit are for pasture improvement, machinery, pasture division and watering points. The Plan also has a special line of credit for swine production. The Plan credit has a 7-year term with 2 to 3 years grace period on payment of interest and principal. The credit is adjusted on the basis of an index of beef and wool price or the cost of living index. Plan credit has also aimed at special assistance to small and medium size producers and charges a progressive interest rate and credit adjustment based on farm size.** Over 60% of the Plan loans granted to producers were under 400 Hectares, 16% under 100 Hectares, during 1972-73.

It can be expected that the Plan can adequately meet any increased credit requirement from an increased adoption of technological change in the livestock sector and any increased availability of technical information will be complementary to their supervised credit program.

The BOR is frequently criticized by producers as being excessively bureaucratic and time consuming. This is particularly true for new credit users that do not have a credit rating established. Branch directors are aware of this problem and are making progress in their efforts to minimize producers' time in the loan application, etc. One has to recognize that the BOR is a government bank and it is used as a means to enforce laws as well as implement agriculture policy. As can be observed in the wheat formula, a producer is required to have his taxes paid up (land tax, social security, etc.) before he can take out credit. If a producer has his credit rating established and is up to date on his obligation to the government, the time he needs in acquiring the credit is reasonable but improvement could still be made in credit processing.

The BOR formula system of loaning is effective for massive credit assistance in a highly inflationary economy.*** It does, however, have the weakness of not being aimed at particular producer's credit needs. Without adjusted credit, it will be impossible for the BOR to establish a balanced credit program recognizing individual producer's short, intermediate and long-term capital needs.

Farm management and financial research and extension at the producer level could be useful to the BOR credit program and assist in developing a basis for overcoming some of the weaknesses of the formula line credit. In any case, with the rates of inflation and instability Uruguay is experiencing any well balanced farm credit program will be

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* This program is supported by IBRD and BOR accounting for 85% and 15% of the funds respectively.

** Interest rates are 3% for farms up to 250 Hects., 6% between 251 and 400 Hects., and 8% for farms over 400 Hects. Credit adjustments are 50% of the adjustment rate for farms under 200 Hects. and 75% of the rate for farms between 201 and 400 Hects.

*** The bank is getting out approximately 60,000 loans a year.

difficult to employ. The formula line credit system may be the best way to deliver a massive credit assistance in Uruguay until the rate of inflation can be reduced and more stability can be achieved in the agricultural sector.

With the background on the past and present agricultural credit programs, consideration can be made as to the adequacies and limitations agricultural credit could have on the IATA assistance program to promote adoption of production-increasing technology.

In evaluating availability and demand for agricultural credit, the following factors must be considered: (1) with the proposed adoption of adjustable credit, the BOR credit demand will decrease and private institutional credit will be more competitive, allowing it to expand into areas not profitable at interest rates now charged by the BOR: (2) with adjustable credit, the BOR could expand credit and develop new lines for intermediate and long-term capital needs: (3) increased productivity from adoption of improved production practices will increase producer operating capital and savings which will, for the most part, offset increased capital requirements: (4) The IBRD's continued credit support of livestock sector, implementation of the new citrus development loan and possible implementation of the Plan Granjero (production area related to fruits, vegetables, poultry and hogs) could cover increased credit demands in these areas: (5) if the GOU continues to purchase wheat and other commodities, this will insure quick payment and reduce producer need for credit to cover delays in receiving payment for commodities: (6) the BOR may be required to respond to special programs or credit needs such as the recent soybean production development program. These types of new demand areas, however, will likely be associated with national policy and resources will be provided to make them feasible.

Given these considerations, the major area of expected growth in demand for credit, which is not directly connected to lines of credit from special development loan programs in progress or expected to be implemented, is for crop production. The growth in demand for crop production credit will be closely associated with: (1) the possible expanded crop area, (2) the increased capital requirement for improved technology of production over the actual technology, (3) increased capital requirement to replace obsolete machinery and to increase machinery capacity, and (4) the national agricultural policy and crop prices which have in the past, in addition to climate, been more important in explaining area planted rather than credit availability.

Increased credit demand from factors 1 and 2 conditioned by 4 for crop production will be for short run operating capital, where the BOR historically has not had difficulty in responding to. The increased intermediate term capital demand required for machinery investments is a potential problem area if the BOR cannot fully implement the credit adjustment program and expand credit in this area.

The allocation to this activity has deteriorated in the past few years with the high rate of inflation and lack of credit adjustment. There is, however, always a possibility that international capital assistance could be acquired in this area to overcome this potential problem.

It should not be overlooked that the BOR has to contribute a portion of the capital to the international development programs that will have to be met (running around US$ 1 million a year for the Plan Agropecuario).* The BOR should not have any difficulty in meeting these demands, however, and these loans should generate considerable BOR deposits and savings that can be used to expand agricultural credit.

Given its record and the fact of its political orientation, there is good reason to believe that if the political leaders of Uruguay as a matter of policy decide that the BOR shall make the needed rural credit available, it will be forthcoming particularly if it stems from adoption of production-increasing technology. If the BOR fails in this effort, it is more likely to be from an administrative breakdown than a credit policy failure.

* Credit demand in the livestock area will likely be depressed until livestock prices recuperate.

INITIAL QUESTIONNAIRE

1. Name and address of applicant.

2. New or existing company.

3. When was business established (in case of new activity, give estimated date of (a) formation of the company, and (b) initiation of production).

4. Purpose of Activity, principal products, and brief description of physical facilities.

5. Names and nationalities of principal shareholders/sponsors (please include curriculum vitae of principals).

6. Name(s) of key management (please include curriculum vitae with emphasis on experience/background in applicant's principal activity).

7. Present total equity.

8. Present total debt:
   (a) less than one year; maturities, interest rates.
   (b) more than one year; maturities, interest rates.

9. Amount requested from Project
   Debt
   Equity
   Other (describe)

10. Projected use of funds.

11. Total cost of project.

12. Source of balance of funds.

13. Market:
   (a) location
   (b) total present annual sales (volume and dollars)
   (c) historical and projected annual growth of market
   (d) estimated percentage of total market served by applicant according to product line
   (e) estimated total annual sales after completion of this project
   (f) estimated percentage of total market served by applicant according to product line, after completion of this project.
   (g) principal competition

14. Names of all banks with which relationship exists (include personal accounts of sponsors; as well as corporate accounts); describe nature of the relationship.

15. A brief summary of the opportunities and risks this project represents.

Please enclose most current audited balance sheet and income statement and audited statements for three previous years of operation, or performa statements in case the project is a new one and the company is not yet in operation.

Project Assessment Form for AID Loan No. ______.

A. The Borrower

1. Name. . . . .
2. Location. . . . .
3. Current activity. . . . .
4. Address of enterprise . . . .
5. Total assets. . . . .
6. Annual sales. . . . .
7. Net worth . . . .

B. Eligibility requirements

	Yes	No
1. Project involves financing (must not be any of the following:)		
a. meat or meat-packing facilities	____	____
b. fisheries or fish-processing activities	____	____
c. textile manufacture	____	____
d. shoe manufacture	____	____
e. manufacture or marketing of alcoholic beverages	____	____
f. wool processing or manufacture	____	____
g. leather and leather products processing	____	____
h. purchase of property owned by the Government of Uruguay or instrumentality thereof	____	____
2. Impact on small and medium farmer: (must be at least one of the following:)		
a. sizeable number of jobs created by project	____	____
b. small and medium farmers contribute over 50% of inputs to project	____	____
c. project creates additional production alternatives for small and medium farmers	____	____
d. project creates additional marketing alternatives for small and medium farmers	____	____
e. project creates additional income benefits for small and medium farmers	____	____

	Yes	No
f. project includes technical assistance, supervised credit, and/or inputs to small and medium farmers supplying enterprise	____	____
g. project provides services to small or medium farmers	____	____
h. project provides essential inputs to enterprises which utilize substantial raw material supplied by small and medium farmers	____	____
3. Export orientation: Enterprise (must be one of the following:)		
a. currently exporting over 50% of production	____	____
b. currently exporting less than 50% of production, but prospects for increased exports are good	____	____
c. has interesting export prospects if equipment is modernized	____	____
d. is new enterprise whose production will be principally export oriented		
(i) at the outset	____	____
(ii) after filling existing domestic demand	____	____
e. provides necessary services of inputs to enterprises which comply with one of criteria a-d	____	____
f. provides necessary services to farmers producing for export	____	____
4. Enterprise		
a. utilizes normal agricultural raw material which has been traditionally produced in reasonable volume	____	____
b. involves minimum packaging costs and complexity	____	____
c. utilizes uncomplicated technology	____	____
d. maximizes utilization of existing facilities	____	____
e. complements existing facilities	____	____
f. involves uncomplicated marketing	____	____
g. will operate effectively within existing limitations	____	____
h. complements the domestic market	____	____

		Yes	No
i.	receives no excessive protection	___	___
j.	exhibits good management	___	___
k.	is solvent	___	___
l.	has internal rate of return greater than 10%	___	___
m.	utilizes over 50% domestic resources	___	___
n.	contributes to improved income distribution	___	___
o.	contributes to integration with neighboring countries	___	___
p.	contributes to production of basic inputs for other agri-industries	___	___

C. Areas of intended impact of sub-project

Impact area	Description of nature of effect to be produced	Baseline data and quantative indicators - estimated outputs or changes Yr. 1 2 3 4 5	Source of data and methodology of collection
1. Target group (small & medium farmers) benefit incidence			
a. employment -direct (as % of total employment)			
b. income -salaries -other (benefits) of total paid			
c. increased production/ productivity -increase in farm production -new methodology imparted -higher skills introduced			
d. increased local value added			
e. other (specify)			
2. Agri-industrial infrastructure development			
a. new or expanded market development			
b. new, non-traditional product development			
c. removal of constraints/ bottlenecks			
d. other (provide services to agri-industries, etc.)			

Impact area	Description of nature of effect to be produced	Baseline data and quantative indicators - estimated outputs or changes Yr. 1 2 3 4 5	Source of data and methodology of collection
3. Macro-economic benefits			
a. increased value added- regionally nationally			
b. net foreign exchange earnings			
c. medium-longer term agri-industry sector growth possibilities			
d. increased overall employment			
e. other			

D. Summary of Financial Data

1. Requirements

a. Projected use of funds: modernization ____________, improvement _________, establishment of new enterprise_________, expansion of present line of production _________, expansion into new product line _________

b. Amount of Proposed Investment

(1) proposed loan ___________
(2) self-financing___________
(3) other sources____________
(4) total____________________
(5) foreign exchange_________
(6) local costs______________

2. Projected rate of internal return over 10 years (or indicate alternate number of years)____

3. Number of years required to recover investment_____________

4. Principal anticipated markets

a. international (specify)____________________________
b. domestic______________________________________

E. Indicators of Project Viability

Indicator	Yes	Yes, with Qualifications	No	Not Relevant
1. Provision of effective management for the project is now available or is assured in the project design.				
2. Enterprise or Cooperative manages its financial affairs well and is a good risk to meet its obligations.				
3. Working capital required by enterprise or cooperative is assured.				
4. Project has been determined to be of economic scale.				
5. Adequacy of supply of raw materials and other inputs required has been demonstrated.				
6. An effective market demand at level of production contemplated and at a satisfactory price has been demonstrated.				

	Yes	Yes, with Qualifications	No	Not Relevant
7. Export potentialities have been adequately investigated.				
8. Project has been determined following consideration of alternative investment options.				
9. Principal risk factors have been identified and satisfactorily considered.				
10. Feasibility study has been reviewed by available technical experts with no adverse reactions.				

Explanation of negative and qualified responses ______________________

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F. Project Description and Justification