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PD-AAD-832-A1

COLOMBIA

PRIVATE INVESTMENT

FY 64-75

PUBLIC SAFETY ADMINISTRATION PROJECTS (700 PURPOSE CODES)

NO ABSTRACT ENTERED IN THE DIS SYSTEM

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PD-AAD-832-B1

514-116

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

UNCLASSIFIED

AID-DLC/P-236
Revised June 15, 1964

MEMORANDUM FOR THE DEVELOPMENT LOAN COMMITTEE

SUBJECT: Colombia - Banco de la Republica (Private Investment Fund)

Attached are revised pages to be inserted in the loan paper for this project.

The recommendations for authorization of a loan in an amount not to exceed $10,000,000 to the Banco de la Republica to assist in financing the costs of sub-loans by the Private Investment Fund (PIF) for industrial, commercial and agricultural projects, and to assist in financing the United States dollar costs of technical assistance rendered in connection with the loan were discussed by the Development Loan Staff Committee at its meeting on June 8, 1964. These revisions were made in accordance with the discussion at that meeting.

A telephone poll was concluded on June 10, 1964 to secure the advice of the Development Loan Committee on this proposal.

Helen E. Nelson
Secretary
Development Loan Committee

Attachments: (Revised)
- Summary and Recommendations
- Project Analysis, pp 3, 13, 27, 34, 44-45, 47-48
- Annex I, p 5
- Draft Loan Authorization, ANNEX III

Previously Distributed:
- Summary and Recommendations
- Project Analysis
- Annexes I-III

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AID-DLC/P-236
June 3, 1964

COLOMBIA - BANCO DE LA REPUBLICA
(PRIVATE INVESTMENT FUND)

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COLOMBIA - BANCO DE LA REPUBLICA (PRIVATE INVESTMENT FUND)

SUMMARY AND RECOMMENDATIONS

1. Borrower: Banco de la Republica, the Central Bank of Colombia which administers a Private Investment Fund (PIF) created in February 1963, as a result of recommendations by the IBRD and Panel of Nine, to provide long-term financing to the private sector with special emphasis on the expansion of export production. PIF resources consist of the peso proceeds of AID program loans as well as external credits designed to finance projects presented by the ultimate borrowers to the commercial banks and investment corporations (financieras).

2. Amount: Up to $10 million for procurement of goods and services in the U.S.

3. Total Cost of Project: Proposed loan complements the equivalent of $30 million in pesos already allocated to PIF from AID's 1963 program loan, the equivalent of another $15 million in pesos to be made available from AID's 1964 program loan, a $3 million IDB loan and $1.4 million credit from the Netherlands as well as contributions of at least 30% of the cost of individual projects by the ultimate borrowers and/or the intermediate credit institutions. In addition, a $10 million IBRD loan to the PIF for exclusive use by the financieras is under discussion and other credits from European countries and Japan are being sought. The total cost of projects to be partly financed by the PIF is likely to exceed the equivalent of $60 million a year during the next two years when the proposed loan is to be disbursed.

4. Background: During its first year of operation, the PIF has proved a very effective mechanism for channeling the peso counterpart of external credits into long-term financing of the private sector. By April 30, 1964, the Banco de la Republica's (BOR) Board of Directors had approved 70 loans with a total amount of 327.9 million pesos (equivalent to approximately $36.9 million) for projects presented by the commercial banks and financieras on behalf of the ultimate borrowers.

The PIF is being operated subject to policies and procedures which assure a measure of "appraisal" banking on the part of the intermediate institutions in analyzing, approving and monitoring sub-loans. (See Resolution 11 - Annex II).

The BOR, with its experienced staff and unique knowledge of the credit-worthiness of virtually all potential borrowers, studies closely the proposed sub-loans to assure that only high priority projects in the areas of export production, import substitution and the elimination of bottlenecks to development are financed and that projects are executed effectively.

PIF resources have thus far been made available to the intermediate credit institutions at 4% interest and relent to the ultimate borrowers at interest rates of from 8-10% per year at varying maturities of from 3-10 years. The intermediate institutions assumed the credit risks of sub-loans.

In the light of PIF's operations to date, there is every indication that it will be able to use effectively in the future an increasing volume of both foreign exchange and peso resources. However, apart from relatively small loans from the Inter-American Bank and the Netherlands, it has not yet attracted foreign exchange resources to complement the peso proceeds from AID's program loans. Available evidence suggests that a small portion of the peso proceeds made available to the PIF thus far is being used by PIF borrowers to buy foreign exchange to acquire third country goods and services abroad which is clearly undesirable both from the point of view of the U.S. balance of payments situation and the U.S. commercial position in Colombia. At the same time, it is apparent that many borrowers from the PIF are financing the foreign exchange component of their projects by having recourse to suppliers' credits, which are very short term and carry no grace period; the excessive use of such short-term credits constitutes one of the most serious aspects of Colombia's present balance of payments situation.

In the light of the these facts, USAID together with AID/W staff members, has reviewed the Fund's policies and operating procedures with the Colombian authorities. As a result of these discussions, a number of understandings concerning future PIF policies have been reached. Among the most significant of these understandings is agreement that the future peso proceeds of AID program loans made available to the PIF are to be used only for local costs financing, while the foreign exchange portion of PIF projects is to be financed increasingly by foreign exchange credits specifically designed for this purpose, such as the proposed loan and that peso loans are to be denied borrowers that propose to utilize foreign suppliers' credits on unsuitable terms. (See Section IV.C)

5. Description of Project: The proposed loan is designed to cover part or all of the foreign exchange cost of high priority projects financed by the Private Investment Fund through its operating arms: i.e. the commercial banks and financieras. The money will be reloaned in accordance with the policies and procedures set forth in Resolution 11 of the Bank of the Republic (See Annex II) and the understandings concerning these matters reached between the Colombian authorities and AID. (See Section IV)

Sub-loans financed by the proposed loan will be limited to a maximum of 70% of the total cost of projects, will cover only procurement of goods and services in the United States, will not be used to finance working capital needs, will carry interest rates of 8-10 percent and maturities of from 3 to 15 years and will not exceed $500,000 except in cases where the Export-Import Bank indicates that it is not interested in financing sub-loans in excess of such amounts. The interest rates at which the PIF relends the loan funds to the intermediate credit institution and which the latter charge the ultimate borrowers are likely to be increased following the completion of a study of all development lending interest rates by the Colombian Monetary Council and the approval of the necessary legal changes by the legislature. The new top limit for the interest on sub-loans is likely to be 12-14 percent for import substitution projects and those designed to overcome domestic shortages, while projects to expand export production are to continue to be financed at interest rates of 8-10%. The BOR which administers the PIF is to furnish AID with detailed periodic reports on the use of the loan funds, of the peso proceeds of AID Program loans made available to the PIF as well as the general operations of the

Fund. A full joint review of PIF operations is to be conducted at least once a year by AID and the borrower.

It is proposed to make the loan to the Bank of the Republic for a term of 15 years, including a 5-year grace period, at a 5½% interest rate. These terms are in line with those proposed by the IBRD for its loan to the financieras via the PIF, are slightly more favorable than the terms of the existing IDB loan to the PIF (12 years, 2 years' grace at 5 3/4%), but harder than the reported terms of the Dutch credit to PIF (15 years, interest rate 4½% or 5%, depending on money market conditions in the Netherlands). At the same time they are broadly in line with those which the Export-Import Bank would be likely to apply if it were to make a loan for the PIF. In view of Colombia's balance of payments problem involving relatively heavy debt service payments during the next few years, the two step procedure is contemplated, i.e. the GOC will be given the option of receiving repayment from the Borrower in pesos and repaying AID in 30 years, following a 10-year grace period, with interest at 3/4% during the grace period and 2% during the repayment period. The Government's option to use the two step procedure is to be open during the first year of the loan because the Government's authorization to contract external debt is almost fully used up and its enlargement by the Colombian Congress will require considerable time.

The proposed two-step procedure will lead to the creation of an interest rate spread as well as a spread between the scheduled repayment by the Bank of the Republic (for the PIF) and the GOC. The interest rate spread might be invested by the Government in readily liquid assets to service as a special reserve against the exchange rate risk. The "principal" spread would be utilized by the GOC with the agreement of A.I.D. for development financing, including loans through the Private Investment Fund.

6. **Justification of Proposed Loan**: Enlargement of the PIF's resources by means of the proposed AID loan, and the changes in some of the Fund's policies and operating procedures, which will be a major by-product of the proposed additional financing of the PIF, are important to the achievement of such priority goals of the U.S. assistance effort in Colombia as:

(1) Financial balance (including solution of the balance of payments problem) at a level permitting accelerated economic growth and social progress;

(2) A more diversified and productive agricultural sector which will lead the way in the export drive; and

(3) Provision of increased stimuli to guide Colombia's vigorous private sector into activities of prime program priority.

The proposed loan appears especially justified for the following more specific reasons:

(1) It will enlarge the PIF's resources for long-term financing, especially for export production.

The size of the proposed loan to be disbursed over a 2 year period appears appropriate in the light of the fact that subloan approvals through the Private Investment Fund mechanism exceeded the equivalent of $24 million during CY 1963 and, according to careful estimates made by the Bank of the Republic's staff are likely to exceed $36 million equivalent during CY 1964 and at least the equivalent of $40 million during CY 1965.

(2) As a result of the proposed loan an increasing portion of the foreign equipment and supplies of the projects which the PIF helps finance will be bought on longer terms much more appropriate from the point of view of Colombia's balance of payments than seems to have been the case up to now. According to the information available, a major portion (perhaps as much as 20 million dollars) of the total foreign exchange cost of PIF projects has, up to now been financed by means of supplier's credits, many of which are short-term (2-5 years) and have no grace periods.

(3) By providing a ready source of dollar exchange for procurement in the U.S. and through the provision that the use of peso proceeds of AID Program Loans is to be restricted to local cost financing, the new loan will help assure that the PIF's peso resources are used for the financing of local costs and not, except for limited off-the-shelf procurement, for the acquisition of third country goods and services. The latter is clearly undesirable from the point of view of the U.S. balance of payments and the U.S. commercial position in Colombia.

(4) PIF borrowers will be able to secure equipment and services needed to carry out their projects in the United States on suitable terms and without incurring the exchange risk since the latter will be assumed by the Bank of the Republic for the account of the Government. AID financing through the PIF is thus likely to result in <u>additional</u> U.S. exports to Colombia.

(5) The proposed loan is likely to constitute powerful pressure on other potential lenders, such as the European countries and Japan to make funds available, on suitable terms to the PIF for foreign exchange and, whenever possible, local cost financing.

7. <u>EXIMBANK Clearance</u>: Export-Import Bank on May 1, 1964 agreed to AID consideration of the proposal with the understanding that all applications over $500,000 which have been approved by the Colombian authorities be referred to the Export-Import Bank for an expression of the Bank's interest in considering such applications directly. The IDB has already granted a $3 million credit to cover the foreign exchange cost of PIF financed projects and IBRD is discussing with the Colombian authorities the possibility of a $10 million loan to the PIF for use by the financieras.

8. <u>Views of Country Team</u>: The USAID/Embassy in Bogota considers this loan as of very high priority in terms of U.S. assistance objectives in Colombia.

9. Statutory Criteria: The statutory criteria of the Foreign Assistance Act have been met (See Annex I for details).

10. Special Terms and Conditions: The special terms and conditions to govern the utilization of the proposed dollar loan as well as future releases of the peso proceeds of AID Program loans are spelled out in Section IV. They are to be incorporated in the loan agreement, implementation documents as well as letters of agreement governing peso releases.

11. Issues: None.

12. Recommendations: A loan of up to $10 million to be made to the Banco de la Republica subject to the terms set forth below:

a. Interest and Terms of Repayment. Borrower shall repay the Loan to A.I.D. in United States dollars within fifteen (15) years from the first disbursement of the Loan, including a grace period of not to exceed five (5) years. Borrower shall pay to A.I.D. in United States dollars on the disbursed balance of the Loan interest of five and one-half ($5\frac{1}{2}$) percent per annum.

b. If prior to the end of the first year subsequent to signing of the Loan Agreement, the Government of Colombia so elects, the Borrower shall fulfill its dollar obligation under the loan by paying to Government in the currency of Colombia the equivalent, determined as of a time and in a manner satisfactory to A.I.D., of the United States dollar amounts payable to A.I.D. under (a) above and in such event the Government shall pay to A.I.D.:

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

(a) All interest immediately upon receipt subject to Government's right to retain all payments in excess of three-quarters of one (3/4 of 1) percent per annum during a grace period of not to exceed ten (10) years from the first disbursement under the loan ("Government grace period") and all payments in excess of two (2) percent per annum thereafter.

(b) Principal within forty (40) years, including the Government grace period.

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

c. Equipment, materials and services (except marine insurance) financed by the Loan shall be procured from the United States of America.

d. Not to exceed one hundred thousand United States dollars ($100,000) of the loan may be used to finance the United States dollar costs of technical assistance rendered in connection with the loan.

e. Subloans by the PIF financed by the Loan shall be made in accordance with Borrower's Resolution No. 11 dated February 28, 1963, as the same may from time to time be modified in a manner mutually satisfactory to A.I.D. and Borrower.

f. Borrower and the PIF will make arrangements satisfactory to A.I.D. to strengthen and improve their staff.

g. Except as A.I.D. may otherwise agree, funds directly or indirectly made available to the PIF by the United States of America will not be used for projects which are likely to result in (1) the increased production of agricultural commodities in world surplus other than foods and feeds, (i.e., cotton and tobacco), or (2) the increased exportation of surplus food and feed in world surplus, (i.e., rice, wheat, vegetable oil, citrus fruits and coffee). A.I.D. will reserve the right to add to or delete from the lists of surplus agricultural commodities contained hereinabove in this section. With regard to subloans to textile producers, the Borrower will assure that additional production as a result of AID-financed subloans, will not be exported to the United States of America.

h. Proposed subloans by the PIF in excess of five hundred thousand United States dollars ($500,000) to be financed by the Loan, shall be referred to the Export-Import Bank for possible financing by such Bank.

i. Procedures acceptable to A.I.D. will be adopted by the PIF to deny the resources of the PIF to potential borrowers utilizing supplier credits having terms which are not mutually satisfactory to A.I.D. and Borrower.

j. At least once per year, A.I.D., Borrower and the PIF will review the status of the Loan, lending policies and procedures and such other matters pertaining to the Loan as A.I.D. may request.

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

Project Committee:

Chairman: PGlaessner, LA/CD
Counsel: HAdelman, LA/GC
Asst Director for Programs: KNathan, USAID/Bogota
Loan Officer: HTennenbaum, USAID/Bogota
Program Officer: JDeForrest, USAID/Bogota

SECTION I - BACKGROUND OF PROPOSED LOAN

As a result of recommendations by the International Bank, the Panel of Nine and the Agency for International Development, the Colombian Government in February 1963 established a Private Investment Fund to provide long-term financing of projects for the expansion of production of commodities for export, import substitution as well as the elimination of development bottlenecks. The Fund, administered by the Bank of the Republic, operates through the commercial banks and investment corporation.

By the end of 1963, it had become evident that the Fund was proving to be a flexible and effective instrument for channeling a major portion of the peso counterpart of AID's 1963 program loan into high priority projects, and that it would be able to use effectively in the future an increasing volume of both foreign exchange and peso resources. However, apart from relatively small loans from the Inter-American Bank and the Netherlands, it had not yet attracted complementary foreign exchange resources. Available evidence suggested that a small portion of the peso proceeds of the AID program loan was being used by PIF borrowers to buy foreign exchange to acquire third country goods and services abroad which is clearly undesirable both from the point of view of the U. S. balance of payments situation and the U. S. commercial position in Colombia. At the same time, it was apparent that many borrowers from the PIF were financing the foreign exchange component of their projects by having recourse to suppliers' credits, which are very short term and carry no grace period; the excessive use of such short-term credits constitutes one of the most serious aspects of Colombia's present balance of payments situation.

In the light of these facts, USAID together with AID/W staff members reviewed the Fund's policies and operating procedures with the Colombian authorities in the spring of this year. As a result of these discussions a number of understandings concerning future PIF policies were reached. Among the most significant is an agreement that in the future peso proceeds of AID program loans made available to the PIF are to be used only for local costs financing, while the foreign exchange portion of PIF projects is to be financed increasingly by foreign exchange credits specifically designed for this purpose, such as the proposed loan of up to ten million dollars ($10,000,000). Both the Finance Minister and top management of the Bank of the Republic have expressed keen interest in the proposed loan, which is warmly supported by the CT as of very high priority in terms of U. S. assistance objectives.

SECTION II - THE BORROWER

The Banco de la República, the Colombian Central Bank, is to be the borrower. It would guarantee repayment of the proposed loan for the Private Investment Fund. The exchange rate risk will be assumed by the Colombian Government under the terms of special legislation governing the Bank's foreign exchange operations.

The Bank of the Republic was established in 1923 as a result of the recommendations of a technical Mission headed by Professor Kemmerer. Like the other Central Banks established as a result of "Kemmerer" Missions, its capital structure, its "autonomous" status vis-a-vis the Government and some of its basic functions and policies were influenced by the salient features of the U.S. Federal Reserve System.

As far as the Bank's capital is concerned, until 1951 it was owned 50% by the Government which held all Class A shares, while the Class B, C, D and E shares were in the hands of the national banks, foreign banks, private individuals and official banks, respectively. The sale of the Government's shares in the open market, in 1951, left ownership of the Bank entirely in the hands of the banking system and the public. Under the law creating the Bank, member banks are obliged to own shares equivalent to 15% of their paid-in capital and reserves, resulting in a continuous increase in the Bank's capital. As shown in Table I, on December 31, 1963 the Bank's capital and reserves totalled 236 million pesos (equivalent to $23.6 million at the "free" exchange rate of 10 pesos per dollar). The paid-in capital amounted to 74.3 million pesos, of which 63% was contributed by Colombian private commercial banks, 27% by official and semi-official banks such as the Livestock and Coffee Banks, 9% by the foreign banks and less than 1% by private individuals.

The Bank of the Republic's policies have until recently been entirely determined by its Board of Directors which also selects top management. The Board consists of 10 members, of which 3, including the Minister of Finance, represent the Government, 3 are elected jointly by the Colombian and foreign commercial banks, while one each represents the National Federation of Coffee Growers, the official banks, the Societies of Farmers and Cattlemen and the Chambers of Commerce.

Under the special powers granted the Government in the summer of 1963 (Law 21 of 1963, Article V) the Colombian Government set up a monetary board consisting of the Ministers of Finance, Development and Agriculture, the Chief of the Planning Department and the Manager of the Bank of the Republic. This monetary board is charged with studying and determining monetary, exchange and credit policies which previously had been the responsibility of the Bank's Board of Directors. It is clear from the Parliamentary discussions that preceded the adoption of this measure and the controversy that surrounded its implementation, that the Monetary Board was created because of the belief that there had been undue commercial bank influence on major policy decisions in the areas of credit and exchange rate policy. While the Board of Directors of the Bank of the Republic has thus been deprived of some of its broad powers of policy making, the Bank remains the operating entity through which Central Bank policies are carried out.

In its 41 years of operations the Bank of the Republic's staff has acquired broad experience in carrying out every type of credit and foreign exchange operation not only with the commercial banks but also with the public and with such financial entities as the "financieras" (investment banks). As a byproduct of these operations, the Bank's general Credit Department has unusually complete information on the credit worthiness and economic-financial situation of virtually every significant enterprise or farm in the country. In addition, the Bank has an excellent Economic Studies Department staffed by economists, engineers and accountants, many of whom are U. S. educated or trained. This Department contains a development lending group which has for some years been in charge of appraising requests for medium and long-term agricultural and industrial loans which the Bank of the Republic is charged with financing through the banks and financieras under a number of special laws and regulations. The Bank was thus in a very favorable situation to assume the administration of the Private Investment Fund upon its creation in February 1963.

As far as the Bank of the Republic's financial situation is concerned, as shown in Table I, at the end of 1963 its total assets amounted to the equivalent of $846 million and its net worth to the equivalent of $23.6 million. Among the assets are the country's official gold and foreign exchange reserves and a loan portfolio which consists primarily of advances and rediscounts for the commercial banks and special longer term credits (including the PIF loans) to these banks and to the investment banks. The special foreign exchange account shown on the assets side of Table I merits some comment. It was set up in accordance with certain provisions of Law 7 of 1935 and Law 67 of 1938 according to which any profit or loss resulting from the Bank's exchange operations is carried to a special government account until such time as the full convertibility of Colombia's bank notes into gold is re-established. In other words, the Colombian Government will assume the exchange rate risk on the proposed AID loan.

As shown in both Tables 1 and 2, finally, the operations of the bank during the last three calendar years have continued to be profitable with annual net profits well in excess of U. S. $1 million. Given the excellent international reputation of the Bank of the Republic, the proven management ability of its staff and its strong financial position, there can be little doubt of its ability to repay the proposed loan.

TABLE I

CONSOLIDATED BALANCE SHEET OF THE BANK OF THE REPUBLIC

AS OF DECEMBER 31 1961, 1962, and 1963
(in million pesos)

ASSETS	1961	End of 1962	1963
Gold and Foreign Exchange	412	1,084	1,176
Cash	10	10	10
Loans and Discounts			
To Commercial Banks	930	1,119	1,452
To National Government	42	63	58
To other official entities	281	285	253
To investment banks, cooperatives, livestock banks, etc.	764	614	525
Total Loans and Discounts	2,017	2,081	2,288
Investments	969	2,173	2,051
Subscriptions to International Credit Institutions	243	935	941
Special Foreign Exchange Account	-	444	539
Other Assets	655	1,305	1,454
Total Assets	4,306	8,032	8,459

LIABILITIES	1961	End of 1962	1963
Bank Notes in Circulation	1,914	2,214	2,661
Deposits			
Commercial Banks	374	907	564
National Government	170	645	435
Importers and Exporters	650	748	1,019
Other	72	100	49
Total Deposits	1,266	2,400	2,067
International Monetary Fund	127	653	1,089
Other Creditors	132	564	250
Total Demand Obligations	3,439	5,813	6,067
Longer Term Obligations			
Foreign Banks	350	1,105	1,040
International Credit Institutions	178	822	805
Private Investment Fund	-	-	210
Other	92	9	8
Total Longer Term Obligations	620	1,936	2,063
Capital and Reserves	201	199	236
Half-yearly Profits	5	5	6
Other Liabilities	41	79	87
Total Liabilities	4,306	8,032	8,459

Source: Bank of the Republic Monthly Bulletin

TABLE II

BANK OF THE REPUBLIC

Annual Profits and Profit Distribution

1961, 1962 and 1963

(in thousand pesos)

	1961	1962	1963
Payments to State for Right of Note Issue	638	638	638
Dividends	7,233	7,594	8,835
10% for Legal Reserve Fund	977	996	1,136
5% for Pension Fund	488	498	568
Social Security Account	429	237	150
Total Annual Net Profits	9,765	9,963	11,327

Source: Bank of the Republic, Annual Reports

SECTION III - PRIVATE INVESTMENT FUND

A. Origin

The Bank of the Republic established the Private Investment Fund on February 28, 1963 by means of Resolution No. 11 as a source of long term credit for industrial and agricultural development, especially for export production. The Fund's origin and economic character are well described in the first and second article of Resolution No. 11 which read as follows:

"Article 1.-In accordance with the recommendations of the Mission of the International Bank for Reconstruction and Development and of the ad-hoc Committee of the Alliance for Progress, which studied Colombia's General Program of Social and Economic Development; and in implementation of the provisions of Article 2 of Decree 756 of 1951, the Private Investment Fund (PIF) is hereby established within the Bank of the Republic. The PIF will possess different characteristics and management procedures from those employed for the usual quotas of credit in the Bank.

"Article 2 - The Private Investment Fund will consist of the peso proceeds generated by foreign loans and of the foreign exchange resources available to the "PIF" from foreign credits, or from other sources, which the Bank of the Republic agrees to accept for the "PIF".

"The Fund will be employed for financing investments exclusively in the private sector, which will significantly contribute to the country's economic development, with particular attention given to investments which contribute to the diversification and promotion of exports."

It may be worthwhile to add that the decision on the part of AID to agree that a substantial portion of the peso counterpart of the 1963 program loan be made available to set up the PIF was heavily influenced by three factors:

1. The strong endorsement of the concept of such a Fund by the International Bank and the Panel of Nine;

2. The fact that one of the objectives of the program loan was to support an exchange reform and internal stabilization effort on

the part of Colombia which was expected to involve a substantial degree of credit restraint. Experience in other countries indicated that in the course of stabilization efforts credit for the private sector and particularly longer term credit for the expansion of existing or creation of new enterprises, was likely to be rather severely reduced. In view of the vigor of Colombia's private sector, this would be very unfortunate from the point of view of the country's achieving a satisfactory rate of growth. The creation of the PIF and its administration through existing credit institutions of proven capacity and reputation promised to obviate a good deal of this danger.

3. It appeared particularly appropriate that AID support a financial mechanism dedicated almost exclusively to the financing of projects for the expansion of export production or import substitution since Colombia's structural balance of payments problem is one of the most significant factors tending to impeded self-generating growth of the Colombia economy without the need for continuing sizable outside assistance.

B. Operating Policies and Procedures

The operating policies of the PIF are spelled out in considerable detail in Resolution No. 11 which is reproduced as Annex II of this Capital Assistance paper. In its first part, the Resolution provides that the Fund is to utilize either foreign exchange credits or the peso counterpart of program (general imports) loans to make medium and long-term loans to the private sector through intermediate credit institutions such as the commercial banks and the financieras. In making such loans top priority is given to investments designed to expand export production. Import substitution and the elimination of critical bottlenecks are given secondary priority. Loans are to be for only a portion of the total project costs. Working capital needs and the purchase of land, building and mining properties are not, under present policies, eligible for financing from PIF resources.

Resolution No. 11 further describes the obligations and functions of the intermediate credit institutions, which make the sub-loans to the ultimate borrowers, the procedures to be followed by these institutions as well as the functions of the Bank of the Republic in administering the Fund. As a study of the Resolution will show, the procedures outlined there are very well thought out. For example, the financial intermediates are specifically enjoined to evaluate loan applications and projects from the point of view of their technical, economic and financial soundness and in terms of their desirability from an over-all national point of view and not merely on the basis of commercial criteria. In other words, in making loans for which they hope to receive funds from the Private Investment Funds, the commercial banks and financieras are enjoined to engage in "appraisal" banking. Before agreeing to endorse a loan application, the intermediate credit institutions are to make sure that the applicant is fully using his own resources and is making every effort to secure funds from normal credit sources, both domestic and foreign. At the same time, the intermediate credit institutions are directed to make end-use checks, to keep informed on the general situation of the borrowing firm and make periodic reports to the Bank of the Republic. In order to enable them to carry out these functions which are quite different from those normally executed by commercial banks, Resolution No. 11 suggests that both in the preparation and analysis of priority projects and in order to carry out satisfactory end-use checks "the intermediates themselves offer services, or contract the services of experts".

It is also interesting to note that among the guaranties which the intermediate credit institutions are instructed to require from the ultimate borrowers is the surrender of foreign exchange from exports made possible as a result of the PIF loans. In actual practice, appropriate clauses have been included in subloan agreements between the intermediate credit institutions and ultimate borrowers giving the intermediate credit institutions the right to call or accelerate the subloans if the borrowers do not live up to their commitment to increase their exports substantially. Finally, it should be observed that under the procedures laid down in Resolution No. 11, the intermediate credit institutions, whether commercial banks or financieras, assume the full credit risk of subloans so that in the case of defaults the Bank of the Republic can have recourse against them.

Among the functions and operating procedures of the Bank of the Republic, spelled out in Resolution No. 11, it is especially significant that the Bank is authorized to accept and contract foreign credits on satisfactory repayment and interest terms, and that it is charged with maintaining a separate PIF account which is to " constitute a special fund with different characteristics and management from the regular credit quotas which the banks and financing corporations have with the Bank of the Republic." Furthermore, the Bank is charged with repaying the loans made by foreign lenders directly to the PIF and can act as guarantor of such credits. At the same time it is to repay the pesos received as the counterpart of foreign loans to the Colombian Government. Finally, the Bank is enjoined to check on the employment of the PIF resources and to apply the necessary penalities in the case of a misuse of these funds including an immediate calling of subloans and/or the denial of further access to the PIF, penalties which can be exercised both against the ultimate borrowers and, when necessary, against the intermediate credit institutions. Both the intermediate credit institutions and the Bank of the Republic are to publicize the PIF so that its characteristics and objectives become well known both at home and abroad.

As far as loan terms are concerned, Resolution No. 11 spells out the following maximum terms for subloans: Up to five years for loans for agriculture and the cattle industry and up to ten years for industrial type loans. The intermediate credit institutions can grant longer terms, subject to the approval on a case by case basis by the Bank of the Republic. The Bank of the Republic itself makes PIF funds available to the intermediate credit institutions for precisely the same length of time as the terms of the subloans which these institutions extend to the ultimate borrowers.

Resolutions No. 11 instructs the Bank of the Republic to charge a uniform 4% interest rate to the intermediate credit institutions, irrespective of the length of time of the subloan or its purpose. The intermediate credit institutions, in turn, are instructed to relend the funds at the following interest rates: up to 8% on loans with a repayment period of up to three years; at 9% in case of loans with a repayment period of three to five years and up to 10% in the case of loans for more than 5 years. This interest rate scheme is slightly modified in the case of agricultural and livestock loans where interest rates on loans with a repayment period in excess of three years is not to exceed 9%. The interest rates set in Resolution No. 11 are subject to modification "when the country's economic conditions require it and when permissible under Colombian Law". This means in practice that interest rate changes must be approved by the Monetary Board as well as by the Board of Directors of the Bank of the Republic.

C. Operating Record

1. Source of Funds

The PIF has been in operation for just over one year (since April 15, 1963, when the first subloans were approved). During this period the Bank of the Republic has received 210 million pesos (equivalent to $23.3 million at the 9 pesos per dollar of the import rate) in counterpart funds from the 1963 AID program loan. A further 60 million pesos from the counterpart of this loan are earmarked for transfer to the PIF; the transfer of 50 million pesos of this total has just been requested by the Manager of the Bank of the Republic. In addition to the peso counterpart from the 1963 program loan, the equivalent in pesos of up to $15 million from the counterpart to be generated by the 1964 program loans is tentatively earmarked for transfer to the PIF.

Besides these peso resources resulting from AID program loans, the Bank of the Republic has secured a $3 million line of credit from the IDB. This loan carries a two-year grace period and calls for repayment within the subsequent ten years. It bears an interest rate of 5 3/4% and a commitment fee on the undisbursed portions of the loan of 3/4 of 1%. The loan is entirely destined to cover the foreign exchange component of projects presented to the PIF through intermediate credit institutions.

Finally, the Bank of the Republic has been granted a $1.4 million loan by the Netherlands, repayable over 15 years at an interest rate of $4\frac{1}{2}$ or 5% per year depending on money market conditions in the Netherlands. The Dutch loan is available to cover both the foreign exchange and peso portions of projects. Procurement under both the IDB and Dutch loans is possible from any free world source. As of the end of April, the Bank of the Republic had not yet utilized the IDB loan although a loan agreement had been signed and disbursement procedures worked out by the Bank of the Republic and the IDB. According to the latest available information, the Bank of the Republic and the Netherlands authorities have not yet reached a definite agreement on the terms of the loan and no loan agreement has been signed as yet.

The foregoing are the only resources that have thus far become available to the PIF or for which definite commitments have been made by foreign lenders. The Bank is actively discussing with the World Bank a possible $10 million loan which would be destined exclusively for use by the financieras. The terms offered by the Bank envisage repayment within 15 years including a five-year grace period and an interest rate of $5\frac{1}{2}$%. The loan would carry the guaranty of the Government of Colombia which would be expected to assume the exchange risk and would be used by the financieras both for long-term loans to and for equity investments in private companies which have productive projects of high priority. The World Bank loan would cover only the foreign exchange costs of projects including imported materials and spare parts needed for the constitution of initial permanent work capital. Subloans by the financieras above a certain size would require the World Bank's prior approval. It is not yet certain when the negotiations between the World Bank and the Bank of the Republic for this $10 million operation will be concluded.

2. Commitments and Disbursements

The most significant data on PIF's record of operations to date are brought together in Tables 3, 4, 5, 6 and 7. As shown in these tables, in the period from April 15, 1963 to April 30, 1964, the PIF received 118 loan applications from the intermediary credit institutions involving a total amount of proposed loans of 512 million pesos. 70 of these applications have been approved resulting in a total of loan authorizations of 327.9 million pesos while 36 of the applications involving over 90 million pesos in proposed loans have been rejected. Another 12, for a total of 30 million pesos in proposed loans, were under study in the Bank of the Republic at the end of April. The total amount of loans approved was 58 million pesos less than the original proposals because of a strict application by the Bank of the Republic of the policy of not financing more than 70% of the total cost of any one project. As a matter of fact, as shown in Table 4, the 66 projects for which loans have been approved up to April 9, 1964 have a total cost more than four times as great as total PIF financing. It is significant to note that even though the 66 projects apparently involve a foreign exchange cost of about 42 million dollars only a little over 5 million dollars of these costs have been financed by the PIF making pesos available to sub-borrowers who, in turn, used them to acquire goods and services abroad. Well over 80% of PIF loans appears to have served to finance the local costs of the various projects.

Of the 70 loans approved as of the end of April 1964, 23 involving just one-third of total funds lent thus far has been for export production while 35 loans absorbing almost 47% of the total funds made available have been for import substitution. The balance of the loans have been made for projects to overcome specific shortages or for those that have for their economic justification a combination of the export production, import substitution or bottleneck breaking criteria.

As far as the economic destination of loans is concerned, six of the projects, involving almost 28% of total loan funds made available went for the expansion of sugar production while 9 involving 16% of loan funds financed chemical projects. The production of paper, vegetable oils (including the planting of African palms) and textiles together accounted for another 23 projects and absorbed another 23% of total loan funds. A great number of smaller but significant projects in both industry and agriculture make up the balance, as shown in Table 8.

TABLE III

Private Investment Fund

Summary Data on Loan Authorizations as of April 23, 1964
(in thousand dollars converted from
pesos at the "free" exchange rate of 10 pesos per $)

Loan Range	No.	%	$US Dollars	%
Under 50,000	9	13	285	0.9
50,000-149,999	13	18	1,038	3.2
150,000-299,999	17	24	3,323	10.1
300,000-499,999	6	9	1,800	5.5
500,000-999,999	5	7	2,465	7.5
1,000,000-1,999,999	9	13	9,687	29.5
2,000,000 and over	11	16	14,195	43.3
	70	100	32,793	100.0
Economic Justification				
a) Export	23	33	10,849	33.1
b) Import Substitution	35	50	15,274	46.6
c) Specific Shortage	3	4	1,115	3.4
d) Export and Import Substitution	6	9	3,995	12.2
e) Export and Shortage	3	4	1,560	4.7
	70	100	32,793	100.0
Type of Production				
a) Sugar	6	9	9,060	27.6
b) Chemicals	9	13	5,165	15.8
c) African Palm	7	10	3,800	11.6
d) Paper	4	6	3,643	11.1
e) Vegetable Oil	5	7	927	2.8
f) Textiles	7	10	2,136	6.5
g) Banana	3	4	350	1.1
h) Miscellaneous	29	41	7,712	23.5
	70	100	32,793	100.0

Source: Bank of the Republic

TABLE IV

Summary Data concerning Projects for which PIF loans have been approved as of April 9, 1964

	(in million pesos)	(in million dollars) 1/
Total Cost of 66 Projects (including working capital)	1,349	137.4
Total Peso Cost	952	95.2
Total Foreign Exchange Cost	397	42.2
Total of 66 PIF Loans Approved	302	30.6
PIF Loans: Peso Component	252	25.2
PIF Loans: Foreign Exchange Component	50	5.4
PIF Loan Disbursements (as of April 28, 1964)	119	11.9

Note: Peso components of projects and PIF loans converted at free rate of 10 pesos to the dollar. Foreign Exchange Component of PIF loans computed at 9 peso per dollar rate at which borrowers acquire foreign exchange to finance equipment imports. Total Foreign Exchange Cost converted at free rate (10 pesos per dollar), in case of foreign investments and suppliers credits, at import rate (9 pesos per dollar) in case of direct purchase by borrowers.

Source: Bank of the Republic

TABLE V

Private Investment Fund
Summary of Operations During
Period from April 15, 1963 to April 30, 1964

	No.	Amount (In million pesos)
Loan Applications Received	118	512.0
Loan Approvals	70	327.9
Loan Rejections	36	94.4
Loan Applications Under Study	12	31.7
Reduction in amount of loans approved compared with applications		58.0
Actual and Projected Disbursement of Approved Loans:		
1963 (actual)		64.9
1964		205.5
1965		54.0
1966		3.5
Total		327.9

TABLE VI

Terms of 66 Subloans Financed With
Funds from the Private Investment Fund
Through April 9, 1964

Terms Years	Interest Rates 8%	9%	10%	Totals at each Term
3	1	1	-	2
4	-	1	-	1
5	-	27	2	29
6	-	-	4	4
7	-	-	3	3
8	-	-	1	1
9	-	-	-	-
10	1	2	23	26
Totals at each int. rate	2	31	33	66

Source: Bank of the Republic

TABLE VII

PRIVATE INVESTMENT FUND

Loans Approved as of December 31, 1963 by Size of Firms 1/

Capital of Companies (in pesos)	No. of Companies	Total Project Cost (thousands of pesos)	Loans Approved (thousands of pesos)	%
0 - 2,000,000	17	49,870	20,089	8.3
2,000,000 - 4,000,000	4	9,021	5,251	2.1
4,000,000 - 6,000,000	3	126,050	26,000	10.8
6,000,000 - 8,000,000	6	73,705	17,509	7.3
8,000,000 - 10,000,000	1	2,220	549	0.2
10,000,000 - 12,000,000	2	66,012	21,800	9.1
12,000,000 - 14,000,000	5	185,840	47,440	19.7
14,000,000 - 16,000,000	4	169,171	33,600	14.0
16,000,000 - 75,000,000	8	528,535	68,692	28.5
	50	1,210,424	240,930	104.0
		100%	19.9%	

1/ Preliminary data

Source: Bank of the Republic

TABLE VIII

Loan Applications Approved by Private Investment Fund
Period April 15, 1963 - April 30, 1964
By Economic Activity

(In million pesos)

	Number of Applicants	Total Amount of Investment Projects	Amount of PIF Loans
Primary Production (Agriculture, forestry and fishing)	15	177.1	45.2
Manufacture and Processing	52	1,224.5	276.6
Foodstuffs	11	407.5	102.1
Textiles	2	6.4	2.4
Clothing and other textile products	1	1.5	0.7
Paper and paper products	4	161.3	36.4
Chemical products	11	397.9	63.8
Non-metallic mineral products	5	55.4	20.7
Metal Products	7	128.1	26.3
Machinery other than electrical	3	8.1	3.7
Electrical machinery	1	10.3	3.0
Printers and related industries	2	3.4	2.2
Other industries	5	44.6	15.3
Transport			
River transport	2	10.1	5.6
Production and distribution of gas for power generation	1	6.7	0.5
Total	70	1,418.4	327.8

Source: Bank of the Republic

It is interesting to note that 39 of the 70 loans approved thus far, accounting for only about 14% of the total volume of loans authorized, were for individual subloans of less than 3 million pesos (equivalent to about 300,000 dollars) which is the "normal" limit for individual loans set in Resolution No. 11. The Bank of the Republic has clearly made full use of the escape clause contained in the Resolution since no less than 11 loans out of 70 absorbing over 43% of total loan funds were for amounts in excess of $20 million pesos (equivalent to $2 million). It should also be noted that of 66 loans for which relevant data were available no less than 22 went to firms which are either wholly or partially foreign-owned, mostly by U.S. investors.

The operating flexibility of the PIF system is reflected in the relatively rapid rate of disbursement which on April 28, 1964 amounted to 119 million pesos, more than one-third of the total loans authorized up to that time.

As far as the terms of subloans financed with resources of the PIF are concerned as shown in Table 6, an overwhelming proportion of subloans have been for 5 years at 9% interest or 10 years at 10% interest.

While information on the size of firms granted PIF loans is incomplete, the preliminary data presented in Table 7 show that at the end of December 1963 over 70% of the total of loans had gone to companies with a capital in excess of 10 million pesos (equivalent to about $1 million).

D. Projected Economic Results of Past Operations

On the basis of the data assembled in Table 9, it appears that the PIF may prove a most valuable instrument in Colombia's efforts to come to grips with its balance of payments problem. As shown there, it is estimated that the projects which the PIF helped to finance during its first year of operations are likely to result in an increase of annual export earnings of about $12 million this year and as much as $25 million by 1968; at the same time the various import substitutions projects financed thus far are estimated to result in annual exchange savings of almost $58 million. Projects for the expansion of the chemical industry are likely to prove most important in terms of replacing presently imported commodities while the expansion of the sugar industry is expected to produce the bulk of new export earnings.

In evaluating the data presented in Table 9 it should be noted that according to World Bank technicians who have been intimately associated with the development of the PIF's operations since the beginning, these projections are conservative in the sense that the applicant's claims of additional exports are supported by evidence of export prospects such as arrangements with foreign importers and relevant market information; moreover the figures quoted in the table represent a reduction of 50% from the applicant's own claims.

TABLE IX

Private Investment Fund

Estimated Value of Imported Commodities Replaced and of Exports Produced by PIF financed Products 1/ as of April 30, 1964

Industrial Group	No. of Loans Approved	Estimated Net Import Substitution (in million dollars)	Exports 1964 (in million dollars)	1965	1966	1967	1968
Agriculture, Forestry and Fishing	15	7.4	0.3	0.6	0.7	0.7	0.7
Agriculture							
Banana	3	-	0.3	0.6	0.7	0.7	0.7
Sugar Cane	1	-	-	-	-	-	-
Cacao	1	0.3	-	-	-	-	-
African Palm	6	7.1	-	-	-	-	-
Mint	1	*	-	-	-	-	-
Cattle							
Sheep Raising	3	*	-	-	-	-	-
Manufacture and Processing	52	50.5	11.6	15.7	19.6	22.0	24.4
Foodstuffs	11	1.6	5.1	7.7	10.6	14.2	16.2
Textiles	2	-	0.9	0.9	0.9	0.9	0.9
Clothing	1	-	0.1	0.2	0.2	0.2	0.2
Paper and Paper Products	4	10.9	-	0.1	0.4	0.4	0.5
Printing	2	-	0.1	0.1	0.2	0.2	0.2
Chemical Products	11	23.9	2.3	2.7	2.7	1.5	1.7
Non-metallic mineral products	5	0.5	-	0.1	0.2	0.2	0.3
Basic metal industries	2	8.8	-	-	-	-	-
Metal Products	5	0.2	1.2	1.6	1.9	1.9	1.9
Machinery other than electrical	3	3.0	0.2	0.5	0.5	0.5	0.5
Electrical Machinery	1	0.1	0.1	0.2	0.2	0.2	0.2
Rubber Products	1	-	*	*	0.2	0.2	0.2
Byproducts of petroleum and coal	1	1.5	-	-	-	-	-
Tobacco	1	-	1.5	1.5	1.5	1.5	1.5
Wood Products	1	*	0.1	0.1	0.1	0.1	0.1
Other Manufactures	1	-	*	*	*	*	*
Transport	2	-	-	-	-	-	-
Public Utility	1	-	-	-	-	-	-
TOTAL	70	57.9	11.9	16.3	20.3	22.7	25.1

* Less than $100,000

1/ The import substitution is in terms of imported commodities to be replaced; the export earnings are deflated around 50% from applicant's own claims.

Source: Bank of the Republic

E. Appraisal of Operating Procedures

Because the Colombian authorities wanted to get the PIF into operation as rapidly as possible, making use of the facilities of the entire financial system, the Fund as organized at present, is essentially a special account administered by the Bank of the Republic. The commercial banks and Financieras act as operating arms of the System. By means of a detailed guideline furnished the borrowers and through policy guidance provided by the Bank of the Republic, the intermediate credit institutions have begun to engage in a degree of appraisal banking. In this respect the Financieras quite understandably are generally doing considerably better than the commercial banks, although the latter have in some cases engaged the services of specialized engineers, economists, and accountants on a contract basis and have organized a technical office through the Bankers' Association.

The Bank of the Republic staff seems to do a conscientious appraisal job of proposed projects before submitting them to their Board of Directors for final approval. Applications endorsed by the commercial banks or Financieras are first examined by the Bank of the Republic's General Credit Department which makes a preliminary finding concerning three aspects of any loan proposed for PIF financing: (i) whether it qualifies generally under the criteria of Resolution No. 11; (ii) whether the borrower is credit-worthy, and (iii) whether the borrower needs the credit in the light of his own availabilities or access to other sources of financing. The application then goes to the special Development Lending Group in the Economic Studies Department, consisting of economists and engineers which conduct a more detailed review and appraisal of the applications. The Bank has also organized an inspection team consisting of an economist, engineer and accountant that checks up on the progress of individual project loans. The loan proposals are finally presented to the Board of the Bank by the Deputy Manager for a final decision.

Aspects involving the negotiation of external financing, making sure that operations conform to conditions agreed upon with foreign lenders, and the handling of foreign funds are the responsibility of the Bank's Foreign Exchange Department.

It is apparent from the above that the group most intimately involved with PIF business is the Special Development Lending Group in the Economic Studies Department, which has excellent staff but is clearly overburdened.

It is the judgment of U. S. AID and AID/W staff members who have examined various aspects of PIF's operations that the appraisal capacity of the intermediate lending institutions (especially of the commercial banks) needs to be improved and that they should be obliged to do a better job in monitoring the loans for which they are responsible to insure that projects are carried out according to plan. At present an undue burden for analysis and follow-up is being thrown on the Bank of the Republic.

An important question concerning the present form of organization of the PIF arises from an appraisal of present operating procedures. Would it be appropriate for the PIF to be transformed into an independent development institution or should at least the PIF functions in the Bank of the Republic be brought together in an independent department? It is the Project Committee's considered view that the transformation of the PIF into an autonomous official development institution is clearly premature and may well be inadvisable even in the long run. Only the Bank of the Republic with its unique knowledge of both the general economic situation and the credit-worthiness of potential borrowers and with its high calibre, experienced staff can be expected to operate a financial system that makes full use of the capacities of the commercial banks and financieras. An autonomous state development bank would have difficulty in securing a staff of comparable capability, would take a long time to build up comparable prestige and would find it infinitely harder to work through private commercial banks and especially the private investment banks which would regard it as an unwelcome official competitor.

As for the concentration of PIF operations into a separate department of the Bank, this would seem to be a question deserving further study as the volume of PIF operations increases. The present arrangement has the obvious advantage that both the operating and overhead costs of the PIF are held to a minimum since specialized personnel in both the Credit, Foreign Exchange and Economic Studies Departments of the Bank handle the PIF operations along with other operations, some of which are fairly similar in nature. On the basis of the evidence up to this time, it appeared to the Project Committee that the outstanding characteristics of the Bank of the Republic's administration of the PIF has been that it has made this complex financial mechnism work quickly and effectively.

SECTION IV - TENTATIVE UNDERSTANDING AND SUGGESTIONS CONCERNING PIF LENDING POLICIES AND PROCEDURES AND THE USE OF THE PROPOSED DOLLAR LOAN AND FUTURE PROGRAM LOAN PESO AVAILABILITIES.

During the review of PIF's operations up to this time conducted by US AID personnel and AID/W staff members, it became evident that some changes of policy and some tightening of procedures might be advisable. It was also considered essential that the Colombian authorities understand that some changes in the use of peso funds derived from AID program loans were desirable from the U. S. point of view and that the proposed dollar loan would be subject to certain conditions. All of these matters were the subject of conversations with the Bank of the Republic's technical staff, the advisors of the Monetary Board and the Minister of Finance. From these conversations a number of tentative understandings and suggestions emerged. These understandings and suggestions together with comments discussing the reason for them are presented below:

A. Suggestions Regarding PIF Lending Policies

1. Interest rates charges to both the intermediate and the final borrower will be lower for export projects than for import substitution or bottleneck breaking. PIF might charge the intermediate credit institutions 7% except for export projects for which the rate would remain at 4%. The rate to t..e final

borrower on import substitution projects would then be raised from 10% to 12%, but remain 8-10% for export projects. Any definitive modification of present interest rates will, of course, have to reflect the conclusion of the Monetary Board study of interest rates, terms and other characteristics of development loans.

Comment: As pointed out in an earlier section, the PIF is presently making its funds available to the intermediate credit institutions at a 4% interest rate, irrespective of the interest rates charged the ultimate borrowers or the economic objective of the project. In the discussions with the Colombian authorities there was a general consensus that every effort should be made to direct as great a proportion of the PIF's resources towards the expansion of export production as possible. One method which would seem to deserve special attention is to give the intermediate credit institutions a larger spread in the case of loans for export projects than in the case of loans for import substitution or bottleneck breaking projects. At the same time, given the uncertainties and special risk of exporting, a lower interest rate for this purpose would seem appropriate. Moreover, the interest rates presently set by intermediate credit institutions to the ultimate borrowers seem unduly low, compared to normal commercial bank rates of 12-14%, particularly in the case of loans for import substitution projects that are likely to be highly profitable. One of the main reasons for the present rates is the fact that under a number of laws and policy determinations going back for many years, special longer term credit facilities for industry and agriculture have been created and specially low interest rates set for these operations. Partly as the result of the discussions between AID staff members and the Colombian authorities concerning the PIF, the new Monetary Board has started a study of the interest rate structure of all long term development financing in Colombia and the definite readjustment of the interest rates charged ultimate borrowers of PIF funds will have to await the recommendations of such a study.

One further aspect of the proposed modification of the PIF interest rate structure deserves special comment, namely the suggestion that PIF's own relending rate to the intermediate credit institutions be increased from 4% to 7% in the case of loans for import substitutions or bottleneck breaking. This may be increasingly important in the future in enabling the PIF to service its own debt obligations and cover its operating costs since it is likely that most of its direct foreign borrowing will be at interest rates in excess of the 4% interest rate it is presently charging the intermediate credit institutions. Thus the IDB loan to the PIF carries a 5 3/4% interest rate, the Dutch loan a 4 1/2 to 5% interest rate and the proposed AID loan would be at 5 1/2% to the PIF even though the Government of Colombia would be offered AID's maximum concessional terms under the two-step procedure. Up to now the management of the PIF has not had to face this problem since, as stated previously, the only funds that PIF has actually made use of thus far consist of the peso counterpart of the 1963 AID program loan for which PIF has to pay the Colombian Government an interest rate of only 3/4 of 1%.

2. At least 55% of available lending funds will be channeled into the expansion of production for export.

Comment: The second suggestion concerning PIF lending policy is closely related to the first one and is aimed at directing as high a percentage as possible of the Fund's resources towards export production. As shown in Table 3, only 33% of both the number and volume of loans authorized thus far have gone for projects that have exports production as their only objective and even if other loans for projects which have both export production and import substitution or export production and bottleneck breaking as their objectives are added, less than 50% of total loan funds have been devoted to the expansion of export production. This occurred during a period when a very large part of the PIF resources went to a few relatively large projects designed to expand the growing of sugar cane and enlarge the capacity of sugar mills. The requirement that at least 55% of total loan funds be devoted to export production is therefore not easy to fulfill and will force both the intermediate credit institutions and the Bank of the Republic to give clear and decided preference to the financing of export projects.

3. Consideration will be given under the import substitution criterion to subloans for the large-scale production of basic food crops such as corn, rice and beans where severe, continuing shortages might require imports. These loans might be preferably destined for the purchase of imported component of the carrying out of such farm improvements as the construction of silos.

Comment: Commercial production of basic food stuffs for the domestic market appears to be emerging as one of the Achilles heels in the Colombian development process. Corn production has actually tended to fall in recent years and the growth of other basic staples has not been satisfactory. In certain areas of the country such as the Cauca Valley, sugar production seems to be displacing corn. While Resolution 11, as now constituted, clearly permits the type of loan visualized under suggestion No. 3, neither the intermediate credit institutions nor the Bank seem to have devoted enough attention to promoting and seeking out these types of projects.

4. The BOR, in consultation with the Planning Department, will arrange to have basic economic studies made in sectors such as sugar production or the expansion of the chemical industry, in which basic detailed information is essential to judge the extent and the criteria for further expansion.

Comment: As shown in Tables 3 and 8, a great proportion of PIF lending to date has gone into two sectors, namely the expansion of sugar production and the financing of the expansion of the chemical industry. The technical staff as well as some members of the Board of Directors of the Bank have expressed the urgent need for detailed studies of these industries, including a realistic long term appraisal of such factors as world production and demand for sugar in order to avoid financing what might turn out to be an excessive expansion of the sugar industry or the financing of projects in the chemical industry which, however sound technically, may have less priority than other projects in the same industry. It is proposed that up to $100,000 of the AID loan be reserved for the financing of such studies if it should prove advisable to contract U. S. consulting firms to assist the Bank of the Republic and the Government Planning Department.

5. a) BOR will continue to finance not more than 70% of the peso cost of the project.

b) BOR will apply clear definitions of acceptable types of borrower's contributions to the proposed project.

Comment: The above suggestions are intended to reaffirm existing policies and practices of the Bank.

6. The PIF will not make commitments in excess of the amount of funds for which it has firm commitments plus repayments. In this connection there should be an exchange of letters among the US AID, the Government, and PIF giving a firm commitment for the use of pesos earmarked for the PIF at the time such an agreement is reached between the Government and US AID.

Comment: Until recently the management of the PIF has tended to authorize loans in excess of funds formally made available to it. It has done so because of its knowledge that there existed a tentative understanding between USAID and the Colombian Government concerning the allocation of up to $30 million equivalent of peso counterpart funds to the PIF. The Bank called for these funds only when it expected that it would need them for actual disbursements in the relatively near future. It is felt that this practice is undesirable and the above suggestion is designed to provide the Bank with adequate assurance of peso availabilities.

7. Accelerated repayment of the subloans should be required if the borrowing firm increases the proportion of its after-tax profit distributed above, say 40% of that profit, or

above the average percentage in the three years preceding the loan, whichever is higher but not normally in excess of say 60%. The accelerated repayment might be equal to the amount distributed above the relevant percentage.

Comment: There was a general consensus that the PIF should make sure that the ultimate borrowers do not increase the distribution of their profits unduly during the period when they are utilizing PIF loan funds. There has been a tendency on the part of important industrial firms in Colombia to distribute an excessive proportion of their profits instead of reinvesting their earnings and the introduction of this procedure would discourage such practices.

8. Every effort should be made to ensure that the intermediate credit institution participates adequately in the financing of the project. Such financing should be a prerequisite, at least, of import substitution and bottleneck breaking loans. Moreover, applications must clearly demonstrate that provision of working capital is assured, often with the help of the intermediate institution.

Comment: The above suggestion is designed to reinforce and spell out the requirement which the Bank of the Republic has tried to enforce in a half-hearted manner thus far. Given the relative credit restraint which is necessary in order to bring the present inflationary pressures under control, it is essential that the commercial banks and financieras supplement PIF loans for priority projects by providing at least a good part of the necessary working capital.

9. Coordination between requests for Cooley loans and PIF loans will be arranged by a mutual exchange of data between BOR and US AID on applications received.

Comment: While the BOR has been coordinating requests for Cooley and PIF loans, a frequent mutual exchange of data between the Bank and US AID should prove helpful to both in avoiding duplications and confusion.

10. The BOR will make additional efforts to give the PIF publicity throughout the country. In this connection preparation of an annual report should be required. In addition to basic information about the PIF, the loans approved, and the movement of funds, the annual report could include pictures of projects financed and description of the contribution of the Fund to the country's economy. In addition, frequent press releases on activities and coverage of the PIF in the BOR monthly bulletin are desirable. The annual report and other publicity should make it clear that Alliance for Progress Funds have been a key factor in the PIF.

Comment: As has been noted the Resolution No. 11 enjoins the Bank of the Republic to publicize the PIF but it is the impression of US AID and AID/W staff members that its efforts in this direction have been rather inadequate. The above suggestion is designed to deal with this criticism.

B. Suggestions Regarding Procedures for Approval and Follow-up of Project Loans by the Intermediate Credit Institutions and the BOR.

1. In the case of all sub-loans in excess of 3 million pesos, the intermediary credit institution will require the sub-borrower to furnish not only an answer to the required questionnaire but also an adequate project study. This requirement might be waived by BOR in exceptional cases where a great deal of information is available on the technical, economic and financial feasibility of similar projects, except where the proposed PIF loan is in excess of 1 million dollars or its equivalent in pesos.

Comment: Actual examination of the type of information submitted by would-be borrowers to the intermediate credit institutions and forwarded by these institutions to the BOR reveals a wide variation in the quality of the material supplied to justify the proposed loans. It is felt that sub-borrowers as well as the intermediate credit institutions should be encouraged and even forced to prepare carefully worked out proposals, including studies of the economic, financial and technical feasibility of all relatively major projects. Colombia possesses an unusual number of able engineers and architects as well as well-trained economists and accountants. Some consulting firms have already acquired considerable experience and reputation but they are not being as fully used by would-be borrowers as would seem desirable.

2. The intermediate credit institution will require that the sub-borrowers provide it with copies of contracts, import licenses, customs clearances, and other documents to support the expenditure of funds according to the project proposal, using the revolving fund method of subloan disbursements where appropriate. A summary of such documentation reviewed will be included in the quarterly report referred to in No. 3 below.

Comment: This suggestion is designed to tighten up the disbursement procedures and end-use checks on the part of the intermediate credit institutions. It is intended to correct some situations in the past where funds were disbursed by the Bank of the Republic to the intermediate credit institution and by the latter to the ultimate borrowers well in advance of actual project needs as well as the tendency of some of the intermediate credit institutions to fail to institute any system of verification that the funds are being used for the purposes described in the project. As mentioned, this has tended to throw an undue burden for end-use checks on the staff of the Bank of the Republic.

3. The intermediate credit institutions will be required to furnish the BOR with a regular quarterly progress report from the time disbursements begin until the project is completed. Such reports would cover the entire project, not only that part financed by the PIF. In each case, preparation of the quarterly report will require on-site inspection by a qualified technician in the field (industrial engineer, agriculturalist, etc.). These technicians might be regular employees of the intermediaries, employees of the Asociacion Bancaria, or independent consultants.

The manager of the local branch of the intermediary, i.e., the person directly responsible for the disbursements will be a co-author of each quarterly report.

Comment: This suggestion is closely linked to the previous one and its adoption will force the intermediate credit institutions into conducting regular end-use checks and preparing regularly reports to the Bank of the Republic. It will obligate them to either put on their staff qualified technical personnel or to make contracts with such personnel and will force branch bank managers in charge of loan disbursements to follow the execution of the projects with special care. The setting up of the proposed system will lighten the burden on the Bank of the Republic's staff and will force the intermediate credit institutions to do a much better job of appraisal banking.

4. The BOR will work out a schedule of site visits which assures that its inspection teams will visit each project at least once within six months following the start of disbursements, and periodically thereafter.

Comment: This suggestion is intended to formalize and systematize the inspections that are already being carried out by the staff of the Bank of the Republic.

5. The Bank of the Republic will make every effort to strengthen its review and monitoring staff. As a minimum the Bank will organize one additional inspection team consisting of a loan officer or economist, engineer and accountant. For this purpose the services of a consulting firm might be engaged.

In addition, the Bank will examine the desirability of a somewhat greater centralization of staff operations concerned with the PIF program.

Comment: As discussed in a previous section of this capital assistance paper, the technical staff of the bank dealing with PIF matters is clearly overburdened and needs urgently to be reinforced either by hiring more staff or by the Bank making contracts with outstanding Colombian or even foreign consulting firms. At the same time it is important that the Bank keep under continuous review its operation of the PIF.

C. Understandings Concerning Conditions of Proposed 10 Million Dollar Loan and Future Releases of Peso Proceeds of AID Program Loans

1. A dollar loan to the PIF will involve two steps, first a loan to the BOR for the PIF at a rate of interest in line with the current rates charged by the Export-Import Bank or the IBRD of 5 1/2% at a maturity of 15 years, including a 5-year grace period and second, an offer to the Government of Colombia to receive repayment of the loan from the BOR in Colombian pesos and repay A.I.D. over 30 years following a 10 year grace period with interest at 3/4% during the grace period and 2% thereafter. Peso funds will continue to be provided on the present basis.

Comment: The above requirement spells out the proposed two-step procedure. In view of Colombia's balance of payments situation, it is proposed that the GOC be offered the two step option of a 40-year dollar loan including a ten-year grace period. The loan would be made to the Bank of the Republic for Private Investment Fund at a 5 1/2% interest rate and for a term of 15 years including a five-year grace period - terms identical with those proposed by the World Bank.

2. The dollar loan would provide an allocation of funds, perhaps $100,000 initially, to cover economic studies which the BOR in consultation with the Planning Department might wish to contract with US or Colombian firms or individual consultants. These funds could also be used to contract suitable firms or specialists who would assist the BOR in providing guidance and assistance to the intermediate credit institutions in loan procedures and other technical aspects of the preparation and review of projects.

<u>Comment</u>: It should be noted that there is no requirement that the Bank of the Republic contract for technical assistance but that funds are to be set aside in case that U. S. technical assistance might become desirable.

3. Except by agreement with the AID, funds available from U. S. sources, either dollars or pesos, may not be used for increased export production of raw materials where there is already a world surplus and in which marketing is limited by international agreements to which either the United States or Colombia is a party.

<u>Comment</u>: This proposed requirement is designed to avoid the use of AID loan funds or peso funds for the financing of the expansion of such products as cotton and coffee which are in world surplus.

4. U. S. generated funds, either dollars or pesos, will not be available to any sub-borrower if information available to the BOR indicates that the sub-borrower has other resources or credit lines on appropriate terms with which the project should be financed.

<u>Comment</u>: This proposed requirement is designed to reinforce the position of the staff and Board of Directors of the Bank of the Republic in resisting pressure from both domestic and foreign interests who try to secure PIF loans even though the information available to the Bank clearly indicates that they have ample resources of their own or ready access to other appropriate sources of financing.

5. When the foreign exchange component of a loan is as much as $500,000, the loan application will be referred through US AID to the Export-Import Bank for possible financing of the dollar part.

<u>Comment</u>: This proposed requirement is based on the fact that the Export-Import Bank was willing to agree to AID consideration of the proposed loan with the understanding that all

applications over $500,000 which have been approved by the Colombian authorities be referred to the Export-Import Bank for an expression of the Bank's interest in considering such applications directly. It should be noted that the Export-Import Bank has made one loan thus far to cover part of the foreign exchange costs of a project which is also receiving a PIF loan and has several other loan requests under consideration.

6. Pesos provided from U. S. Program Loans will be in future limited to the financing of peso costs.

Comment: While information available to date indicates that the overwhelming proportion of peso funds resulting from the AID Program Loans made available to the PIF has been used to finance local costs, a certain proportion has been used to buy foreign exchange for the direct importation of goods and services from abroad. Such a use of pesos was not confined to purchases from the United States. In order to assure that this will not occur in the future and encourage the management of the PIF to seek foreign exchange financing actively and on appropriate terms from European countries and Japan, it is essential that the use of pesos from U. S. Program Loans be limited to the financing of peso costs, except for a limited amount of off-the-shelf procurement (not to exceed $5,000) of goods and services of Free World origin.

7. The Bank of the Republic and AID are to work out a mutually acceptable procedure under which the resources of the PIF would be denied borrowers who utilize unduly short term supplier credits to finance a portion of the project for which PIF financing is proposed.

Comment: Available information seems to indicate that perhaps as much as half of the foreign exchange costs of the projects for which PIF loans had been approved as of April 9, 1964, were financed by means of supplier's credits. It is further known that many of these credits are very short-term, carry no grace period and are, therefore, very undesirable from Colombia's balance of payments point of view. Best available estimates seem to indicate that suppliers' credits to the private sector amount to several hundred million dollars and have been rapidly increasing in recent years. The Colombian authorities are engaged in formulating a broad program to deal with the troublesome problem of short-term debt, of which the undue growth of short-term suppliers' credits is only a part. It seems essential nevertheless that the PIF mechanism be used in helping to cope with this problem. Of course, the very existence of a sizable A.I.D. credit for procurement in the United States, available through the PIF, the fact that the latter can also lend pesos and that the Bank of the Republic rather than the ultimate borrower will be assuming the exchange rate risk is likely to result in a good many borrowers using the A.I.D. credit rather than incurring unsuitable, short-term debts to suppliers.

8. a. The PIF will furnish US AID on a quarterly basis, using a format to be agreed on, summary reports on the utilization of the proposed dollar loan, peso funds and general information on availability and utilization of other external credits.

b. The PIF will continue to furnish US AID on a monthly basis with information as agreed between them covering subloan applications, intermediary credit institutions involved, approvals, rejections, breakdown of total project costs and of loan use for peso and foreign exchange costs, economic category of loans, borrower's identity, subloan terms, disbursements, repayments and delinquencies.

c. The PIF will furnish US AID quarterly progress reports containing, in addition to a summary of the information referred to under 7-b, data on the progress in implementing projects for which subloans have been authorized, in such detail as PIF and US AID will agree upon.

Comment: The above requirements spell out the desirable types of progress reports which will help A.I.D. in monitoring PIF activities.

9. At least once a year, PIF and US AID will review the progress of the PIF financing program, including lending policies, the procedures used by the BOR and the intermediary credit institutions in reviewing, approving, implementing and checking on the use of both peso and dollar subloans.

Comment: The proposed requirement, together with the rather elaborate reporting requirements outlined previously, is especially important since it is not proposed to insist that the Bank of the Republic engage consultants that would check on the operations of the PIF nor is it proposed to have A.I.D. review subloans above a certain size which has often been a requirement in loans to intermediate credit institutions. It is felt that PIF's operating record to date and the excellent quality of the Bank of the Republic's staff make it unnecessary to insist upon such devices. Moreover, it was felt that any such requirement would set an undesirable precedent for other potential lenders.

10. For the proposed dollar loan, A.I.D. and PIF will work out together the simplest and most expeditious disbursement methods compatible with applicable U.S. legislation. One possible approach would be as follows:

(a) In the case of procurement in the United States by the sub-borrower of equipment and supplies involving total disbursements in excess of $25,000 the letter of commitment method would be used under which A.I.D. opens letters of credit directly in favor of the suppliers from whom the sub-borrowers order the equipment.

(b) For total purchases of less than say $25,000 the reimbursement method might be used.

11. BOR will undertake an early study of ways and means of mobilizing domestic savings especially to complement the resources made available to the PIF by the United States and other foreign lenders.

Comment: The PIF has been conceived until now as being essentially a device to utilize external financing. While existing data indicate that PIF loans have supplemented internally mobilized resources of several times their size, it would seem appropriate that the Colombian authorities study seriously the possibility of mobilizing internal savings for industrial and agricultural development since the existing devices for this purpose do not seem to operate satisfactorily in the present inflationary environment.

V. ECONOMIC JUSTIFICATION OF THE PROPOSED LOAN

Enlargement of the PIF's resources by means of the proposed AID loan, and the changes in some of the Fund's policies and operating procedures, which will be a major by-product of the proposed additional financing of the PIF, are important to the achievement of such priority goals of the U.S. assistance effort in Colombia as:

(1) Financial balance (including solution of the balance of payments problem) at a level permitting accelerated economic growth and social progress;

(2) A more diversified and productive agricultural sector which will lead the way in the export drive; and

(3) Provision of increased stimuli to guide Colombia's vigorous private sector into activities of prime program priority.

The proposed loan appears especially justified for the following more specific reasons:

(1) It will enlarge the PIF's resources for long-term financing, especially for export production.

As shown in Table X, subloan approvals through the Private Investment Fund mechanism exceeded the equivalent of $24 million during CY 1963 and; according to careful estimates made by the Bank of the Republic's staff are likely to exceed $36 million equivalent during CY 1965. This is very much in line with the estimates made in the recent IBRD report on Colombia which states the following:

"Experience of the PIF thus far and the recent flow of project applications indicate that the equivalent of US $40 million can be effectively utilized by the PIF in 1964 for loans to help expand production for export and in substitution for imports. This non-inflationary financing of the private sector is needed to supplement local funds available through the banking system. The new IMF standby agreement approved in February 1964 indicates levels of credit expansion consistent with overall monetary stability. Under the program agreed with the Fund for 1964, total Central Bank credit would expand by about 6%, most of which would be for the private sector. The expansion of credit from domestic sources would be combined with disbursement under the Private Investment Fund. PIF disbursements would need to amount to at least US $40 million equivalent if total credit to the private sector is to increase by about the minimum necessary - about 10% - to provide adequate financing for the investment and working capital requirements of the private sector. Substitution of additional Central Bank credit for PIF financing would have unfavorable inflationary and balance of payments risks.

The amount of PIF credits needed during 1965 will depend largely on whether current strong incentives for investment in private agriculture and industry continue and on the extent to which domestic savings can be increasingly channeled toward financing private investment."

TABLE X

Estimate of PIF Loan Approvals
CY 1964

	No.	Amount
Approvals during CY 1963	50	240.3
Approvals during first four months of CY 1964	20	87.6
Approvals expected during remaining eight months of CY 1964	69	279.1
Projected Loan Approvals in CY 1964	89	366.7

Source: Bank of the Republic

The proposed loan is designed to finance a portion of the foreign exchange cost of PIF approved projects and is to be disbursed during the next 18 to 24 months. Considering the fact that, as shown in Table IV the foreign exchange cost of the projects approved during the first year of the Fund's operations exceeded $42 million, of which only $5.4 million were financed by PIF peso loans and that in the future the peso proceeds of AID program loans made available to the PIF are not to be used to finance the foreign exchange component of projects, there can be little doubt that the size of the proposed loan is rather moderate. This will be true even if the negotiations for a $10 million loan from the World Bank for the financieras were to be concluded in the very near future.

The foregoing judgment appears to be borne out by all presently available information on levels of industrial investment and the volume and value of industrial and agricultural machinery and equipment imports during recent years. All the data appear to indicate that there exists a very strong latent demand for such equipment.

(2) As a result of the proposed loan an increasing portion of the foreign equipment and supplies of the projects which the PIF helps finance will be bought on longer terms much more appropriate from the point of view of Colombia's balance of payments than seems to have been the case up to now. According to the information available, a major portion (perhaps as much as 20 million dollars) of the total foreign exchange cost of PIF projects has, up to now been financed by means of supplier's credits, many of which are short-term (2-5 years) and have no grace periods.

(3) By providing a ready source of dollar exchange for procurement in the U.S. and through the provision that the use of peso proceeds of AID Program Loans is to be restricted to local cost financing, the new loan will help assure that the PIF's peso resources are used for the financing of local costs and not to any significant extent for the acquisition of third country goods and services. The latter is clearly undesirable from the point of view of the U.S. balance of payments and the U.S. commercial position in Colombia.

(4) PIF borrowers will be able to secure equipment and services needed to carry out their projects in the United States on suitable terms and without incurring the exchange risk since the latter will be assumed by the Bank of the Republic for the account of the Government. AID financing is thus likely to result in additional U.S. exports to Colombia.

(5) The proposed loan is likely to constitute powerful pressure on other potential lenders, such as the European countries and Japan to make funds available, on suitable terms to the PIF for foreign exchange and, whenever possible, local cost financing. Up to this time only the Netherlands has negotiated a small (1.4 million dollar) credit with the Bank of the Republic for use by the Fund.

VI. FINANCIAL ASPECTS OF THE PROPOSED LOAN

1. Proposed Loan Terms

It is proposed to make the loan in two steps. First, the proposed loan to the Bank of the Republic for the PIF is to be for a term of 15 years, including a 5-year grace period, at a $5\frac{1}{2}$% interest rate. These terms are in line with those proposed by the IBRD for its loan to the financieras via the PIF, are slightly more favorable than the terms of the existing IDB loan to the PIF (12 years, 2 years' grace at 5 3/4%), but harder than the reported terms of the Dutch credit to PIF (15 years, interest rate $4\frac{1}{2}$% or 5%, depending on money market conditions in the Netherlands). At the same time they are broadly in line with those which the Export-Import Bank would be likely to apply if it were to make a loan for the PIF. Second, in view of Colombia's balance of payments problem involving relatively heavy debt service payments during the next few years, the most concessional A.I.D. lending terms are contemplated for the option to be offered the GOC, i.e., a 40-year loan with a 10-year grace period, with interest at 3/4% during the grace period and 2% during the repayment period. (For an analysis of Colombia's balance of payments situation see AID-DLC/P-228, Airgram A-592 from Bogota, and the recent IBRD Report on the Colombian Economy, especially Chapters VI and VII.) As mentioned in an earlier section, the Government's authorization to contract external debt is almost fully used up and its enlargement by the Colombian Congress will require considerable time so that there may be a significant delay in the Government excercising the 2-step option which will be offered to it.

The proposed 15-year term for the loan to the BOR is in excess of the maximum limit for subloans which is fixed at 10 years under the provisions of Resolution No. 11. But, as noted in a previous section, this limit can be waived by the Board of Directors of the Bank of the Republic in the case of individual subloans whenever there are valid reasons for doing so. Moreover, the World Bank, in discussing the terms of its proposed loan to the financieras, has been exploring with the Colombian authorities the desirability of subloans repayable over a 15 year period in the case of certain types of industrial and agricultural projects that have a long gestation period. Finally, it appears desirable to enable the PIF to utilize AID funds on a revolving basis. Should the present pattern of subloan maturities continue, then a 15 year AID loan for the PIF would enable the funds to be used twice on the average before repayment is completed. The five year grace period appears desirable as a method of helping the PIF in consolidating its position and being in a position of attracting additional non-U.S. resources.

The proposed 2 step procedure will lead to the creation of an interest rate spread as well as a spread between the scheduled repayment by the PIF and the GOC. The interest rate spread might be invested in readily liquid assets to serve as a special reserve against the exchange rate risk. The "principal" spread would be utilized by the GOC with the agreement of A.I.D. for development financing, including loans through the Private Investment Fund.

The proposed interest and repayment terms on the first step of the proposed AID Loan - $5\frac{1}{2}\%$ interest, 15 year repayment including a 5 year grace period - must, of course, be viewed in the light of the present and proposed relending rates of the PIF as well as the Fund's operating results to date.

As shown in Table XI, during its first year of operations the PIF was able to realize a small operating surplus. Its income consisted of the 4% interest charged the intermediate credit institutions; its outlays of the operating expenses that are surprisingly low, (reflecting the economical way in which the Bank of the Republic operates the PIF) and of interest payments at the rate of 3/4% on AID Program Loan Generated Pesos disbursed up to now.

TABLE XI

PIF: Profit and Loss Statement for First Year of Operations
(April 15, 1963 - April 30, 1964)
(in thousand pesos)

Income from Interest		1,585
Less Operating Expenses	836	
Less Interest Payments on AID Program Loan Generated Peso Funds	522	1,358
Operating Surplus		227

Source: Bank of the Republic

Any projection of the financial situation of the PIF made at this time is of very limited significance because of the uncertainty concerning a possible modification of the interest rates charged by the PIF, the likelihood of the PIF attracting foreign financing on terms difficult to forecast and the fact that no loans for direct foreign procurement have been utilized up to now by the PIF System. Consequently, no projection is presented at this time. There is no doubt that the Colombian authorities will adjust the interest rate structure in such a way that the Fund will be in a position to meet its operating and overhead costs and service its debt obligations.

2. Ability to Repay

It may be concluded that there are not only reasonable but excellent prospects for repayment of the proposed loan since the intermediate credit institutions will assume the credit risk of subloans while the country's Central Bank will be the borrower and will assume the exchange rate risk for the account of the Government. The latter, in exercising the 2 step option, will be responsible for the eventual repayment in dollars of the proposed A.I.D. loan.

VII. IMPACT ON U. S. ECONOMY

The proposed loan is likely to have a number of very favorable effects on the U. S. economy. First, the loan will be entirely for procurement of goods and services from the United States. At the same time, it is proposed that the peso proceeds from AID Program loans be restricted to local cost financing. Under these circumstances, the potential sub-borrowers will be offered a very attractive financing package: dollar financing for procurement in the United States with the exchange rate risk being assumed by the Bank of the Republic together with peso financing of local costs. Second, the sale of U. S. exports of equipment, machinery and supplies is likely to be additional to the goods U. S. exporters would otherwise sell in Colombia. The proposed PIF loan is thus a vital complement to the AID program loans. Third, the loan will involve the financing of forward procurement - i.e., the U. S. exporter will know in advance that his sale of goods and services to PIF sub-borrowers will be AID financed.

While the expansion of export production is one of the major objectives of all PIF lending, many of these exports are of tropical or semi-tropical products not produced in the United States.

VIII. IMPLEMENTATION PLAN

As pointed out in a previous section of the Capital Assistance Paper, the Project Committee consisting of USAID and AID/W staff members have discussed the likely conditions and modus operandi of the proposed loan rather fully with the Colombian authorities. They also made a number of suggestions concerning the operations of the PIF and the use of the peso proceeds of AID Program loans by the PIF. Some of these suggestions and understandings will form part of the loan agreement, others will be spelled out in implementation letters or in an exchange of letters between USAID and the Bank of the Republic.

It is planned that USAID will conduct the actual loan negotiations in Bogota with the assistance of AID/W legal and loan staff members and that the loan agreement will be signed there within 2 - 3 weeks after authorization. In view of the fact that likely loan conditions have been fully discussed with the staff and top management of the Bank of the Republic, it should prove possible to confine conditions precedent to disbursement to a minimum. The major points to be worked out prior to disbursements are likely to involve:

(1) An understanding concerning disbursement procedures;

(2) An understanding concerning procedures that will deny PIF financing to ultimate borrowers who plan to utilize suppliers' credits which are excessively short-term and costly.

As far as disbursement procedures are concerned, it is proposed to work out arrangements which would permit reimbursement by AID for procurement by sublenders in the United States of items costing less than $25,000 while all dollar procurement costing more than that would be financed under the letter of commitment procedure.

It is believed that conditions precedent to disbursement will be satisfied within 3 months following loan authorization, and that the entire loan will be committed in loans to sub-borrowers within about 18 months and will be disbursed within 24 to 30 months.

USAID will have monitoring responsibility, including that of carrying out of site inspection and periodic reviews of policies and operations. Several USAID staff members have been closely familiar with PIF operations since the Fund's inception.

IX. ISSUES

None.

COLOMBIA - BANCO DE LA REPUBLICA
(PRIVATE INVESTMENT FUND)

CHECKLIST OF STATUTORY CRITERIA (ALLIANCE FOR PROGRESS)

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

2. FAA Section 201(d). Loan funds are not to be loaned or re-loaned at rates of interest which are excessive or unreasonable for the ultimate Borrower or in conflict with Colombian legislation.

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

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

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

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

7. FAA Section 251(b)(2). The activity to be financed is economically and technically sound.

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

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

10. FAA Section 251(b). The loan complements financing from other Free-World sources.

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

12. FAA Section 251(b). Account has been taken of the extent to which Colombia is making reasonable efforts to encourage repatriation of capital invested in other countries by its own citizens.

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

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

15. FAA Section 251(g). In view of the nature of the project, it is not appropriate to utilize the loan to assist in promoting the cooperative movement in Latin America.

16. FAA Sections 601(b); 621. The loan will be administered in such a manner as to encourage and facilitate participation by private enterprise to the maximum extent practicable.

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

18. FAA Section 604(a). Equipment, materials, and services (except Marine Insurance) financed for the project under the loan shall be procured from the United States.

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

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

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

22. FAA Section 611(a)(2). No further legislative action in Colombia in required for implementation of the project.

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

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

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

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

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

28. FAA Section 620(c). Colombia is not indebted to any U. S. citizen for goods or services furnished or ordered, where such a citizen has exhausted available legal remedies or where the debt is not denied or contested by or the indebtedness arises under an unconditional guaranty of payment given by Colombia.

29. FAA Section 620(d). It is not anticipated that loan funds will be used to finance construction or operation of any facility which will compete with United States enterprise. In the event loan funds are so used, appropriate procedures will be made to prevent the exportation to the U. S. of more than 20% of the annual production of any such facility.

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

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

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

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

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

35. FAA Section 636(h). Colombian private firms and credit institution will contribute local currency in the amount of at least equivalent to US $3 million to meet the cost of contractual and other services to be rendered in conjunction with the project. Foreign currency owned by the United States will, to the maximum extent possible, be utilized to meet the costs of contractual and other services for the project.

36. App. Section 102. Not applicable.

37. App. Section 104. Funds obligated by the loan will not be used to pay pensions, annuities, etc., as prohibited in this section.

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

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

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

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

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

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Chairman, Project Committee

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BANK OF THE REPUBLIC

P R I V A T E   I N V E S T M E N T   F U N D

Resolution Number 11 of 1963
of the Board of Directors of
the Bank of the Republic

BOGOTA-COLOMBIA

PRIVATE INVESTMENT FUND

"PIF"

RESOLUTION No. 11, OF 1963

(February 28)

The Board of Directors of the Bank of the Republic,

in the exercise of the powers conferred by

Decree-Law 756 of 1951,

RESOLVE:

Article 1.- In accordance with the recommendations of the Mission of the International Bank for Reconstruction and Development and of the ad-hoc Committee of the Alliance for Progress, which studied Colombia's General Program of Social and Economic Development; and in implementation of the provisions of Article 2 of Decree 756 of 1951, the Private Investment Fund "PIF" is hereby established within the Bank of the Republic. The "PIF" will possess different characteristics and management procedures from those employed for the usual quotas of credit in the Bank.

Article 2.- The Private Investment Fund will consist of the peso proceeds generated by foreign loans and of the foreign exchange resources available to the "PIF" from foreign credits, or from other sources, which the Bank of the Republic agrees to accept for the "PIF".

The Fund will be employed for financing investments exclusively in the private sector, which will significantly contribute to the Country's economic development, with particular attention given to investments which contribute to the diversification and promotion of exports.

Article 3.- The operations of the Private Investment Fund will be based upon the following general principles:

I - OBJECTIVE

To supply the private sector with financial resources earmarked for the highest priority investments within the framework of the General Development Program contributing to the diversification and promotion of the Country's exports. These investment projects will be subject to the requisites and conditions established hereunder.

II - FINANCING

The Private Investment Fund will consist of the peso proceeds of foreign loans and of the foreign exchange resources extended to the "PIF" by means of foreign credits, or from other sources, which the Bank of the Republic may or may not accept for this purpose.

III - ELIGIBLE INVESTMENTS

The Private Investment Fund will direct its resources to the financing of investments in the area of primary activities (agriculture, cattle industry, fisheries, mining, etc.) and industry in accordance with the following order of general priorities:

a) Diversification and Promotion of Exports.-

Under this criterion, acceptable investments will be those which significantly contribute to a strengthening of the Country's balance of payments, by providing new resources of foreign exchange or by increasing the foreign exchange earning potential of current export activities. In order to achieve this objective, the following, among other considerations, will be taken into account: the conditions of supply and demand in foreign markets, and the net foreign exchange impact of the investment.

b) Elimination of Shortages in the Production of Goods and Services.-

Under this criterion, acceptable investments will be those which tend to eliminate shortages in domestic production of goods or services necessary to achieve the objective stated in paragraph (a), or necessary to the normal development of industrialization in accordance with the objectives of the General Development Program.

c) Import Substitution.-

Under this criterion acceptable investments will be those that also contribute to a strengthening of the balance of payments by re-placing necessary imports of basic goods. The type of product under examination will be considered in the light of this objective. This consideration will determine whether or not luxury goods are involved; whether or not they are final, intermediate or primary products; whether they are capital or consumption goods, etc.; and the net impact on the balance of payments and the time which it will take for this impact to be felt.

Changes regarding the activities to be financed and the priorities or order of the priorities, can only be effectuated by the Bank of the Republic and in accordance with the general economic development policy of the country.

In view of the fact that it is possible that upon applying these general criteria some projects may prove of equal rank in eligibility, other criteria may be applied, as for example, the proportion of labor to the investment, value added, location, size of the project, and other similar considerations.

IV - EXPENSES TO BE FINANCED

"PIF" loans will be employed exclusively for the acquisition of capital goods (national or foreign machinery and equipment) and for the construction, assembly and installation necessary for the initiation or for the expansion of production of economic value as well as the payment for certain technical studies necessary for the adequate preparation of investment projects.

In the case of agriculture, cattle raising and fishing, the Bank of the Republic may authorize, as an exception, the extension of "PIF" credit in order to make possible disbursements which are recoverable only in the long-run and which are in a different category of investments from those specified in the previous paragraph and, finally, which are an integral part of a medium or long-range investment.

In no case will capital requirements classified as short term or easily recoverable be financed. These requirements should be financed from other sources.

V - INTERMEDIATE INSTITUTIONS

The employment of the resources of the Private Investment Fund will be effectuated by means of the banking system which is understood to be all banks having access to the services of the Bank of the Republic and the financial development corporations.

The only institutions that may carry out "PIF" operations will be legally constituted organizations that demonstrate that they possess the facilities and the absolute impartiality to expeditiously implement their part of the "PIF" operations, while faithfully fulfilling the fundamental requirement of channeling funds into clearly private investment activities.

VI - THE OBLIGATIONS AND FUNCTIONS OF THE FINANCIAL INTERMEDIARIES

The Banks and the financial corporations will have, among others, the following responsibilities:

a) To publicize the nature of the "PIF" and its objectives within the private sector;
b) To promote investment plans beneficial to the country;
c) To orient clients in the preparation of plans and projects, and to assure adequate technical assistance from specialized organizations, either national or foreign;
d) To evaluate investment applications and projects in terms of national desirability and not a merely commercial criteria - in regard to the technical, economic and financial aspects involved;
e) To assist clientele in obtaining basic capital for high priority projects;
f) To appraise applications for credit in such a way that resources will not be used in projects which could be financed with the applicant's own resources, or by use of other normal credit sources, domestic or foreign;
g) To handle applications for credit in accordance with the procedures established hereunder;
h) To furnish the guarantees or the signatures required by the Bank of the Republic to assure satisfactory repayment of the loan and the fulfilment of each and every obligation forming part of this credit system;

i) To provide to the borrower the funds corresponding to the loan granted in the form previously established by the Bank of the Republic;
j) To check on the precise employment of the funds by the borrower and the general progress of the borrowing firm, without prejudice to the supervision to be carried out by the Bank of the Republic;
k) To report periodically to the Bank of the Republic on the development of the projects financed, and on any proven irregularity, in such a way that the Bank may impose penalties; and
l) To supply the Bank of the Republic with the additional information it may require at any time.

The way in which the intermediaries will operate in fulfilment of some of the functions and obligations indicated above, is left to their own initiative. What is important to the system is that high priority projects be presented to the Bank of the Republic satisfactorily prepared and analyzed. It is most desirable, of course, that the intermediaries themselves collectively offer services, or contract the services of experts, in order to discharge the above functions — particularly those under points c), d) and j) — in the most expeditious and technical manner possible and at the least cost.

One of the main responsibilities of intermediary institutions will be to verify that the credit applications presented to the "PIF" conform strictly to the criteria established for the Fund's operations.

VII - PROCEDURES TO BE FOLLOWED BY THE INTERMEDIARIES

Once an application for credit has been duly received by the intermediary, the recipient will proceed to record the application and study it from the standpoint of the reputation and solvency of the firm, its financial standing, etc.; proceeding then to the analysis — either directly or by means of entities created for this purpose — of the technical practicability of the project along with an economic evaluation. Once these procedures have been complied with, the application will be approved in principle by the intermediary institution's highest authority, and it will then be submitted for the consideration of the Bank of the Republic, along with relevant documents and analyses.

Once a request is received by the Bank of the Republic it will follow the procedures indicated under sub-section X.

Once a loan has been approved by the Bank of the Republic, the Bank will proceed to inform the intermediary bank or corporation, so that subject intermediary can complete the operation and procure the relevant guarantees, including surrender of foreign exchange from exports, were this to be the case.

The intermediary will then enter into contract with the borrower, employinga form previously approved by the Bank of the Republic.

Once the contract has been executed, the bank or financial corporation will present the document to the Bank of the Republic for a drawing against the "PIF" account. The total value of the negotiated document will be charged to the intermediary's account or only part of said value will be charged, if the Bank of the Republic has established the provision of funds on an installment basis corresponding to the various stages of the project.

VIII - ADMINISTRATION

The management of the Private Investment Fund will be assumed by the Bank of the Republic, which will appoint the personnel necessary for effective operation and will establish the studv groups and the decision-making committees deemed advisable. When the Bank considers it necessary, it may make arrangements to have technical atudies made by specialized firms or entities, of acknowledged prestige and independence, either national or foreign.

IX - FUNCTIONS OF THE BANK OF THE REPUBLIC

The Bank of the Republic will have, among other functions, the following:

a) To publicize to the banks and other financial intermediaries the nature of PIF and its objectives;

b) To accept, transact and contract foreign credits having satisfactory installment and interest terms as well as other types of financing for the PIF, particularly the peso proceeds of foreign loans granted to the country;

c) To sell the foreign exchange, the peso proceeds of which becomes part of the PIF;

d) To make an accounting of the amount of national currency or of foreign exchange employed in PIF credit operations independently of any other Bank resources; the accounts thus established will constitute a special credit fund with different characteristics and management from those of the regular credit quotas of the banks and finance corporations in the Bank of the Republic;

e) To reimburse to foreign lenders the credits granted directly to the PIF, and to act as guarantor of said loans whenever necessary. Likewise, to reimburse to the National Government the amounts in Colombian currency initially received as the counterpart of foreign loans, as well as the accrued interest;

f) To process the applications for credit chargeable to the PIF, in accordance with the procedure indicated in Sub-Section X;

g) To check on the precise employment of PIF resources in accordance with authorized purposes, and to observe the general progress of the borrowing enterprises, without prejudice to the obligation to which the financial intermediaries are bound, namely, that of controlling the use of PIF credits granted, and checking on the administration and operation of the borrowing firms;

h) To change the terms of the agreement with or apply the pertinent penalties to the enterprises which have violated the provisions established by PIF regulations or by the credit document in accordance with the reports of the financial intermediaries or of the Bank of the Republic's own inspectors.

The penalties may include demand for immediate payment of the obligation and/or denial of further access to PIF resources, and these penalties may be extended to the intermediary entities whenever the breach or the proven failures can be charged to the latter;

i) To review periodically the eligibility of the intermediary institution, as such, for PIF credit, particularly from the standpoint of their general capacity to repay the loans from the Fund and when necessary, suspend PIF credit to any institution, or limit the additional amount of Fund resources it may receive;

j) To periodically publish official reports on the progress and development of the Private Investment Fund, and to supply to the institutions which have financed the PIF any additional information they may require at any time, and

k) To act as liquidator of PIF, when necessary.

X - LENDING PROCEDURES TO BE OBSERVED BY THE BANK OF THE REPUBLIC

Once an application for credit has been filed, the Bank of the Republic will proceed to record it and to study it from the standpoint of the applicant's business history, solvency and financial situation, etc. The Bank will then verify whether or not the project submitted for consideration falls within the established economic priorities and whether or not it is in accord with other requirements of the system. It will then review and verify the study and analysis of the technical feasibility and economic justification of the investment submitted by the intermediary. Should these prove acceptable, the loan application will then be evaluated and awarded a certain number of points in order to facilitate final selection by a committee in the Bank of the Republic.

Once the loan has been approved, the intermediary will be informed accordingly so that it can complete the operation and demand the relevant guarantees.

Once the credit document, duly signed, has been presented to the Bank of the Republic to be charged against the PIF account, the total value of subject loan will be credited to the intermediary's account, or only the corresponding portion of the loan in the event that credits are to be extended on an installment basis correlated to the various stages of the project.

XI - CONDITIONS AND TERMS OF CREDITS

Beneficiaries.- PIF credit may be awarded either to natural or legal persons of a private character, the latter being established in accordance with the Colombian law, regardless of the amount of their capital and the origin thereof, provided they do not have available resources of their own nor financing opportunities from other sources to carry out the total investment either domestic or foreign.

Amount of Loans.- PIF credits will be awarded only for the purpose of completing the financing of projects, and in no case will they be extended for the total value thereof. Initially and in order to attain a wider distribution of PIF resources, a maximum limit of $ 3,000.000 pesos will be established for a complete project.

Nevertheless, the Bank of the Republic may exceed this limit in the case of projects which, in the Bank's opinion, possess exceptional characteristics, and provided the amount required would not detrimentally reduce the availability of PIF funds for other projects that are also of value to the country.

Loan Terms.- The banks and financial corporations, in so far as possible, will extend credit terms which will be adjusted to the recovery period of the investment. However, given the existing legal limitations, the following maximum terms must be observed:

Up to five (5) years for loans for agriculture and the cattle industry, and

Up to ten (10) years for industrial type loans.

Should special statutes authorize longer terms than those above and should such terms be required for particular PIF investments, the financial intermediaries may enter into transactions for longer periods than those indicated above, but the final acceptance thereof will require in case a special decision of the Bank of the Republic.

Rates of interest.- In industrial transactions acceptable to PIF, the intermediary institutions may charge the following annual rates of interest:

Up to 8 per cent on loans with a maximum term of three (3) years;

Up to 9 per cent on loans with three (3) to five (5) years terms, and

Up to 10 per cent on loans with terms of over five (5) years.

In transactions involving agriculture and cattle-raising which are acceptable to the PIF, the intermediaries may charge the following rates of annual interest:

Up to 8 per cent on loans with a maximum term of three (3) years, and

Up to 9 per cent on loans with terms of over three (3) years.

When the Country's economic conditions require it and when permissible under existing Colombian law, the rates of interest may be changed by the Bank of the Republic.

Rates of interest that will be applied by the Bank of the Republic.- The Bank of the Republic, as soon as it becomes involved in PIF operations, will charge a rate of 4 per cent whatever the term of the obligation. These funds will be used to meet the costs of foreign financing, PIF administrative costs, and any other costs involved in the system. Should there be funds in excess of these costs this surplus will be returned to PIF. However, the funds thus transferred may be used by the Bank to finance certain basic technical studies which may open new fields to private activity and provide a more dynamic utilization of PIF resources.

Whenever warranted by existing circumstances or Fund requirements, the Bank of the Republic may modify the rates of interest it charges for PIF operations.

Margins for intermediaries.- The difference between the rates of interest charged to their clientele by the banks and corporations, and those charged by the Bank of the Republic, will constitute the margin of the intermediaries, who are not authorized to collect any additional surcharge or commission. From this operating margin they must meet the expenses of consultation and review and evaluation of the projects, in all aspects, as well as supervision and risks.

Guarantees.- The beneficiaries of a PIF loan will furnish the financial intermediary the usual payment guarantees and whatever special guarantees required by the Bank of the Republic, in order to assure the fulfilment of all the obligations of the system. The intermediaries, in turn, shall guarantee the Bank of the Republic, with their own signature, the payment of the loan and the fulfilment of the obligations laid down by PIF.

Article 4.- In order to contribute to the objectives of the Private Investment Fund, the Bank of the Republic may grant loans in foreign currencies in accordance with the powers conferred by articles 2 to 7 of Law 83 of 1962, and in accordance with the regulations which the National Government may establish for these operations through the Board of Directors of the Bank of the Republic.

<u>Article 5.</u>- In the event that the resources destined for the Private Investment Fund were to be turned over to the Bank of the Republic in trust, the operations will be carried out pursuant to the rules established by the founders of the trust in the corresponding contracts.

<u>Article 6.</u>- The Manager of the Bank of the Republic will satisfy the necessary requirements of the Ministry of Finance and Public Credit so that the Government can negotiate for the foreign credit resources necessary for the operation of the Fund, and will provide all the cooperation required for this purpose.

<u>Article 7.</u>- This resolution will become effective as of this date.

LOAN AUTHORIZATION
Provided from: Alliance for Progress Funds
COLOMBIA: Banco de la Republica
(PRIVATE INVESTMENT FUND)

Pursuant to the authority vested in the Administrator, Agency for International Development ("A.I.D."), by the Foreign Assistance Act of 1961, as amended, and the delegations of authority issued thereunder, I hereby authorize the establishment of a loan ("Loan") pursuant to Part I, Chapter 2, Title VI, Alliance for Progress, to the Banco de la Republica ("Borrower") of not to exceed ten million United States dollars ($10,000,000) to assist in financing the costs of sub-loans by the Private Investment Fund ("PIF") for industrial, commercial and agricultural projects, and to assist in financing the United States dollar costs of technical assistance rendered in connection with the Loan, the Loan to be subject to the following terms and conditions:

1. Interest and Terms of Repayment:

(a) Borrower shall repay the Loan to A.I.D. in United States dollars within fifteen (15) years from the first disbursement of the Loan, including a grace period of not to exceed five (5) years. Borrower shall pay to A.I.D. in United States dollars on the disbursed balance of the Loan interest of five and one half ($5\frac{1}{2}$) percent per annum.

(b) If prior to the end of the first year subsequent to signing of the Loan Agreement, the Government of Colombia so elects, the Borrower shall fulfill its dollar obligation under the loan by paying to Government in the currency of Colombia the equivalent, determined as of a time and in a manner satisfactory to A.I.D., of the United States dollar amounts payable to A.I.D. under (a) above and in such event the Government shall pay to A.I.D.:

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

a. All interest immediately upon receipt subject to Government's right to retain all payments in excess of three-quarters of one (3/4 of 1) percent per annum during a grace period of not to exceed ten (10) years from the first disbursement under the loan ("Government grace period") and all payments in excess of two (2) percent per annum thereafter.

b. Principal within forty (40) years, including the Government grace period.

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

2. Other Terms and Conditions.

(a) Equipment, materials and services (except marine insurance) financed by the Loan shall be procured from the United States of America.

(b) Not to exceed one hundred thousand United States dollars ($100,000) of the loan may be used to finance the United States dollar costs of technical assistance rendered in connection with the loan.

(c) Subloans by the PIF financed by the Loan shall be made in accordance with Borrower's Resolution No. 11 dated February 28, 1963, as the same may from time to time be modified in a manner mutually satisfactory to A.I.D. and Borrower.

(d) Borrower and the PIF will make arrangements satisfactory to A.I.D. to strengthen and improve their staff.

(e) Except as A.I.D. may otherwise agree, funds directly or indirectly made available to the PIF by the United States of America will not be used for projects which are likely to result in (1) the increased production of agricultural commodities in world surplus other than foods and feeds, (i.e., cotton and tobacco), or (2) the increased exportation of surplus food and feeds in world surplus, (i.e., rice, wheat, vegetable oil, citrus fruits and coffee). A.I.D. will reserve the right to add to or delete from the lists of surplus agricultural commodities contained hereinabove in this section. With regard to subloans to textile producers, the Borrower will assure that additional production as a result of AID-financed subloans, will not be exported to the United States of America.

(f) Proposed subloans by the PIF in excess of five hundred thousand United States dollars ($500,000) to be financed by the Loan, shall be referred to the Export-Import Bank for possible financing by such Bank.

(g) Procedures acceptable to A.I.D. will be adopted by the PIF to deny the resources of the PIF to potential borrowers utilizing supplier credits having terms which are not mutually satisfactory to A.I.D. and Borrower.

(h) At least once per year, A.I.D., Borrower and the PIF will review the status of the Loan, lending policies and procedures and such other matters pertaining to the Loan as A.I.D. may request.

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

____
Administrator

____
Date