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

UNCLASSIFIED

AID-LA/P-78/1
April 11, 1969

MEMORANDUM FOR THE DEVELOPMENT LOAN COMMITTEE

SUBJECT: Honduras: Feasibility Studies (Increase)

Attached for your review are the recommendations for an amended authorization increasing by \$500,000 a loan in an amount of \$500,000 made to the Government of the Republic of Honduras to finance the United States dollar and local currency costs of equipment, material, and services necessary for the conduct of certain sectoral or resource surveys, prefeasibility studies, and feasibility studies.

Please advise us as early as possible but in no event later than close of business on Tuesday, April 22, 1969, if you have a basic policy issue arising out of this proposal.

Rachel C. Rogers
Assistant Secretary
Development Loan Committee

Attachments:

Summary and Recommendations
Project Analysis
ANNEXES I-IV

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AID-LA/P-78/1

April 11, 1969

HONDURAS - INCREASE TO FEASIBILITY STUDIES LOAN

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HONDURAS - FEASIBILITY STUDY LOAN INCREASE

SUMMARY AND RECOMMENDATION

1. BORROWER: The Government of Honduras
EXECUTING AGENCY: Superior Council of Economic Planning
2. AMOUNT OF LOAN: This paper recommends an increase of \$500,000 in existing loan No. 522-L-015 to a total of \$1,000,000.
3. LOAN TERMS: Repayment in dollars within 40 years with 10 years' grace on the repayment of principal. Interest at 2% per annum during the grace period and 3% per annum thereafter for the new funds.
4. DESCRIPTION OF PROJECT: The funds provided by this loan will be used to finance dollar and local costs of sectoral or resource surveys, prefeasibility studies and feasibility studies of both government executed infrastructure projects and for certain private sector investment proposals. It is anticipated that the greater part of the funds will be used for feasibility studies of infrastructure projects. The National Economic Council will coordinate and supervise the loan by evaluating the study proposals submitted by the various ministries and determining which are of sufficient priority and timeliness to warrant presentation to A.I.D. for financing. Studies will be made for possible projects in roads, agricultural development including irrigation, industrialization and tourism.
5. PURPOSE OF PROJECT: The studies financed under this loan will enable the Government of Honduras to identify and determine the economic feasibility and potential of selected development projects as well as to provide adequate engineering, economic and financial data for applications for external financing of such projects.
6. BACKGROUND: This loan is an addition to Loan

522-L-015 which was authorized in February, 1966. One study, the Central Highway, has been financed under this loan to date and has required all but a small amount of the available funds. The Superior Council for Economic Planning has identified several additional studies it believes should be undertaken in the near future. The GOH planned to request an increase to the loan of almost \$2,500,000 but, after further discussions with the USAID about the studies to be financed, decided to request \$560,000 for studies which are in an advanced stage of planning.

7. OTHER FINANCING: The Eximbank on April 17, 1967 indicated it had no interest in this project. The IDB on May 5, 1967 and the IBRD on April 5, 1967 both stated they did not wish to consider loans for this purpose.
8. MISSION VIEWS: The Mission considers this a priority project and recommends its approval.
9. STATUTORY CRITERIA: The statutory criteria for this loan have been met (See Annex I).
10. ISSUES: None
11. RECOMMENDATION: Authorization of an increase in A.I.D. Loan 522-L-015 not to exceed \$500,000 to the Government of Honduras under the following terms and conditions:
 - (a) Repayment within forty (40) years from the first disbursement, including a grace period of ten (10) years;
 - (b) Interest of two percent (2%) during the grace period and three percent (3%) thereafter;
 - (c) Repayment of principal and interest in United States dollars;

(d) All conditions of Loan 522-L-015 shall apply to this increase;

(e) Such other conditions as A.I.D. may deem advisable.

Project Committee:

Loan Officers: Van Dyne McCutcheon
 : Paul W. Fritz
Engineer : William S. Gardner, Jr.
Economist : Al Zucca

Rate of Exchange:

One U.S. dollar (\$) = two Lempiras (L.)

SECTION I - DETAILED DESCRIPTION OF PROJECTA. BORROWER

The Borrower will be the Government of Honduras. The executing agency will be the Superior Council for Economic Planning (SCEP), successor to the National Economic Council (NEC), which will coordinate the requests for feasibility studies made by the various ministries and semi-autonomous agencies of the GOH. The NEC was established as an autonomous institution in 1955 to advise the President on matters of general economic policy and specifically to direct and coordinate development planning. It became the SCEP in late 1965 when it was reorganized and given additional responsibility. SCEP also has additional responsibilities in government administrative reform, budget review, coordination of certain statistical programs as related to planning, and overall coordination of foreign or other long-term lending to the various governmental agencies.

The following seven representatives comprise the governing council of SCEP:

Minister of Economy and Finance (President)
Minister of Communications and Public Works
Minister of Natural Resources
President of Central Bank
President of the National Development Bank
Representative of Private Sector
Representative of Private Sector - Labor

B. AREAS TO BE STUDIED

The loan application submitted by the SCEP lists nine specific projects under three major headings, agriculture, industry and transportation. USAID and the SCEP have previously discussed other specific studies which were not included in the application. Those included are considered to be of high priority and are in an advanced stage of planning. The principal areas to be studied, with background comments on each, are indicated below.

1. Transportation - Estimated amount \$80,000.

The inadequacy of the Honduran road system has been officially recognized by the Central American countries in the decision to allocate a greater than proportionate share of the Integration Fund to the Honduran "integration roads."

Construction work is already well underway on paving the North road, a major highway between Tegucigalpa and San Pedro Sula jointly financed by the IBRD, IDA and IDB. Other road sections either under construction or being studied will complete the basic trunk network of the country. A national secondary road plan has been developed and numerous roads are either under construction, being studied or designed.

The only road project to be included in this loan is an inter-connection of all the trunk routes radiating from Tegucigalpa. The North road entrance into the city is already badly congested and will become worse when paving is completed in two years. The South road is paved into Tegucigalpa; the East Road is presently under study by an English firm; final design is nearing completion for CABEI financing of construction of the road from Tegucigalpa to Danlí; the Central Highway study is nearing completion.

There are no present plans to avoid concentrating this traffic in Tegucigalpa and increasing the already severe congestion. The study would be directed toward interconnecting all the above routes without routing traffic through the city and would also determine ways to disperse traffic coming into the city.

2. Agriculture - Estimated amount \$230,000

a. Irrigation - \$130,000

Honduras has only about 2-1/2 percent of its cultivated land area under irrigation, a total of approximately 21,500 hectares. Much of the cultivated land is in production only during the rainy season. It is estimated that sufficient water is available to irrigate well over 300,000 hectares. The GOH plans to intensify irrigation efforts in various parts of the country over the next three years to bring an additional 30,000 hectares under irrigation. It also intends to carry out feasibility studies with its own resources for several small scale irrigation projects throughout the country. However, the GOH realizes that it needs external assistance for financing studies of larger, more complex irrigation projects by qualified engineering firms. Therefore, the application requests funding for a study of the Nacaome River basin of the Department of Valle in Southern Honduras. The basin encompasses approximately 10,000 hectares of potentially good agricultural land, connected to markets by existing roads.

Although the southern part of Honduras presently accounts for almost all of the cotton production of Honduras, nevertheless the level of economic activity of this zone lags behind the rest of the country. A 1966 survey performed by Stanford Research Institute on the "Development of the Southern Zone" recommends a diversification program through irrigated agriculture along with the development of food and feed crops and livestock. If undertaken, the feasibility study for irrigating the Nacaome river basin would be closely coordinated with the Crop Development and Diversification Program recently approved by the United Nations for financing by the U.N. Special Fund. Estimated costs of the Program, including the GOH contribution, are almost \$1.0 million. Through agricultural research, demonstration plots, training, and market surveys this U.N. Program will be an important step towards stimulating production for local consumption and reducing Honduras' reliance on exports of bananas, coffee and cotton for its foreign exchange earnings. Accordingly, before authorizing the Nacaome study, the USAID will, among other things, want to be satisfied that there would be adequate coordination between the development of the study and the U.N. Program.

Also, the USAID is familiar with a feasibility study for an irrigation and power project in the Choluteca region recently completed by a U.S. engineering firm under a CABEI financed contract. The irrigation aspects of this study covered plans for irrigating some 15,500 hectares located approximately 50 kilometers from Nacaome. The total estimated costs of the project, including the development of hydroelectric facilities, are \$32,750,000; the calculated benefit/cost ratio was 1.6:1 with an internal rate of return estimated at 8.5 percent. In view of the large investment required and the absence of large economic returns, the GOH has decided not to undertake the project for the time being. Although the Nacaome and Choluteca regions are very similar, the GOH believes that the proposed Nacaome study is essential to considering any further large scale irrigation projects in the South. Nevertheless the USAID will give further careful review to the need of a second large irrigation study in Southern Honduras before deciding whether to approve financing of the Nacaome study.

b. Natural Resource Surveys - \$100,000

The GOH has received bids on 1:20,000 scale aerial photography of some 12,500 kilometers of principal valley areas in the country. The lowest bid received was for \$58,000 from a qualified U.S. firm. The low bidder has been invited to come to Tegucigalpa by late December 1968 to sign the contract; mobilization should start shortly thereafter. The company should begin flying by January 15, 1969 to assure completion by the end of the dry season.

The photography is needed to determine agricultural and natural resources development priorities, particularly those related to agrarian reform projects. The photographs could also be used for property evaluation contemplated in the USAID's Natural Resources Evaluation loan being considered for possible FY 1969 or FY 1970 funding.

A.I.D. has participated in all stages of the bid for this photography, has approved the contractor and will have an opportunity to review and approve the contract before work begins. The GOH, to take advantage of this season's good flying weather, has decided to undertake the photography contract for its own account. It must be undertaken immediately or smoke from the spring forest fires and cloud-cover the remainder of the year will force a one year delay. A.I.D. has agreed to reimburse the GOH for all eligible payments under the contract if and when this increase to Loan 522-L-015 is approved. It is therefore proposed that funds from the increase be available to reimburse the GOH for expenses incurred under this contract.

3. Industry - Estimated Amount \$250,000

The GOH Action Plan establishes a goal of increasing the contribution of the industrial sector to GDP from about 13 percent in 1964 to 18 percent in 1971. They have included three particularly promising projects in the group of studies to be financed with this increase.

a. Forest Products - \$100,000

Almost half the land area of Honduras contains forest stands of commercial value. International Paper Co. and the GOH recently concluded an agreement under which IPC will establish a pulp and paper mill to produce linerboard, lumber and wood by-products. It is hoped that this will be a first step in planned utilization and regulation of these vast resources.

There is virtually no production of secondary wood products from Honduras' forests with the exception of limited domestic output of furniture and cabinet work, and two plywood plants.

The GOH has proposed a study to develop improved methods of drying and curing wood products, to identify marketable products which could be produced, to locate potential markets and do some preliminary design work. It is hoped through this method that private enterprise will be stimulated to invest in this promising area.

b. Foundries and Metal Working - \$50,000

GOH is reviewing possibilities of encouraging the development of a private steel industry to utilize this resource. In order to rationalize future private investment in the metals industry, and in order to integrate this investment with the needs of the CACM, the GOH proposes to undertake a pre-feasibility survey to determine the needs and potential for foundries and metal working industries for both ferrous and non-ferrous metals.

c. Tourism - \$100,000

The North Coast of Honduras has an enormous tourist potential which has not as yet been tapped. All the natural attractions of the Caribbean are present - sandy beaches, clear water, proximity to the U.S., etc. Punta Sal is located on a peninsula some 20 kms. northeast of the north cost city of Tela, and according to a Porter International study is one of the best Honduran sites for tourist facilities. The proposed study would focus on the potential for tourism and the specific projects needed, including transportation facilities, for developing tourist facilities at Punta Sal. The study would complement general surveys already undertaken by potential private investors.

4. Other Studies

The above studies have been specifically requested by the GOH but not all have been thoroughly reviewed by the USAID. In order to be able to undertake other high priority studies, the authorization should use the same project definition as the present loan which is "... for the conduct of certain sectoral or resource surveys, prefeasibility studies,

and feasibility studies, ...". Other studies considered high priority by the GOH include: sector studies of the development of the Guayape Valley and the Yojoa lake district, at an estimated cost of \$300,000 each; and prefeasibility investigations and feasibility studies for projects in the industrial sector, such as pork meat processing, rug making, and various other projects at an estimated total cost of \$150,000.

C. IMPLEMENTATION PLAN

The GOH, through the-SCEP, will submit requests to the Mission for the funding of each individual prefeasibility or feasibility study or survey. The prefeasibility studies or surveys will produce information upon which to determine and to select projects for further specific feasibility studies. In order to present all available information that would be of use to the Mission in evaluating each request by the SCEP, the request will include, but not be limited to, the following:

1. Prefeasibility Studies or Surveys

- a. Name and location or extent of investigation.
- b. Agency within the GOH that will sign and administer the contract.
- c. Short description of the objective of the investigation and how the resulting information can be used in the evaluation of the project's priority for further feasibility study, or for other priority studies.
- d. Description of previous studies and their availability. (If available to the SCEP they should be included in the request.)
- e. Scope of work for the contract.
- f. Contribution to be made to the investigation by the GOH.
- g. Estimated cost of the study, broken into dollar and local costs.
- h. Estimated time to make the investigation.
- i. If available, name(s) of engineering or technical consultants that the Borrower believes are qualified to do the investigation.

2. Feasibility Studies

- a. Name and location of the subproject.
- b. A short description of the subproject.

- c. The agency within the GOH that will sign and administer the contract.
- d. Description of previous studies and their availability. (If available to the SCEP, they should be included in the application.)
- e. Scope of work for the contract. (A.I.D. will assist the Borrower in the development of the scope of work since it must be approved by A.I.D. before contract negotiations can be initiated by the GOH.)
- f. Contribution to be made to the project by the GOH.
- g. Priority and general economic justification of the development project for which the feasibility study is to be undertaken and a general statement on the way it will be carried out (institution, mechanisms, financing, additional legislation, etc.)
- h. Estimated total cost of the study, with a breakdown, if possible, of foreign and local costs, showing estimated amount of loan funds required and GOH contribution.
- i. Estimated time for making the study.
- j. If available, name(s) of engineering or other technical consultants the Borrower believes are qualified to make the survey. (This is not necessary until after the subproject is approved but if available at the time of the application, it can be included.)

The USAID and the Regional Legal Adviser will have the responsibility for approving the project and the priorities selected by the GOH. The scopes of work for the contracts, the qualifications of the firms proposed and the contracts will be reviewed and approved by the USAID and the Regional Legal Adviser in accordance with its existing delegations of authority before negotiation by the GOH.

All contracts will be made with prequalified United States engineering or Central American technical firms and will be negotiated by the two parties without direct assistance from A.I.D. Joint ventures of U.S. firms and Central American firms will be acceptable for contracting as well as contracts directly with Central American firms.

Any feasibility survey application that may appear to qualify by CABEI Feasibility Loan will, upon determination by the USAID, be sent to CABEI by the SCEP to determine its interest. The USAID will not approve such a project until CABEI has indicated it has no interest.

In approving proposed subprojects, the USAID will ensure that: (a) the proposed development project is considered of high priority to Honduras' development; and (b) there is both serious intent on the part of the prospective investor to carry out the development project in the reasonably near future if it is judged feasible, and a reasonable probability that financing for the project will be made available, either from domestic or external resources.

It is anticipated that the Loan Agreement Increase will be signed in the summer of 1969, and ratified by the Honduran Congress before the end of 1969. In view of the fact the amount of the original GOH request has been substantially reduced, the SCEP should be able to execute all contracts under the amended loan within 18 months from the ratification of the Amendment with final payments to contractors being made by 12 to 18 months after the last contract is signed. Therefore the terminal disbursement date of the amended loan will be approximately December 31, 1972.

SECTION II - HISTORY OF LOAN

The original feasibility study loan in Honduras, No. 522-L-015, was signed on February 25, 1966, to finance sectoral or resource surveys, prefeasibility studies and feasibility studies of both government executed infrastructure projects and for certain private sector investments proposals. It was anticipated that the greater part of the funds would be used for feasibility studies of infrastructure projects.

The SCEP signed a cost plus fixed fee contract in September, 1967 with a U.S. engineering firm in the amount of \$357,879 for a feasibility study and preliminary plans for the 214 kilometer Central Highway. The order to proceed was issued in December, 1967. Until recently, progress has been poor due to circumstances both within the control of the firm and outside of its control. The results have been that the cost has gone up to an estimated \$485,000 and the completion date extended by several months.

Under the consultant's revised schedule, approved by the GOH and the USAID, all field work will be completed by the end of December. Aerial photo interpretation is being made by a qualified U.S. firm. The economic analysis has been completed. The GOH is now providing closer monitoring of the project and in view of the consultant's recent progress it now appears that the final report will be ready by May, 1969 and will be within the revised cost estimate.

The delays between the dates of signing the Loan Agreement, executing the first contract, and issuing the notice to proceed was indicative of the SCEP's limited capabilities during the early implementation stages of this first loan. To date, there have been three Executive Secretaries of the SCEP since the Loan Agreement was signed. The first Executive Secretary was replaced in June, 1967 by an individual who was also named the Director of the National Agrarian Institute at the same time. Although this individual is a highly capable administrator, it eventually became apparent that he lacked the time to meet the requirements of both positions. In August of 1968, the present Executive secretary of the SCEP was appointed.

He has been able to devote full time to his new duties and resolved the problems concerning the Central Highway feasibility study in an expeditious and technically sound manner. The USAID believes that the experience gained by the staff of the Planning Council over the last two years in this type of project and the willingness of the present Executive Secretary to act quickly and follow through will result in greatly improved performance in implementing a second tranche to the feasibility studies loan.

SECTION III. FINANCIAL AND ECONOMIC ANALYSIS

A. Loan Amount

The preliminary request from the SCEP was for a \$1,000,000 increase to the A.I.D. Feasibility Studies loan. The IRR requested approval of a loan up to \$1,000,000 which amount was approved (See Annex III).

Subsequently, the SCEP developed a more specific list of priority projects to be financed, with estimated total costs of almost \$2,500,000. However, experience with the first A.I.D. loan and further discussion on the proposed studies convinced the USAID that a smaller loan would be more within the present administrative capabilities of the GOH and the likely availability of funding for the projects themselves. Accordingly, the USAID is requesting \$500,000 at this time. As these funds are expended additional funding may well be sought.

We are financing 100% of the direct costs of the program in line with our usual policy. The GOH will provide support in the form of office space, vehicles, translators, etc., which we have not tried to quantify. Our strong interest in the program, the departure from local customs in undertaking costly and detailed studies of this nature, administrative difficulties and expense of financing small contracts from two sources, provide ample justification for A.I.D. financing of all direct costs.

In order to provide local currency for the Project, the GOH would have to secure legislative approval to amend the 1969 budget. This would be difficult in the face of reductions made by A.I.D. in the local currency component of the Agricultural Credit and Storage Loan (522-L-018) and the controls placed on Honduran exports of meat and brassieres.

B. Loan Terms and Local Currency Financing

The loan will be the major source of financing for this type of activity in Honduras. As with the first loan the loan increase will be used for both foreign exchange and local currency costs of the consulting contracts. Assuming a preponderance of U.S. consultants, it is anticipated that the local currency requirement will be minimal. The present contract with TCI is 65% dollar costs, a ratio which should hold with this addition. Not more than \$175,000 should be required for local cost financing. The GOH will be encouraged to provide supporting services to the project. Any local currency required in the operation of the loan will be generated through the special letter of credit procedure customarily used by the USAID to finance procurement of U.S. goods and services in exchange for local currency.

The loan terms and financing of minimal local costs, as proposed herein, can be justified by consideration of the GOH budget, debt service and balance of payments situations in relation to its development plan. This subject was analyzed thoroughly in the Capital Assistance Paper for the Agricultural Credit & Storage Loan, written only a few months ago. The analyses and conclusions contained therein support the granting of a non-revenue producing loan such as this on the most lenient terms possible.

There are no U.S.-controlled local funds available for this project except those that are generated through the special letter of credit procedure.

The U.S. receives approximately \$575,000 equivalent annually from repayments of two loans repayable in local currency. These repayments cover only a small portion of U.S. Government local currency needs in Honduras, which were almost \$4,500,000 in 1968.

All two-step local currency repayments have been committed through CY 1970. Only approximately the equivalent of \$22,000 is expected to be available in CY 1971. The GOH uses all two-step funds to finance revenue producing projects since it must in time use the funds to repay A.I.D. There is no PL-480 program in Honduras and none planned.

C. Place of Project in the Program

A.I.D. strategy in Honduras is geared to increasing the absorptive capacity of the Public Sector by: (1) improving the general efficiency of public administration; (2) assisting in the preparation of detailed economic planning and its execution; and (3) advising in the administration of revenue collection. It is directed primarily at the long range objective of establishing the human and institutional base for more rapid development. It recognizes the need for substantial inputs of economic resources to construct the infrastructure in which the economy will develop in the future. This loan will contribute directly in helping to increase the planning capacity of the GOH by providing detailed data on specific projects, thereby enabling the logical and long range planning necessary to achieve satisfactory growth.

D. Economic Analysis

1. Setting - Honduras is still considered the poorest country in Central America both in terms of natural and human resources, and is among the poorest in Latin America. A rather rapid rate of economic growth in the recent past, which in 1966 and 1967 averaged 6.7 percent in current prices, was mainly due to a moderately strong performance of agricultural exports. Between 1962 and 1967 the export sector accounted for more than one-third of the total increase in GNP and made up for lagging investment expenditures in the public sector. This lag is mainly attributable to delays in project preparation partly due to the scarcity of qualified personnel to push investment projects at the administrative and executive levels.

2. Investment Absorption Capacity of the GOH
Experience thus far in 1968 indicates that the GOH is substantially overcoming its past problem of public under investment. During the first three quarters of 1968, utilization of public loans from international public and private sources amounted to more than \$ 10.0 million. However, during the same period the GOH signed loan agreements for \$ 11.5 million for the Rio Lindo Hydro-electric project (IBRD/IDA) and \$ 4.0 million for a road from Puerto Cortes to the Guatemala frontier (CABEI). As of September 30, 1968 the loan pipeline amounted to \$ 85.8 million against a total level of lending from public and private international sources to the GOH of \$ 164 million.

Some \$ 45.1 million, or more than 52 percent, of the loan pipeline is accounted for by undisbursed balances of loans for six large road construction projects. Construction is underway on all phases of the North road; the paving contract for the Western Highway has been signed and work will begin in January, 1969; construction has begun on one section of the Tela-La Ceiba road and the contract has been awarded for the remaining section; the supervisory engineering contractor for the San Pedro Sula-Tela road has been selected and the contract will be signed in early January 1969; construction of the Puerto Cortes-Guatemala frontier road is scheduled to begin in May, 1969; problems under the A.I.D. Farm-to-Market Access Road loan have been resolved which will enable the remaining construction contracts to be executed in the Spring of 1969. A full time Minister of Public Works and Communications was appointed in August, 1968. His previous performance as the Director of INVA, the Honduran housing institute, and his actions to date as Minister are further encouraging indications that the pipeline of international loans for major infrastructure projects will be drawn down within a reasonable time schedule.

Approximately three quarters of the balance of the loan pipeline is accounted for by the undisbursed balance of the following loans: A.I.D. Secondary Education; IBRD/IDA Rio Lindo Hydro-electric; IBRD Puerto Cortes port expansion; IDB Agricultural Loan to the ENF; and IDB Labor Union Housing Project. For other than the recently signed loans for the Rio Lindo Hydro-electric project, disbursements have already begun under these loans.

As the GOH further improves performance of utilizing its existing pipeline, it will need additional, well conceived project proposals in order to carry out meaningful development planning. The proposed increase to the feasibility studies loan will help assure a continued availability of priority development projects with sufficiently detailed analyses to enable sound decision making.

3. Financing of Future Investment. If Honduras is to achieve her economic growth goals and to develop at Alliance for Progress rates, much greater public investment is necessary. The GOH's Immediate Action Plan for 1968-71 calls for \$ 222 million in new investment during the period. Domestic resources will finance \$ 56 million of this investment while foreign financial sources are expected to provide

\$ 166 million for the period, or about \$ 42 million annually. To the extent foreign credits are not available at planned levels, the GOH would be forced to rely on the current account surplus and domestic borrowings to meet its development goals.

The present tax structure is rather inflexible and the partial tax reform of 1963, which contributed to a rapid growth in revenues between 1964 and 1967, lost much of its effectiveness. Nevertheless, as a positive gain the proportion of direct taxes has increased from 17.4 percent of the total tax revenue in 1960 to 32.3 percent in 1967 and income tax collections have increased substantially through improved administration carried out with the assistance of USAID's IRS PASA Team. Honduras still depends heavily on indirect taxes as do all developing countries, with import duties representing about 40 percent of the total tax receipts.

The GOH is fully aware of the shortcomings of its present tax system considering future investment needs. It is reviewing measures to limit annual increases of the current account expenditures to about 9.4 percent and reforms to: remove present deficiencies in tax investigation; apply control systems for collection of direct taxes; revise tax exemptions and tariffs; and improve the tax billing system. All these measures and reforms, though badly needed, will not increase current and capital revenues to the projected levels of public expenditures including capital outlay. To cope with the financial requirements of the projected investment program, the GOH is also undertaking a series of new tax measures based upon agreement with the Central American Common Market Countries (CACM) under the San José Protocol. These measures will include a 30 percent import tax surcharge on most imports external to CACM and consumption taxes on 26 categories of items imported from CACM with a maximum tax rate of 20 percent. The new tax program is expected to add about \$ 7 million annually to the GOH revenues, which is to be used almost exclusively for public investment and amortization of debt.

Measures necessary for progress have been taken in improvement of ability to absorb investment and in the regional tax measures. The support evidenced by this loan increase has been earned by Honduran action; it is also needed to assure continued improvement.

April 11, 1969

HONDURAS - INCREASE TO FEASIBILITY STUDIES LOAN

CHECKLIST OF STATUTORY CRITERIA

(Alliance for Progress)

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

The following abbreviations are used:

FAA - Foreign Assistance Act of 1961, as amended by the Foreign Assistance Act of 1968.

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

COUNTRY PERFORMANCE

Progress Towards Country Goals

1. FAA §.208; §.251(b).

A. Describe extent to which country is:

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

(1) Loan 522-L-018 was made to support such a program.

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

(2) The GOH is creating a favorable climate for foreign and domestic private enterprise and investment, through its stable monetary and fiscal policies, lack of foreign exchange restrictions, and participation in the A.I.D. investment guaranty program.

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

(3) The GOH's active encouragement of cooperative organizations is an indication of its interest in increasing the public's role in the development process.

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

(4) The GOH is making allocations necessary to support its development program.

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

(b) The GOH does not appear to be diverting budgetary resources for unnecessary military expenditures or for intervention in affairs of other free and independent nations.

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

(5) The GOH will provide assistance to contractors under the loan.

- (6) *Making economic, social, and political reforms such as tax collection improvements and changes in land tenure arrangements, and making progress toward respect for the rule of law, freedom of expression and of the press, and recognizing the importance of individual freedom, initiative, and private enterprise.* (6) The GOH is making economic social and political reforms; there exists freedom of expression and of the press; plans to improve tax collection and land tenure patterns are being initiated.
- (7) *Adhering to the principles of the Act of Bogota and Charter of Punta del Este.* (7) The GOH is satisfactorily adhering to such principles.
- (8) *Attempting to repatriate capital invested in other countries by its own citizens.* (8) The GOH has consistently followed policies that encourage the repatriation of capital invested in other countries by its own citizens.
- (9) *Otherwise responding to the vital economic, political, and social concerns of its people, and demonstrating a clear determination to take effective self-help measures.* (9) The GOH is undertaking effective self-help measures in response to vital concerns of its people.

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

Treatment of U.S. Citizens

2. FAA §.620(c). *If assistance is to government, is the government liable as debtor or unconditional guarantor on any debt to a U.S. citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) debt is not denied or contested by such government?*
 2. There is no evidence of such GOH indebtedness.

3. FAA §.620(e)(1). *If assistance is to a government, has it (including government agencies or subdivisions) taken any action which has the effect of nationalizing, expropriating, or otherwise seizing-ownership or control of property of U.S. citizens or entities beneficially owned by them without taking steps to discharge its obligations toward such citizens or entities?*
 3. There is no evidence of such action.

4. App. §.106. *If country attempts to create distinctions because of their race or religion among Americans in granting personal or commercial access or other rights otherwise available to U.S. citizens generally, what steps (will be) (have been) taken during loan negotiations to influence elimination of such distinctions?*
 4. Honduras does not attempt to create distinctions among Americans in granting personal or commercial access or other rights otherwise available to U.S. citizens generally because of their race or religion.

5. FAA §.620(o); Fishermen's Protective Act. §.5. If country has seized, or imposed any penalty or sanction against, any U.S. fishing vessel on account of its fishing activities in international waters. 5. Honduras has not seized or imposed sanction on any U.S. fishing vessels on account of its activities in international waters.

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

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

Relations with U.S. Government and Other Nations

6. FAA §.620(d). If assistance is for any productive enterprise which will compete in the U.S. with U.S. enterprise, is there an agreement by the recipient country to prevent export to the U.S. of more than 20% of the enterprise's annual production during the life of the loan? 6. This loan does not fund assistance to a productive enterprise.
7. FAA §.620(j). Has the country permitted, or failed to take adequate measures to prevent, the damage or destruction by mob action, of U.S. property? 7. Honduras has not permitted, and takes adequate measures to prevent damage or destruction of U.S. property by mob action.

8. FAA §.620(l). *If the country has failed to institute the investment guaranty program for the specific risks of expropriation, in convertibility or confiscation, has the A.I.D. administration within the past year considered denying assistance to such government for this reason?* 8. Honduras has signed and instituted such an agreement.
9. FAA §.620(q). *Is the government of the recipient country in default on interest or principal of any A.I.D. loan to the country?* 9. Honduras is not in default under any A.I.D. loan to the country.
10. FAA §.620(t). *Has the country severed diplomatic relations with U.S.? If so, have they been resumed and have new bilateral assistance agreements been negotiated and entered into since such resumption?* 10. Honduras has consistently maintained diplomatic relations with the United States.
11. FAA §.620(u). *What is the payment status of the country's U.N. obligations? If the country is in arrears, were such arrearage taken into account by the A.I.D. Administrator in determining the current A.I.D. Operating Year Budget?* 11. It does not appear that Honduras is delinquent on its U.N. obligations.
12. FAA §.620(a); App. §.107(a) and (b). *Does recipient country furnish assistance to Cuba, sell strategic material to Cuba, or permit ships or aircraft under its flag to carry cargoes to or from Cuba.* 12. Honduras has complied with the prohibitions.

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

Military Expenditures

17. FAA §.620(s). ^(a) *What percentage of country budget is for military expenditures?* ^(b) *How much of foreign exchange resources spent on military equipment?* ^(c) *Is U.S. P.L. 480 or development assistance used for military purposes?* ^(d) *Are country's resources devoted to unnecessary military expenditures to a degree which materially interferes with* 17(a) 8.9% in 1968.
(b) Zero in 1967; N/A for 1968.
(c) No.
(d) No.

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

18. FAA §.620(v). App. §.119. *How much spent by country during current U.S. fiscal year for sophisticated military equipment purchased since January 1, 1968? Has corresponding amount been deducted from current OYB, or is the weapons purchase determined by the President to be important to U.S. national security? (Responses to these questions to be coordinated with PPC/MAS.)*
18. Honduras has spent no funds during the current U.S. fiscal year for sophisticated military equipment.

CONDITIONS OF THE LOAN

General Soundness

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

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21. FAA §.251(b). Information and conclusion on capacity of the country to repay a loan, including reasonableness of repayment prospects.
21. It appears reasonably certain that the Country's dollar reserves will continue to be maintained at sufficient level to enable the country to meet the reasonable repayment requirements of the loan.
22. FAA §.611(a)(1). Prior to signing of loan will there be (a) engineering, financial, and other plans necessary to carry out the assistance and (b) a reasonably firm estimate of the cost to the U.S. of the assistance?
22. Engineering, financial and other plans necessary for each study will be reviewed before approval of any study. Reasonably firm cost estimates will be developed before approval of any study.
23. FAA §.611(a)(2). If further legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of purposes of loan?
23. No such legislation is required.
24. FAA §.611(e). If loan is for capital assistance, and all U.S. assistance to project now exceeds \$1 million, has Mission Director certified the country's capability effectively to maintain and utilize the project?
24. This required certification is contained in Annex II.
25. FAA §.251(b). Information and conclusion on availability of financing from other free-world sources, including private sources within the United States.
25. No other sources of financing have been found. See Summary and Recommendations.

Loan's Relationship to Achievement
of Country and Regional Goals

26. FAA §.207; §.251(a). Extent to which assistance reflects appropriate emphasis on; (a) encouraging development of democratic economic, political, and social institutions; (b) self-help in meeting the country's food needs; (c) improving availability of trained manpower in the country; (d) programs designed to meet the country's health needs, or (e) other important areas of economic, political, and social development, including industry; free labor unions, cooperatives, and voluntary agencies; transportation and communication; planning and public administration; urban development; and modernization of existing laws.
26. Emphasis is not placed
(a) on institutional development.
(b) Agricultural studies will contribute to this.
(c) Little emphasis is placed on this.
(d) Emphasis is not placed on health in this loan.
(e) It is anticipated that industry and transportation will be affected by the loan.
27. FAA §.209. Is project susceptible of execution as part of regional project? If so why is project not so executed?
27. The project is not susceptible of execution as part of regional project; however, some of the studies may contribute to regional development.
28. FAA §.251(b)(3). Information and conclusion on activity's relationship to, and consistency with, other development activities, and its contribution to realizable long-range objectives.
28. The studies to be undertaken are consistent with Honduras's development activities and will contribute to realization of its development program.

29. FAA §.251(D)(7). *Information and conclusion on whether or not the activity to be financed will contribute to the achievement of self-sustaining growth.*
29. The activity will identify specific projects which will contribute to self-sustaining growth.
30. FAA §.281(a). *Describe extent to which the loan will contribute to the objective of assuring maximum participation in the task of economic development on the part of the people of the country, through the encouragement of democratic, private, and local governmental institutions.*
30. Emphasis is not placed on this provision.
31. FAA §.281(b). *Describe extent to which program recognizes the particular needs, desires, and capacities of the people of the country; utilizes the country's intellectual resources to encourage national development; and supports civic education and training in skills required for effective participation in governmental and political processes essential to self-government.*
31. The program is designed to meet the particular needs, desires and capacities of the people of the country, and to encourage institutional development.

32. FAA §. 301(a). Information and conclusions whether loan will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; (c) encourage development and use of cooperatives, credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture, and commerce; and (f) strengthen free labor unions.
33. FAA §. 619. If assistance is for newly independent country; is it furnished through multilateral organizations or plans to the maximum extent appropriate?
34. FAA §. 251(h). Information and conclusion on whether the activity is consistent with the findings and recommendations of the Inter-American Committee for the Alliance for Progress in its annual review of national development activities.
35. FAA §. 251(g). Information and conclusion on use of loan to assist in promoting the cooperative movement in Latin America.
32. It is anticipated that the loan will affect the balanced development of the Honduran economy in agriculture, transportation and industry. The studies will identify sound projects and encourage the flow of investment into these areas.
33. Honduras is not a newly independent country.
34. The project is consistent with the CIAP recommendations.
35. Emphasis is not placed on this provision.

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

36. Emphasis is not placed on this provision although individual studies will take it into account.

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

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

37. This project has no significant direct effects on the U.S. economy. Assistance will be furnished in a manner as consistent as possible with improving the U.S. balance of payments. (See Section III.)

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

38. The loan will finance the procurement of some goods and services from U.S. private sources, thereby encouraging private U.S. participation.

39. FAA §.601(d). *If a capital project, are engineering and professional services of U.S. firms and their affiliates used to the maximum extent consistent with the national interest?* 39. N.A.
40. FAA §.602. *Information and conclusion whether U.S. small business will participate equitably in the furnishing of goods and services finance by the loan.* 40. Small business notification in accordance with A.I.D. procedure will be complied with.
41. FAA §.620(h). *Will the loan promote or assist the foreign aid projects or activities of the Communist-Bloc countries?* 41. No assistance under the loan will promote any project or activity of a Communist-Bloc country.
42. FAA §.621. *If technical assistance is financed by the loan, information and conclusion whether such assistance will be furnished to the fullest extent practicable as goods and professional and other services from private enterprise on a contract basis. If the facilities of other Federal agencies will be utilized, information and conclusion on whether they are particularly suitable, are not competitive with private enterprise, and can be made available without undue interference with domestic programs.* 42. Technical assistance provided under the loan to the fullest extent practicable will utilize goods and professional and other services from private enterprise on a contract basis. It is not anticipated that loan funds will finance the use of other Federal agencies.

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

Loan's Compliance with Specific Requirements

44. FAA §.201(d). Is interest rate of loan at least 2% per annum during grace period and at least 3% per annum thereafter?
44. Yes.
45. FAA §.608(a). Information on measures to be taken to utilize U.S. Government excess personal property in lieu of the procurement of new items.
45. N/A.
46. FAA §.604(a); App. §.108. Will all commodity procurement financed under the loan be from U.S. except as otherwise determined by the President?
46. Commodities may be procured in the United States or from any member country of the Central American Common Market; statutory reporting requirements will be met.

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47. FAA §.604(b). What provision is made to prevent financing commodity procurement in bulk at prices higher than adjusted U.S. market price?
47. No such procurement is contemplated under the loan.
48. FAA §.604(d). If the host country discriminates against U.S. marine insurance companies, will loan agreement require that marine insurance be placed in the U.S. on commodities financed by the loan?
48. Honduras does not discriminate against U.S. companies.
49. FAA §.604(e). If off-shore procurement of agricultural commodity or product is to be financed, is there provision against such procurement when the domestic price of such commodity is less than parity?
49. N/A.
50. FAA §.611(b); App. §.101. If loan finances water or water-related land resource construction project or program, is there a benefit-cost computation made, insofar as practicable, in accordance with the procedures set forth in the Memorandum of the President dated May 15, 1962?
50. N/A.
51. FAA §.611(c). If contracts for construction are to be financed, what provision will be made that they be let on a competitive basis to maximum extent practicable?
51. No construction contracts will be financed under the loan.

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52. FAA §.620(g). *What provision is there against use of subject assistance to compensate owners for expropriated or nationalized property?*
52. The loan will not be used for such purposes.
53. FAA §.612(b); §.636(h). *Describe steps taken to assure that, to the maximum extent possible, the country is contributing local currencies to meet the cost of contractual and other services, and foreign currencies owned by the U.S. are utilized to meet the cost of contractual and other services.*
53. No foreign currencies owned by the United States are available for this loan. The GOH will contribute space and services to the extent possible. (See Section III A.)
54. App. §.104. *Will any loan funds be used to pay pensions, etc., for military personnel?*
54. Loan funds will not be used for this purpose.
55. App. §.111. *Compliance with requirements for security clearance of U.S. citizen contract personnel.*
55. This will be complied with.

56. App. §.112. *If loan is for capital project, is there provision for A.I.D. approval of all contractors and contract terms?*
56. All contractors and the terms of all the contracts will be approved by A.I.D. However, loan funds will not be used to finance capital projects.
57. App. §.114. *Will any loan funds be used to pay U.N. assessments?*
57. Loan funds will not be used for this purpose.
58. App. §.115. *Compliance with regulations on employment of U.S. and local personnel for funds obligated after April 30, 1964 (Regulation 7).*
58. This will be complied with.
59. FAA §.636(i). *Will any loan funds be used to finance purchase, long-term lease, or exchange of motor vehicle manufactured outside the United States, or any guaranty of such a transaction?*
59. No.
60. App. §.401. *Will any loan funds be used for publicity or propaganda purposes within U.S. not authorized by the Congress?*
60. No.

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

61. N/A.

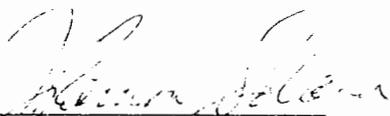
INCREASE FOR FEASIBILITY STUDIES LOAN

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

I, J. Ramon Solana, the principal officer of the Agency for International Development in Honduras, having taken into account among other things, the maintenance and utilization of projects in Honduras previously financed or assisted by the United States, do hereby certify that in my judgement the Government of Honduras has both the financial capability and the human resources capability to effectively maintain and utilize the capital assistance project of the increase to the feasibility studies loan.

This judgement is based in the facts that:

1. The loan executing agency, the Superior Council for Economic Planning (SCEP), has demonstrated an improved capability for carrying out projects of this nature;
2. Arrangements will be made to improve further the implementation capability of the SCEP by providing increased coordination with other GOH entities with specialized abilities to assist in monitoring the activities under the loan; and
3. The project will be executed through private consultants to be prequalified by the GOH and approved by the USAID.


J. Ramon Solana

December 18, 1968

MINUTES

L.A. CAPITAL ASSISTANCE EXECUTIVE COMMITTEE MEETING

March 30, 1967

HONDURAS - Feasibility Study Loan Increase - IRR
(LA-CAEC/P-67765)
Ref: A.I.D. Loan 522-L-015

The CAEC authorized an intensive review of the subject loan request, for up to \$1 million, subject to the following considerations:

1. It was the feeling of the Committee that general studies on municipal government organization are of marginal value unless they are practically oriented. Therefore, if any studies are to be undertaken on urban-related developmental problems, they ought to be so conceived as to result in feasible plans of action.
2. The loan paper should include a provision requiring the Economic Planning Council to coordinate any proposed feasibility studies with the other international lending agencies, in particular the Inter-American Development Bank.

DRAFT
LOAN AUTHORIZATION

Provided from: Alliance for Progress

HONDURAS: Feasibility Studies (Increase)

Pursuant to the authority vested in the Deputy U.S. Coordinator, Alliance for Progress by the Foreign Assistance Act of 1961, as amended, and the delegations of authority issued thereunder, I hereby authorize the establishment of a loan pursuant to Part 1, Chapter 2, Title VI, Alliance for Progress, of said Act, to the Government of the Republic of Honduras ("Borrower") of not to exceed one million dollars (\$1,000,000) to finance the United States dollar and local currency costs of equipment, material, and services necessary for the conduct of certain sectoral or resource surveys, prefeasibility studies, and feasibility studies, this loan to be subject to the following terms and conditions:

1. Interest and Terms of Repayment:

(a) Borrower shall repay the loan to the Agency for International Development ("A.I.D.") in United States dollars within forty (40) years from the first disbursement under the loan, including a grace period not to exceed ten (10) years.

(b) The Borrower shall pay interest to A.I.D. in United States dollars on the disbursed balance of five hundred thousand dollars (\$500,000) of one (1) percent per annum during the grace period and two and one-half (1 1/2) percent per annum thereafter;

(c) The Borrower shall pay interest to A.I.D. in United States dollars on the disbursed balance of the loan in excess of five hundred thousand dollars (500,000) of two percent (2%) per annum during the grace period and three percent (3%) thereafter.

2. Other Terms and Conditions:

(a) All sub-projects will be subject to prior approval by A.I.D.

(b) All sub-projects which in the judgement of A.I.D. may be eligible for financing by the Central American Bank for Economic Integration (CABEI) will be submitted by Borrower to that organization with a request for financing before approval for financing under this loan will be given by A.I.D.

(c) Equipment, materials and services (except shipping and marine insurance) financed under the loan shall have their origin in and be procured from the United States or Member Countries of the Central American Common Market. Shipping financed under the loan shall be procured from the United States, and marine insurance financed under the loan shall be placed in the United States with a company authorized to do marine insurance business in any state of the United States.

(d) United States dollars utilized under the loan to finance local currency costs shall be made available to Borrower or its designee through Special Letters of Credit and shall be used only for procurement in the United States.

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

Deputy U.S. Coordinator

Date