

UNITED STATES GOVERNMENT

DUPLICATE

Memorandum

FD- AAI - 581

TO : LA/DR

*Mary Grant*  
*LA/CP*  
*3917*  
*U.S.*  
*5960037006801*

DATE: 9/26/77

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FROM : Barry Sidman, Deputy Director, ROCAP *[Signature]*

SUBJECT: Loan Completion Review Report on AID Loan No. 596-L-009  
(CAMSF) -- Supplement

ROCAP's Dec. 10, 1975 Report on the loan to the Central American Monetary Stabilization Fund indicated that developments would be reported from time to time, although formal monitoring would be terminated in 1976.

The enclosed memorandum dated Sept. 26, 1977 by ROCAP's Economic Officer updates the earlier report, and may be of interest.

cc: ARA/ECP  
LA/DP (Attn: B. Goldstein)

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UNITED STATES GOVERNMENT

# Memorandum

UNCLASSIFIED

TO : Mr. Barry Sidman, Deputy Director

DATE: September 26, 1977

FROM : Clark Joel, Regional Economic Officer *CJoel*  
Gustavo A. Ruiz, Assistant to REO

SUBJECT: Latest Developments on Central American Monetary Stabilization Fund (CAMSF - Loan 009)

Following a brief background statement on the \$10 million AID loan to the Central American Monetary Stabilization Fund, this paper will summarize latest developments with respect to the Fund's paid-in capital, loans and credit lines, prospects for further loans from the CAMSF, and assessment of prospects for further progress in pooling the region's foreign exchange reserves.

## Background

On October 1, 1969, the five central banks of the region established the Central American Monetary Stabilization Fund (CAMSF) to a) create a mechanism for mutual balance of payments assistance to a member country experiencing a loss of reserves as a result of short-term disequilibrium in its balance of payments; and b) to assist with the gradual process of establishing a monetary union and broadening the base of regional economic integration. It was hoped that the CAMSF would cause the region's central banks to partially pool their foreign exchange reserves, and that the Fund would strengthen the hand of the Monetary Council in harmonizing the monetary, fiscal and foreign exchange policies of the five countries. It was also hoped that the Fund would contribute to the maintenance of exchange stability and currency convertibility by providing more time to the monetary authorities to adopt corrective balance of payments measures, thus relieving the need for the countries to adopt unilateral measures that would restrict intraregional trade, such as exchange controls or unilateral devaluation.

In support of this project, AID provided to the five central banks of the region a loan for \$10 million in August 1970. The CAMSF made no loans until August of 1975. This was due to several factors, including the fact that the balance-of-payments position of several of the C.A. countries, notably Guatemala, El Salvador

and Nicaragua, was relatively strong through 1973; political problems and conflicts that discouraged Honduras and Costa Rica from applying for loans from the CAMSF; and the structure of the Fund itself which made it difficult for member countries to borrow.

To facilitate access of the Fund's resources, the Fund was restructured in August, 1974. This restructuring, together with a substantial deterioration in the current account situation of the C.A. region, resulted in the submission of loan applications from three C.A. countries in August and September, 1975. Honduras and El Salvador each received a loan for \$25 million (for 5 and 8 years, respectively) while Nicaragua applied for and received a short-term loan for \$10 million (maturity of one year). The full amount of the \$10 million AID loan was transferred to the Bank of Guatemala on October 15 for use in connection with the loan to Honduras. All three loans were drawn down before December 31, 1975. No new loans were solicited since then.

#### Paid-in Capital

The Fund's paid-in capital, consisting of capital contributions plus reinvested earnings, now stands at \$37.9 million, up from \$25 million on July 31, 1976 and \$18 million at the end of 1975. The Executive Secretary of the CAMSF expects that the Fund's paid-in capital will reach \$50 million by December 31, 1977, which is equal to the Fund's total authorized capital to-date.

#### Loans and Credit Lines Available to the Fund

No new credit lines were negotiated during the year, as none were needed. Total loans and credit lines thus remain at the same level of \$102 million, derived from the following sources:

<u>S o u r c e</u>	<u>U.S. \$ Millions</u>
AID Loan	10.0
Venezuelan's Investment Fund	50.0
Central Bank of Mexico	10.0
Wells Fargo Bank	20.0
Deutsche Sudamerikanische Bank	8.0
Union Bank of Switzerland	<u>4.0</u>
	102.0

Loans Granted by the Fund

No new loans were granted by the Fund during 1976 and 1977 owing to the strong balance of payments position of the region. Repayments by El Salvador, Honduras and Nicaragua proceeded according to schedule. The amounts of the loans granted and outstanding (as of August 31, 1977) are as follows:

<u>Country</u>	<u>Amount of Loan</u>	<u>Balance Outstanding</u>
El Salvador	CA\$ 25 million	CA\$ 16.9 million
Honduras	CA\$ 25 million	CA\$ 10.0 million
Nicaragua	CA\$ 10 million	-0-

The balance outstanding of the loan granted to El Salvador is \$6.9 million above that of Honduras because the loan to El Salvador carried an 8-year term, compared with a 5-year term of the loan to Honduras.

Prospects for the Fund's Use

Owing to the region's favorable balance of payments position this year and the record level of international reserves achieved as a result of favorable coffee prices and substantial capital inflows, it is doubtful that new loan applications will be received by the Fund in either 1977 or 1978. However, a substantial reduction in coffee prices, if it should occur, would have serious adverse balance of payments consequences, as noted in ROCAP's "Economic Assessment of the CACM Region"<sup>1/</sup> and might well force recourse to the Fund's resources in late 78 or 79.

The Executive Secretary of the C.A. Monetary Council indicated that a study of prospects for coffee prices is currently under way and that the Council will have a better idea of prospects for the Fund's utilization by the end of the year.

Comment

The CAMSF has made substantial progress since its inception in 1969. When it was created, its total paid-in capital amounted to only \$5 million. This was raised to \$10 million as a condition

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<sup>1/</sup> Report by Clark Joel dated August 29, 1977, pages 6-14.

for the \$10 million AID loan granted in 1970. It now stands at \$38 million and is expected to reach \$50 million by the end of this year. It is clear that the Fund has achieved its primary objective of providing the C.A. Monetary Council with an important instrument to help the C.A. countries finance temporary balance of payments deficits. The record of mutual consultation and coordination by the members of the C.A. Monetary Council in recent years has also been very encouraging.

Still, the Fund has pooled only a small fraction of the region's total foreign exchange reserves. As of June 30, 1977, the region's total foreign exchange reserves stood at \$1,755 million. Thus, even if the year-end goal of a \$50 million capitalization is achieved, the foreign exchange pooled by the Fund would amount to only 2.9% of the region's total foreign exchange resources. A major aspect of the problem is that the C.A. countries consistently follow the procedure of equal contributions to the capitalization of integration institutions. This means that the amount that each country can contribute to an organization like the CAMSF is limited by the willingness and capacity of the weakest member to contribute. There is nothing, of course, that would prevent a country from making voluntary deposits in excess of the capitalization requirement, but it would have little incentive to do so since this will not enhance its voting power in the Fund's management. Still, the Executive Secretary believes that C.A. countries in a strong foreign exchange position could be persuaded to make voluntary deposits in the Fund in an emergency situation.

REO:CJoel:sr