

ISN 378

AGENCY FOR INTERNATIONAL DEVELOPMENT

PROJECT DATA SHEET

1. TRANSACTION CODE

A = Add
 C = Change
 D = Delete

Amendment Number

DOCUMENT CODE

3

2. COUNTRY/ENTITY

PERU

3. PROJECT NUMBER

527-0241

4. BUREAU/OFFICE

LA

05

5. PROJECT TITLE (maximum 40 characters)

Urban Small Enterprises Development

6. PROJECT ASSISTANCE COMPLETION DATE (PACD)

MM DD YY

7. ESTIMATED DATE OF OBLIGATION
(Under 'B.' below, enter 1, 2, 3, or 4)

A. Initial FY 82

B. Quarter 3

C. Final FY 83

8. COSTS (\$000 OR EQUIVALENT \$1 =)

A. FUNDING SOURCE	FIRST FY 82			LIFE OF PROJECT		
	B. FX	C. L/C	D. Total	E. FX	F. L/C	G. Total
AID Appropriated Total	155	4,845	5,000	180	9,820	10,000
(Grant)	()	()	()	()	()	()
(Loan)	(155)	(4,845)	(5,000)	(180)	(9,820)	(10,000)
Other U.S.						
1.						
2.						
Host Country		2,400	2,400		3,500	3,500
Other Donor(s)						
TOTALS	155	7,245	7,400	180	9,820	10,000

9. SCHEDULE OF AID FUNDING (\$000)

A. APPROPRIATION	B. PRIMARY PURPOSE CODE	C. PRIMARY TECH. CODE		D. OBLIGATIONS TO DATE		E. AMOUNT APPROVED THIS ACTION		F. LIFE OF PROJECT	
		1. Grant	2. Loan	1. Grant	2. Loan	1. Grant	2. Loan	1. Grant	2. Loan
(1)	710		840						
(2)									
(3)							5,000		10,000
(4)									
TOTALS							5,000		10,000

10. SECONDARY TECHNICAL CODES (maximum 6 codes of 3 positions each)

869

11. SECONDARY PURPOSE CODE

12. SPECIAL CONCERNS CODES (maximum 7 codes of 4 positions each)

A. Code

BU

B. Amount

13. PROJECT PURPOSE (maximum 480 characters)

To institutionalize through new policies and operational initiatives a self-sustaining credit and technical assistance program for small urban enterprises.

14. SCHEDULED EVALUATIONS

Interim MM YY MM YY Final MM YY

15. SOURCE/ORIGIN OF GOODS AND SERVICES

000 941 Local Other (Specify)

16. AMENDMENTS/NATURE OF CHANGE PROPOSED (This is page 1 of a _____ page PP Amendment)

17. APPROVED BY

Signature *Malcolm Butler*
Malcolm Butler

Title
Director

Date Signed
MM DD YY
3 5 82

18. DATE DOCUMENT RECEIVED IN AID/W, OR FOR AID/W DOCUMENTS, DATE OF DISTRIBUTION

MM DD YY

URBAN SMALL ENTERPRISE DEVELOPMENT

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PROJECT ANNEXES

Annex I STANDARD ATTACHMENTS

- Exhibit
- A. Statutory Checklist
 - B. Draft Authorization
 - C. Director's 611 (e) Certification
 - D. Borrower Loan Request
 - E. Logical Framework Matrix
 - F. PID DAEC Guidance Message
 - G. Environmental Threshold Decision

Annex II. PROJECT EXHIBITS

- Exhibit
- A. Map
 - B. Summary Rural Enterprises Evaluation
 - C. Rural Enterprises Evaluation *
 - D. Promotional Material on Indexation
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* For reasons of bulk, Exhibit C and I of Annex II are not included as part of the Project Paper. They are available in the files of LAC/DR and USAID/Peru.

PART I. SUMMARY AND RECOMMENDATIONS

A. Recommendation

The Project Development Committee recommends that a concessional Loan be authorized to the Government of Peru (GOP) for \$10 million to assist in financing the new Urban Enterprise Fund (UEF) to be established in the Banco Industrial del Peru (BIP).

B. Borrower and Implementing Agency

The Borrower will be the Ministry of Economy, Finance and Commerce, representing the GOP. The implementing agency will be the BIP, which will administer the operations of the UEF.

C. Summary Rationale/Strategy

Creating an employment base in urban centers is one of the most urgent priorities and challenges facing Peru. In response to this challenge, the Mission believes that the promotion of Small-Scale Enterprises (SSEs) provides a rational, cost-effective approach to creating urban employment opportunities and improving the socio-economic condition of the urban poor. The Project builds upon the market-oriented policy framework being promoted by the GOP, particularly in regards to SSE development, as well as on the experiences of the Mission's previous activities with the BIP--the Rural Enterprises I and II Projects. The shift in geographic focus, from rural to urban, is a logical expansion of activities. The proposed Project, however, goes beyond the expansion of a successful experience. More importantly, it will address a number of policy-related issues described below. In this regard, it is consistent with the Mission's strategy of supporting projects and programs where the Mission can influence significant policy innovations. Specifically, the Project is designed to have an immediate impact on the demand for labor in the pueblos juvenes and to institutionalize, at the branch and central BIP levels, a sustainable program of credit and technical assistance for SSEs in these areas. It will also strengthen the financial viability of the BIP by helping it to become a self-sustaining financial institution capable of undertaking an SSE credit delivery system which will remain in place long after Project resources have been expended. To achieve this objective, the Project will assist the BIP in implementing a number of important policy initiatives, including: (1) a savings mobilization campaign, (2) provision of credit to SSEs based on realistic rates of interest, (3) an option to index loans, (4) liberalized lending procedures, and (5) provision of technical assistance to BIP personnel and SSE entrepreneurs to make more effective use of the credit made available under the loan.

D. Summary Project Description

1. Goal and Purpose

The goal of the Project is to generate employment and increase urban incomes in Peru; the Project purpose is to institutionalize,

through new policy and operational initiatives, a self-sustaining credit and technical assistance program for small urban enterprises.

2. Project Activities

The Project will consist of the establishment and operation over a four-year period of an Urban Enterprise Development Fund (UEF) with an initial capitalization of \$13.0 million available for sublending to eligible small-scale enterprises located in slum areas (pueblos juvenes) of Lima and four other Peruvian cities. The Project will also include up to \$500,000 for technical assistance and commodities for: (1) the staff administering UEF lending operations in BIP branch offices; (2) UEF sub-borrowers, both in preparing their credit applications and in subproject execution; and (3) the BIP in the technical and promotional aspects of mobilizing savings and inducing demand for credit at positive interest rates.

The Project will touch on two sensitive and difficult areas in which the Belaunde administration is presently forming policies: the long term, but increasingly visible, social problems inherent in fast-growing slums; and the destructive effect on credit programs caused by inflation greatly exceeding allowed interest rates. Specifically, the Project proposes to offer credit, averaging \$5,300 per loan, to some 2,800 individual small businessmen, creating jobs and new income in the pueblos juvenes; and to offer these credits on terms not now available to small entrepreneurs in Peru (over one year) and at a rate reflecting the real cost of funds. The intent is to support the Central Bank's new policy of real interest rates. The mechanics of doing so, as conceived by the Central Bank, will be to offer borrowers a choice: (1) a relatively high interest rate that is tied to the inflation rate, as calculated by the Central Bank, subject to adjustment every six months (currently this would approximate a rate of 50%); or (2) an indexed loan, under which repayments are graduated over the life of the loan, thereby requiring substantially lower payments in the initial year. (See the Project Description for a detailed explanation of indexation). In either case the value of the Fund will be maintained through a maintenance of value clause in the Project Agreement, a commitment required throughout the loan repayment period.^{1/}

E. Summary Financial Plan (\$000)

<u>Item</u>	<u>A.I.D</u>	<u>GOP</u>	<u>TOTAL</u>
Urban Enterprise Fund	9,500	3,500	13,000
Technical Assistance	390	-	390
Commodities	110	-	110
TOTAL	10,000	3,500	13,500

^{1/} The dollar will be used to adjust the fund level in future years.

F. Summary Findings

1. Project Findings

The Project Committee has reviewed all aspects of the proposed Urban Small Enterprises Development Project and finds that it is technically, financially, socially, and economically sound, and consistent with the development objectives of the GOP and those objectives set forth in the Mission's CDSS strategy. It has further found that the BIP is institutionally capable of administering the Project and disbursing the UEF funds within the time period discussed in the Project Paper.

2. Rural Enterprises I and II Evaluation

An impact evaluation of the Rural Enterprises I and II Projects has demonstrated the economic and financial feasibility of SEE lending in Peru. A summary evaluation report is presented in Annex II, Exhibit B. A sample of Rural Enterprises sub-borrowers demonstrated that average yearly sales increased by 28% since the FDR loan was made; average yearly increase in net income (in present value) was 54%.^{1/} Significantly, the evaluation found a good repayment record for sub-borrowers, with 90% of the loans repaid on schedule. Other significant accomplishments highlighted in the recent impact evaluation include a successful policy initiative to decentralize BIP operations and allow greater autonomy to branch offices. Over 80% of all loans made under the AID program did not require approval beyond the branch office level. This compares with approximately 20% at the time the project started. In addition, the BIP at the branch office level, undertook an aggressive promotion campaign which resulted in approximately 46% of all sub-loans being made outside the provincial capitals. Prior to initiation of the AID program, lending outside provincial capitals was rare. In several branch offices repayment records by small-scale enterprises under FDR were better than those of other BIP lending programs involving larger firms. The evaluation supports the Mission's findings that the BIP has the institutional capability to implement the proposed Project. Additional economic, financial, and institutional information is found in the evaluation report.

^{1/} Increases represent real gains in sales and income.

G. Project Development Committee

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PART II. BACKGROUND AND JUSTIFICATION

A. Urbanization and Unemployment in Peru

1. Background

Since the 1960's, Peru has been experiencing a period of rapid urbanization. Peru's urban population has grown from 40% of the total population in 1960 to 55% in 1972 and to 67% in 1980. Government of Peru (GOP) projections of future population growth, which are in line with estimates by international organizations, show total and urban population figures as follows: in 1990, 23.3 million (17.2 million urban); and in 2000, 29.8 million (23.4 million urban). Thus, Peru's urban population will nearly double between 1980 (12.0 million urban) and the year 2000 and account for approximately 78.5% of the country's total population.

While declining urban mortality rates and other factors have contributed to this rapid urbanization, rural to urban migration has been the main force in urban growth. As demonstrated during the 1961-1972 intercensal period, Peru's total population grew by an average rate of 2.9% annually; its urban population grew by an average annual rate of 5.6% whereas its rural population increased by only 0.7% each year.^{1/} During that time, Lima was the fastest growing city in Peru, growing 20% faster than the total urban population. However, this concentrated pattern of migration and urbanization has been changing. Although Lima will continue to be Peru's largest city, today medium-sized cities are growing at a faster rate and absorbing an increasing percentage of the migratory population.

Migration to Peru's cities is explained by a number of factors: greater and higher paid employment opportunities; greater accessibility to social services, including health and education; and access to electricity, potable water, and other public utilities.

In contrast, the rural sector offers fewer opportunities due to Peru's limited agricultural base and past government policies which subsidized urban centers and industrial growth at the expense of the rural sector. Food subsidies and ceilings on agricultural goods, subsidized utility rates, and cheap energy prices are examples of past administrations' urban-biased policies.

Evidence indicates that net economic and social returns to urban migrants have been positive. Nevertheless, the majority of urban poor experience real economic and social hardships. Since 1970, it is estimated that real urban incomes have declined by 36%. In the informal

^{1/} Intercensal data for the 1971-1982 period is now in the process of being compiled.

urban sector, which employs a substantial portion of the poor, real incomes have fallen by approximately 16% during the past two years.^{1/} This decline is the result of various factors, including: (1) the shortcomings of the redistributive policies implemented by the previous military government; (2) the 1976 economic recession, the worst Peru has experienced in the last four decades; (3) an inflation rate which reached 70% in 1981; (4) a decline in real output in the urban-based manufacturing, construction, and related trade and finance sectors, and (5) decreased availability of credit to the private sector which has hindered growth and employment generation.

The majority of the population in Lima and expanding secondary cities work in predominantly low-paying jobs which require minimal skills. A 1978 study done by the National Institute of Statistics (INE) found that one-third of Lima's labor force is concentrated in two occupational groups: retailers, composed mainly of street vendors, and service workers, composed mainly of domestic servants.

Urban subsidies and, to some extent, high rates of unemployment and underemployment are the result of past official economic policies which promoted highly protected, capital-intensive industrialization oriented to substitute imports. Since the 1940's, high import tariffs, non-quantitative trade barriers, over valuation of the Sol, and cheap and abundant credit for selected major industries have characterized Peru's approach to industrialization. The result has been the creation of a domestic industrial base that has absorbed a large percentage of the country's productive credit but is for the most part inefficient, capital-intensive and unable to compete in international markets.

Furthermore, these large, import-substituting enterprises have provided only limited employment opportunities for the growing urban labor market. Policies such as cheap credit and cheap foreign exchange have subsidized capital-intensive factors of production at the expense of labor. In 1980, the manufacturing sector accounted for 27% of Gross Domestic Product (GDP), but it employed only five to six percent of the urban labor force.^{2/} In sum, the formal industrial sector has been an insignificant source of employment opportunities for the urban poor.

^{1/} Ministry of Labor Statistics, 1981.

^{2/} This percentage translates into approximately 270,000 jobs. If one includes industries in the informal sector (defined as industries not registered with the Ministry of Industry and usually employing less than five people) the figure increases to between ten and eleven percent.

2. The Present Challenge

Given projections of continuing high rates of population growth, particularly in the urban areas, as well as estimates of the number of jobs required to employ this growing labor base, the Belaunde government is reversing many of the policies discussed above. The cornerstone of the current economic program is to open the industrial and other sectors to foreign competition, promote market-oriented growth in all areas of the economy and eliminate the sectoral price subsidies which were implemented at the expense of agriculture development and the rural sector. These policies have been discussed in the FY 1983 Congressional Presentation, the FY 1984 CDSS, and other USAID documents submitted to AID/W during the past year.

Despite the renewed attention being given to the agricultural sector, rural-urban migration will continue, thereby increasing demand for urban employment opportunities. 1980 figures indicate that approximately 11% of the urban population is unemployed and an additional 44% is considered underemployed. ^{1/} Peru's labor force is expected to grow by more than three percent per year throughout the remainder of the century, but increasing employment growth has been lagging at a rate of 2.7% yearly. According to a 1980 World Bank study, keeping up with the projected increase in the labor force will require the creation of approximately 195,000 jobs per year. Creation of this number of jobs would not, however, reduce the current levels of unemployment and underemployment. Further, at the prevailing capital-labor ratio, an annual investment of \$5.5 billion (in 1980 prices) would be necessary to absorb all new urban job seekers in the modern industrial sector. ^{2/} Such an investment is clearly unreasonable at this time or in the near future.

The present government faces the challenge of providing sustainable employment opportunities for the population through an economic growth strategy incorporating labor absorptive means of production. In view of the enormous existing and future supply of untrained urban labor in Peru, unemployment and underemployment will persist or worsen, unless the supply of investment capital can be spread more widely than in the past. Creating a sustainable employment base in urban centers is clearly one of the most urgent priorities and challenges facing Peru today.

^{1/} Underemployed is defined as earning less than the minimum legal wage, presently at \$78.00 per month or working less than 35 hours per week, although desiring to work more.

^{2/} Based on an average job creation cost in the formal sector of approximately \$36,500 per job (IBRD figure).

B. Response to the Problem: Small-Scale Enterprise(SSE) Development 1/

President Belaunde, in his first major address to the nation after taking office in 1980, cited the creation of jobs as one of the highest priorities of his administration. As part of the strategy to generate employment, the GOP is promoting the development of small-scale enterprises (SSEs). Based on the Success of SSE development efforts in Peru and in other countries the GOP believes that SEEs can play a more significant role in creating balanced economic and social development in Peru. 2/

To date, SSEs have participated vigorously in Peru's economic growth. During the 1977-1979 recession, industry as a whole was severely affected by the economic downturn, and value-added production in that sector dropped by eight percent. However, among SSEs within the informal industrial sector, value-added production grew by 100%. The total number of SSEs also grew substantially between 1975 and 1980, indicating that small-scale enterprises are adaptive to altering economic conditions and represent an important component of the urban economy and are a primary generator of employment opportunities. Approximately 67% of workers employed by "industry" are employed in the small-scale (up to 49 workers) manufacturing and artisan sector. The underlying dynamism of the informal sector and SSEs indicates that growth in this sector occurs without the assistance of the government or the financial sector. However, it also implies that, with reasonable support, SSE growth could be rapidly expanded.

The advantages of supporting SSEs are many:

1. Employment creation potential: Based on comparative data on investment cost per job created, SSEs tend to employ more direct labor per unit of invested capital than large enterprises. Studies also show that SEEs generate more indirect employment as well, due to the stimulation of complementary businesses.

2. Income distribution effect: SSEs generally sponsor activities having appreciably higher employment demands for unskilled workers. The unskilled are not only trained in the specifics of their task within the SSE but also due to the small scale of the SSE and its division of labor, often gain experience and skills in management and other business activities on the job.

1/ As defined in the 1976 Peruvian Law on Small Enterprises, SSEs include firms with annual sales equivalent to up to a total of 590 legal minimum wages (in mid-1981 approximately \$550,000). The BIP uses a broader definition including fifty or less employees and total assets less than US\$250,000.

2/ The GOP has already taken a number of steps to improve the policy climate for SSE growth. These are described in Section II.D. "Project Strategy".

3. Creation of complementary businesses: Related to the indirect employment effect, backward and forward linkages between SSEs and other sectors of the economy support the creation of complementary businesses by increasing the demands for or supply of their goods. One reason that small-scale businesses create these linkages more effectively than larger enterprises is that SSEs seldom require significant raw material imports as do larger enterprises, but more often rely on locally produced inputs.

4. High productivity of resources: SSEs with a lower level of investment per worker tend to achieve a higher productivity of capital than do larger, more capital-intensive enterprises. In addition, reliance on local materials has resulted in a resourcefulness and inventiveness on the part of the entrepreneur to utilize goods that otherwise would be wasted. As observed in the Rural Enterprises I and II Projects, entrepreneurs used old bicycles, used car engines, and other technological adaptations to meet their needs.

5. Supporting economic decentralization: Due to their generally limited infrastructure requirements, SSEs can be easily established in various locations, thereby facilitating the GOP objective to decentralize employment opportunities and economic activities.

6. Encouragement of private sector development: Fostering urban small-scale enterprises directly supports an AID priority--the development of a dynamic indigenous private sector. SSEs make use of entrepreneurial resources that may otherwise not be drawn into the development process. The involvement of people at the lowest income scale in the decision-making process will have an important impact on private sector development. Linkages to larger-scale private enterprises, such as sub-contracting arrangements, for example, could provide a means for established firms to play an important role in technical assistance, marketing, and other enterprise functions.

Other arguments for promoting SSEs include:

- they lend stability and coherence to communities;
- they generally have a minimal adverse environmental impact;
- They can be important generators of savings. ^{1/}

^{1/} Experience with small firms in Indonesia, for example, shows that firms' owners have a surprisingly high propensity to save and reinvest, even at quite low income levels.

USAID/Peru and the implementing agency, the Industrial Bank of Peru (BIP), have had significant experience in SSE development. ^{1/} Through two earlier A.I.D. projects the BIP successfully implemented a rural SSE Credit Program. The program successfully demonstrated that SEE development is an economically viable means to promote economic growth and employment in Peru. Approximately 30,000 jobs were created at a relatively low cost per job of \$7,000 compared to \$35,000 for Peru's formal industrial sector; ^{2/} taking into consideration indirect employment effects increases the number of jobs created and lowers further the cost per direct employment created. The BIP institutionalized a program of rural SSE lending within its participating branch offices and provided a diversified group of sub-borrowers with significant financial services previously not accessible. Creating jobs in a cost-effective fashion and changing the attitudes of the BIP toward lending to SSEs were the projects' most important accomplishments.

Besides responding to a large unmet demand for credit, ^{3/} expansion of the program to Peru's urban areas has several other justifications. First, the proposed Project expands the coverage of an innovative programmatic approach to a major development problem in Peru. Second, it encourages and assists Peru to change national policies and procedures which discriminate against the use of labor absorptive production techniques in favor of an excessive use of capital. Third, it addresses a major GOP and A.I.D. development priority to support and strengthen private sector initiatives. Fourth, this Project supports A.I.D.'s objective of replicating successful approaches to development and reducing project-related administrative problems. Fifth, this Project expands upon a number of significant policy initiatives that evolved partially as a result of the rural project. These initiatives are discussed under "SSE Project Strategy", Section II.D.

^{1/} See Annex II, Exhibit B for summary impact evaluation of Rural Enterprises I and II Projects. The complete evaluation is on file in LAC/DR.

^{2/} The \$7,000 figures derived from a sample included in the Projects' evaluation. Other BIP data indicate, however, that the cost per job could be significantly lower.

^{3/} USAID's BANCOOP Savings Mobilization Project demonstrated that significant demand exists for credit among small-scale enterprises, even with positive interest rates. Greater discussion of the project is provided in Section IVc.

C. Constraints to Development of Small-Scale Enterprises

The major constraints to the development of SSEs as proposed under this Project include: (1) insufficient credit caused by an overall scarcity of resources scarcity in the financial system, and restrictive lending policies and practices on the part of financial institutions; (2) lack of technical assistance; and, (3) socio-cultural barriers between the small-scale entrepreneur and formal financial institutions.

1. Insufficient Credit

a. Resource Availability

As a result of the financial crisis the country experienced in the late 1970's total credit availability within the Peruvian financial system has decreased dramatically in real terms. The decrease in the loan portfolios of principal financial institutions from 1975 to 1980 is indicative of the scarcity of credit resources in the system.

TABLE I
Loan Portfolio of Peruvian Financial
Institutions
1975-1980 (US\$ million)

	<u>12/31/1975</u>	<u>12/31/1980</u>	<u>% Variation</u>
<u>COFIDE</u> ^{1/}	340.2	417.9	+ 22.8
Development Banks	1,240.1	1,032.4	- 16.7
o/w Agricultural	384.4	365.5	- 4.9
Industrial (BIP)	395.7	320.6	- 19.0
Mining	66.7	74.7	+ 12.0
Housing	393.3	271.7	- 30.9
<u>Commercial Banks</u>	<u>1,314.7</u>	<u>1,173.3</u>	<u>- 10.8</u>
TOTAL	2,895.0	2,623.6	- 9.4
Conversion Rate (Sol/\$)	45	342.61	

Total Sol-denominated lending increased seven-fold from 1975 to 1980. However, due to high rates of domestic inflation, the actual amount of credit extended in dollar terms declined by 9.4%. Assuming an international inflation rate of ten percent p.a., this translates into a dramatic drop in lending in real terms of 50% over the five years.

^{1/} COFIDE's loan portfolio's expansion is explained by its very selective lending program which has been almost exclusively directed toward large-scale public enterprises.

b. Lending Policies and Practices

The limited resources available have, predictably, led most commercial institutions to lend primarily to their most-credit-worthy clients, principally well established enterprises engaged in mining, fishery, textiles, and export industries. High rates of inflation combined with artificially low interest rates also limited lending activities to short-term commercial transactions and working capital loans. Concerned about the stability of the banking system in an inflationary economy, the GOP closed the door altogether to medium-and long-term lending by commercial banks in the mid-1970's. Term lending was allowed only through financieras or finance companies.^{1/} However, interest rate policy still limited the viability of lending for much longer than one year.

In addition, commercial banks as well as financeras continue to require very conservative debt-equity ratios of 1.5(60/40) to 1.8 (65.35) and other conservative banking practices which preclude the majority of SEE entrepreneurs from applying to formal lending institutions for credit.

Lending to SSEs from formal sources has been limited, in general, to borrowers offering sufficient collateral and limited risks.

The BIP is currently the only institution in Peru that operates an active lending program for SSE. However, as described in the Institutional Analysis only recently did the BIP begin to concentrate on SSE lending despite its institutional mandate.

2. Technical Assistance

SSEs in Peru are characterized by a wide range of managerial and technical shortcomings apart from limited access to finance. These constraints include inadequate expertise in financial management and cost accounting procedures as well as limited knowledge of marketing, purchasing, and related areas of business management. Limited experience in these areas may thwart the entrepreneur's desire to establish or expand his operation. For example, the challenge of the following procedures and decisions may be particularly disheartening:

- finding outlets for products;
- negotiating with wholesalers from what is perceived as a weak position;
- determining the cost of each unit produced and fixing its selling price;
- keeping minimal accounting records;
- developing new lines of products (or new patterns and designs for the artisan);

^{1/} Many commercial banks created or became associated with financieras as a consequence.

- getting all the licenses and permits required to run a legitimate business;
- hiring and administering new workers, often from outside the immediate family.

At present, a large number of agencies, institutions, and public consultancies in Peru offer a wide range of technical assistance services that address these constraints. These include the Servicio Nacional de Adiestramiento en Trabajo Industrial (SENATI) Instituto de Investigacion Tecnologica Industrial y de Normas Tecnicas (ITINTEC); Banco Industrial del Peru (BIP); Universidad del Pacifico; and the Escuela Superior de Administracion de Negocios (ESAN). Efforts have been made, notably in Arequipa, Trujillo and Piura, to coordinate the activities of these institutions and thereby meet the technical assistance needs of SSEs in these regions more effectively.

Progress has been made toward the provision of technical assistance in recent years, but much remains to be done. A study, undertaken by the BIP in 1981 at AID's request,^{1/} revealed that out of 120 SSEs surveyed in Lima and other urban centers, 84 % had not received any type of technical assistance or training and 87% wanted it.

3. Socio-Cultural Constraints

The SSE entrepreneur's lack of familiarity with the formal banking system will often discourage him from seeking financial assistance from formal channels. Since the small entrepreneur, particularly in the pueblos jovenes, lives in an environment in which formal relations with banks are uncommon, he has a psychological barrier to approaching such institutions. Even when contact is made, applying and qualifying for bank credit can be a very discouraging experience. Dealing with government bureaucracies for the first time can also easily put off the potential borrower. The granting of a municipal license, for example, can take up to six or eight weeks. Additional requirements for establishing a legitimate business are: industrial registration, an electoral card, a tax collector certificate, proof of military service for men, plus numerous other documents required by the bank such as routine invoices and income statements. In addition to actually going through all the steps of obtaining financing and establishing a SSE, an additional threat to the entrepreneur's initiative is the underlying fear that all the information required both before and after loan disbursement will end up with the tax collector. This social intimidation is further accentuated by the attitude of the small entrepreneur who wants to minimize his risks. This attitude is primarily a function of the tenuous financial position of the small entrepreneur and is made evident by the fact that, on the average, ten percent of the credits approved by the BIP's Small Enterprise Division are not drawn down.

^{1/} See Annex II Exhibit J for Technical Assistance Survey.

D. SSE Project Strategy

SSE development programs in many countries show that if such enterprises are to flourish the right conditions must exist. While there are no simple solutions and much remains to be learned about how to create the "right conditions" for SSEs, several countries have employed a more market-oriented approach to fostering a favorable environment.^{1/} Essentially, this approach entails specific measures designed to: (1) reduce subsidies and policy preferences which favor large industry and discriminate against the small business; (2) enhance the availability and efficient use of inputs commonly needed by small firms; (3) increase the range of marketing opportunities. Fundamental to the market-oriented approach is the view that SSEs will thrive, if they are economically efficient, without a plethora of special subsidies and government intervention.

In Peru, the Belaunde government has already taken a number of steps to create the right conditions for SSE development. At the macroeconomic level, large, inefficient industries are no longer being indiscriminantly protected against foreign and domestic competition. Tariffs have been reduced, imports liberalized, and credit is going to the private sector that in the past went to public enterprises. Increased competition often results in better prices for production inputs. For example, domestic synthetic fibers, an input for many SSEs in the textile field, costs over four times world market prices. More importantly, the emphasis on increased private-sector oriented competition means that government resources--both financial and human--will be more evenly distributed.

Specifically, a new Industrial Law is presently under review which would assist SSEs in a number of ways. Registration procedures for small business will be simplified as will be their presently complex tax structure. Labor laws for SSEs will be revised and assure that they are not enimical to the government's goal of increasing employment.^{2/} Besides specific policies being formulated, the GOP has expressed a public commitment to small-scale enterprise growth, articulated by Prime Minister Ulloa in a major speech last year.

It is under this type of favorable policy framework that the proposed Project has been designed. Although the GOP is committed to enhancing the availability of inputs needed by the small firm, lack of medium- and long-term credit continue to be a constraint to SSE development. Through specific policy initiatives, the GOP has revitalized the financial sector and has made long-term credit feasible once again.

^{1/} See "Creating the Right Environment for Small Firms", by Keith Marden in Finance and Development, Vol. 18, December 1981.

^{2/} Under old laws, firing a worker was a difficult and costly undertaking. This policy intended to assure worker stability was actually detrimental to increasing employment. As a result many of the smaller SSEs would not register their employees with the government and as a result would not qualify for any type of government assistance.

However, the lack of experience in financial institutions in dealing with the type of entrepreneur who has limited capital, will continue to limit the access of credit of the smaller SSEs. This Project directly addresses this constraint by proposing to institutionalize a sustainable credit program to service SSEs in legally recognized pueblos jovenes. Furthermore, the Project will assist the GOP to implement recent financial sector policies and demonstrate that these market-oriented initiatives can be instrumental in helping the poor as well as creating a financially sound environment. Finally, sub-borrowers under this Project can be expected to graduate into the commercial banking sector in subsequent years.

Project components include: (1) provision of credit to SSEs based on positive rates of interest, liberalized lending procedures, and an option to index loans; (2) savings mobilization through passbook savings; and, (3) provision of technical assistance to BIP personnel and SSE entrepreneurs to provide for better utilization of the credit made available under this loan and to improve marketing operations.

Due to the successful role played by the BIP in implementing the two previous AID-financed projects, Rural Enterprises I and II, the BIP has been selected to carry out the activities planned under this Project. Whereas both the urban and rural projects have common objectives related to employment generation and credit availability, this Project builds upon and goes beyond the replication of successful experiences under the previous two projects; it includes as one of its major objectives assistance to the BIP in implementing sound financial policies to strengthen its long-term viability as a lending institution.

Under Rural Enterprises I and II, a number of important policy initiatives in the area of credit delivery were adopted (lower collateral requirements, lower debt-equity ratios, optional financial records). This Project expands and builds upon these initiatives in new policy areas. Specifically, this Project will address three important policy issues: (1) interest rate lending to sub-borrowers, (2) mobilization of savings, and (3) implementation of a system of loan indexation.

The innovative nature of the Rural Enterprise I and II projects limited to some extent the involvement of the BIP in these three areas. For example, the relatively low interest rates initially charged to sub-borrowers meant that the Rural Development Fund (RDF) was to be rapidly decapitalized without new injections from outside the BIP. However, this less-than-sound lending practice must be evaluated in the context of the primary project objective which was to convince the BIP to accept risk capital for a lending program which it initially viewed with considerable doubts. Although A.I.D. realized the limitations of subsidized lending practices, the Project's greater intent--demonstrating the viability of a SSE lending program--overrode these concerns.

The expansion of A.I.D.'s earlier efforts to urban branches of the BIP that did not participate in the previous projects will be important in strengthening the momentum toward SSE lending within the BIP. The Rural Enterprises Projects demonstrated that the institutionalization of an innovative credit program occurs from the "bottom up" as well as from the Central Lima office downward. Injection of FDR funds in rural areas generated a demand for SSE credit that branch offices could not simply "shut off" when funds ran out. Branch offices then exerted pressure on BIP management to continue the program. Since September 1981, the BIP has added approximately \$6.0 million dollars of their own funds to the FDR, indicating a commitment on the part of the BIP to maintain the momentum created under the two rural enterprise projects. Hence, a relatively small line of credit (less than \$20.0 million under Rural Enterprises I and II) has had a significant favorable impact on the BIP's long-term lending policy.

The proposed Project will assist the Belaunde administration's efforts to revitalize the Peruvian financial system by assuring that BIP lending rates to sub-borrowers are consistent with the policy of positive rates for both savings and lending activities. The BIP has agreed to set interest rates according to the forecasted inflation rate, and to adjust them semi-annually based on the inflation rate of the previous six months. The policy will result in positive interest rates which will prevent decapitalization of the UEF. ^{1/}

Project technical assistance will assist the BIP in implementing the Central Bank's loan indexation program at the SSE level. The new indexation plan, Sistema de Reajuste de Deudas, was unanimously approved by the Congress and is being aggressively promoted by a number of financeras (Annex II, Exhibit D presents examples of promotional literature on indexation). Indexation is recognized by the BIP and other development banks as a significant step toward developing the financial viability of medium-and long-term lending. At present, however, there is some uncertainty in the BIP as to how the new plan will work and how well it will be accepted by sub-borrowers. With A.I.D.'s assistance, the BIP will be one of the first institutions in Peru to demonstrate to public institutions, development banks and other financial institutions the feasibility of indexation as a means to provide long-term credit to low-income customers.

^{1/} Loan funded TA will be made available to the BIP to assist them in further examination of their interest rate policy.

Due to a past dependence on cheap Central Bank funds and international donor contributions, only a handful of Latin American development banks now mobilize domestic savings to expand their lending base. However, since concessionary support from these sources is less available, development banks are becoming increasingly interested in self-sustained operations and policies. In Peru, the BIP has taken the lead in this regard by mobilizing public savings with the introduction of one-year time deposits in July 1981. USAID's dialogue with BIP officials during the implementation of the Rural Enterprises projects was an important factor in moving toward this initiative. Under this Project, passbook savings will be offered in two new agencies to be opened in the vicinity of the pueblos juvenes of north and south Lima, and most likely, in the main offices in Lima and Callao. This innovation will permit the mobilization of savings from the target group. Based on the lessons learned under this Project, the BIP will expand this program to other branches throughout the country.

The Project is designed to have an immediate impact on the demand for labor in pueblos juvenes, and to institutionalize, at the branch and central BIP levels, a sustainable program of credit and technical assistance for SSEs in these areas. The Project will also have a positive demonstration effect in several policy-related areas, and will be important in promoting policy changes within the BIP, which will strengthen the long-term financial viability of the institution.

E. Relationship to USAID Program

1. Relationship to CDSS Strategy

The Project complements the Mission's urban development strategy as presented in FY 82 and FY 83 CDSSs. These documents discuss, among other things, the severe conditions of urban poverty and outline the Mission's response through the provision of food aid under the Title II program and basic social services and infrastructure through the provision of development assistance funds and the HG program.

During the last eighteen months, the GOP has undertaken an array of bold policy initiatives to implement their market-oriented approach to economic growth and development. These provide an ideal setting to carry out a development assistance program; particularly the newer themes in U.S. development assistance. The GOP has established a clear and paramount role for the private sector. It has decreased import duties, reduced subsidies and controls, and in general has been actively shaping a competitive framework which will allow entrepreneurs to move dynamically into their role as the major participants in the development process.

Nevertheless, much remains to be done. As highlighted in our FY 84 CDSS, the Mission's development assistance resources will be specifically targeted to projects and areas in which we can influence

significant policy changes and innovations. In some policy areas, USAID projects will guide the GOP on to what we consider the right policy track. In others, the USAID will assist the GOP in filling the gap between its policy initiatives and its ability to implement them. Under the proposed Project, AID will support GOP policy changes which seek to deliver needed credit to small-scale enterprises, and strengthen the financial base of a public institution through a market approach to meeting the needs of the poor. This latter objective will be achieved by mobilizing savings, implementing the indexation of loans, and establishing positive rates of interest for lending:

The Mission will also support development areas of priority GOP concern. The creation of productive employment opportunities has been cited by President Belaunde as one of the principal economic objectives of the GOP; in this regard, the institutionalization of a viable lending program to SSEs--and the immediate and potential employment effects that the program will generate--is in line with GOP and USAID objectives.

Agricultural development and sierra and high jungle economic development will continue to be an important focus on the Mission's development strategy. However, as a matter of policy and strategy, the Mission will support projects in all areas that have a significant impact on the poor, and which are consistent with broader Agency and Mission program objectives. The proposed Project will enable the USAID to direct further attention to a growing portion of Peru's poor--the residents of its sprawling pueblos juvenes.

2. Relationship to Other USAID Projects

As noted above, the Mission has successfully implemented, through two earlier loans, a rural small enterprise development program. Experience gained in these two projects has been instrumental in the design of the proposed Project and will be important in the implementation of Project activities. Other Mission projects have also provided useful guidance for design of this Project's components as well as benefit from this project's implementation activities. For example, lessons learned from the savings mobilization program with BANCOOP (527-0237) will be important in assisting the BIP to implement its own savings mobilization programs. The proposed Project will also draw upon the experiences of the Rural Agribusiness Rediscount Fund project (527-0159), implemented through the Central Bank of Peru. In turn, Mission projects for which medium- and long-term credit is an important component and/or the lack of such credit is a serious development constraint will benefit from lessons learned under this Project.

In recent years, the Mission has complemented its urban infrastructure and food aid programs with several OPGs which provide vocational training to the poor, particularly women. These include Fe y

Alegria Vocational Training (527-0234); Hipolito Unanue Family Planning (527-0245); and Obras de Bien Comun, Community Centers in the pueblos jovenes (527-0249). These identify and develop a base of potential entrepreneurs who could benefit from a program of expanded credit to SSEs as proposed under this Project. Lack of seed capital and working capital has in fact been cited as a major constraint by several of these groups who wish to organize small-scale enterprises.

F. Other Donors

Due to the supportive policy environment fostered by the GOP and the attractive attributes of SSEs in general, an interest in small- and medium-scale enterprise development has been revived among the international donor community. Other donors, notably the IDB and World Bank (IBRD) have been active in small- and medium-scale industrial lending programs to Peru. The Inter-American Foundation and the Governments of Holland and West Germany have also provided technical assistance to SSEs in recent years.

The Mission's rural enterprises projects resulted in a number of significant policy and operational initiatives subsequently supported by other donors such as the IDB. These include decentralization and increased autonomy to branch offices, greater outreach in lending operations both in geographic terms and with regard to clientele profile, increased technical assistance support to sub-borrowers, and a significant shift in the BIP's portfolio away from the predominance of large industrial clients to SSEs. These are discussed in greater detail in the evaluation report of the rural enterprise projects. The proposed Project, as discussed earlier, will continue to support important new policy initiatives such as indexation or other comparable positive interest rate systems. While this strategy is directly in line with current IBRD objectives, the IDB continues to favor subsidized interest rates in many of their projects. All donors, however, have indicated support for the Mission's savings mobilization initiative with the BIP, as well as the move to expand lending activities to the pueblos jovenes.

The Mission's rural SSE projects have complemented the efforts by the BID and IBRD by targeting sub-loans to considerably smaller-scale enterprises, and by lending to activities such as commerce, service, tourism, and agricultural enterprises which have not been included in the other donor's projects. Duplication of efforts has also been avoided by differences in several structural design features such as limited local cost financing under the IDB program, and the size of sub-loans, with the USAID program targeting sub-loans to considerably smaller-scale enterprises than the other donors. The UEF created under the Project will make maximum loans without prior AID approval of \$60,000 with an average loan size of approximately \$5,300. In comparison, maximum loan size under the IBRD SSE

project is \$180,000. The IDB has set a maximum limit of \$1.5 million.^{1/} These limits for sub-loans, including those under the USAID Project, refer to amounts for which donor approval is not required but are not strict lending limits for the credit institutions. Past experience shows that the loans from the international finance institutions tend to be greater than their upper limits, thereby requiring IDB or IBRD approval. Under the IBRD's Industrial Credit Loan, 15 out of 62 sub-projects exceeded the limit and accounted for 57% of total IBRD project funds. In contrast, no loans under the Rural Enterprises I and II projects approached the \$60,000 AID limit. Another indication of the larger scale of enterprises that these IBRD and IDB projects will support is related to borrower eligibility. For example, the IBRD SSE loan served firms with up to \$750,000 in annual sales and with fixed assets, excluding land, of up to \$300,000. Under the IDB small- and medium-scale enterprise project, the limit is set at \$5.0 million in sales and \$2.4 million in fixed assets. Furthermore, 90% of IDB funds will be used to finance foreign exchange costs. In contrast, AID project beneficiaries will normally not be in a position to import, nor will many of the SSE sub-projects require directly imported goods. Although the IDB is currently developing a loan to the BIP to finance small and medium-sized enterprises, the Project is a continuation of their ongoing program under which the majority of sub-loans exceed \$200,000 and rarely if ever fall below \$60,000. In addition, IDB assistance tends to be directed at the commercial mining and fishing sectors. The IDB also has a small grant program to ESAN under which this graduate business school provides assistance to artisans regarding export operations.

Another important distinction between the various donor SSE projects is the institutional arrangements through which they will be implemented and the implication of these arrangements. The most recent IBRD SSE loan will be made to The Central Bank but discounted through the Corporacion Financera de Desarrollo (COFIDE) which will rediscount project sub-loans retailed by financial intermediaries and commercial and regional banks participating in the program.^{2/} A major strategy objective in using this arrangement is to upgrade COFIDE's technical skills as a wholesaler of GOP and international donors' funds to financial intermediaries, and to actively upgrade its ability to lend to the SSE sector. The Bank's program will expand credit to SSEs through Peru's private and public sector institutions with the exception of the BIP. Given the risk-minimizing nature of commercial banks and financial intermediaries, it can be assumed that the more managerially "solid" larger SSEs will be the major beneficiaries of the IBRD program.

^{1/} A second Industrial Credit Project by the IBRD for public, private and mixed enterprises will have a limit of \$5.0 million.

^{2/} The Second Industrial Credit Project of the IBRD will also be implemented through COFIDE.

In contrast, the AID Project will finance the smaller SSE that does not qualify for credit through intermediaries and commercial banks due to collateral, debt/equity ratios, and other prerequisites required by these institutions. Significantly, this Project will not place the BIP in a position of competing with private sector financial institutions but rather, by providing risk capital, will solidify the role of the BIP as a development bank whose role is to nurture the creation of small-scale enterprises in an economically sound way so that they eventually become eligible for credit from the traditional and more numerous commercial lending institutions. As the profitability of SSE lending is demonstrated through this Project, and increased competition in the financial system increases, the need for financial institutions to aggressively seek new borrowers, these institutions will eventually "reach down" to the smaller enterprises. It is anticipated that the BIP will continue to play a leading role in the development of smaller SSEs.

PART III. DETAILED PROJECT DESCRIPTION

A. Introduction

The goal of this four-year Project is to generate employment and increase urban incomes in Peru. The purpose of the Project is to institutionalize, through new policy and operational initiatives, a self-sustaining credit and technical assistance program for small urban enterprises.

The BIP's Division of Finance will have direct responsibility for Project implementation and will coordinate the activities to be carried out by other participating divisions and branch offices within the BIP. These divisions include: (a) the Small Enterprise Division, which provides technical assistance, organizes training programs, and approves sub-project lending in the Lima area; (b) the Branch Management Division, which administers and oversees branch activities such as staffing and branch authorization levels on loans, and (c) the Credit Division, which evaluates specialized credits and credit policies. The regional branch offices will play the major role in program promotion, sub-project analysis, approval and monitoring, and provision of technical assistance. In light of the increased autonomy recently delegated to the branch offices, it is estimated that approximately 95% of all sub-loans under this Project will be approved at the branch level. A more complete institutional analysis of the BIP's operational structure can be found in Part IV, Section A.

The Project purpose will be achieved by strengthening the long-term financial viability of the BIP and supporting a continued shift in the BIP's principal lending focus from traditional large- and medium-scale industry, to SSEs, particularly the smallest within the latter target group. These objectives, in turn, will be attained through the following Project outputs ^{1/}: (1) establishment of an Urban Small Enterprises Development Fund within the BIP with indexation and fixed nominal interest rate alternatives; (2) a mobilization of savings program in the Project areas; (3) expansion of BIP coverage to pueblo joven areas presently not serviced by the BIP; and (4) a technical assistance plan for BIP field level staff and sub-borrowers.

This Project directly supports current GOP policy initiatives aimed at strengthening the entire network of financial institutions. The BIP through this Project, will become increasingly self-reliant and less dependent for its survival on contributions from the Central Bank and the international donor community.

^{1/} See Logical Framework, Annex I, Exhibit E.

B. Project Activities

1. The Urban Enterprise Fund (UEF)

A \$13.0 million UEF will be capitalized with an A.I.D. contribution of \$9.5 million and a GOP counterpart contribution of \$3.5 million. A.I.D. will provide an additional \$0.5 million in Project funds to finance technical assistance to sub-borrowers and BIP personnel, and some limited commodities for participating BIP offices. All sub-lending and technical assistance activities will be carried out by the BIP through its offices in the Lima area and its branches located in the four other target cities, Ica, Chimbote, Trujillo, and Chiclayo. (See map of Project areas, Annex II, Exhibit A.) Final selection of the cities to be included in the Project will be made by the BIP with approval of the Mission prior to initiation of lending activities.

a. Eligible Enterprises Classification

Existing or proposed enterprises eligible to receive financing from the UEF will belong to one of the following basic sectors of activity:

- cottage industries (including artisan)
- small-scale industry/manufacturing
- services/commerce
- small-scale agribusiness

These sectors, similar to those included in the Rural Enterprise projects, represent the majority of SSE activities in coastal cities. However, they are not exclusive. Other activities which merit consideration will be analyzed by USAID and the BIP on a case-by-case basis, as occurred under the rural projects.

b. Eligibility Criteria and Other Guidelines

In order to be considered for UEF financing, the sub-borrowers will be required to meet the following criteria, which will be checked by the branches as an integral part of the loan review process:

(i) financing: The enterprise is not eligible for alternative financing from commercial banks.

(ii) location: Enterprises must be located within legally recognized pueblos juvenes surrounding the cities previously selected. All sub-projects will be located within pueblos juvenes and all new jobs will be filled by pueblos juvenes residents. In addition not less than 80% of all sub-borrowers will be pueblos juvenes residents.

(iii) loan size: As under Rural Enterprises I and II, the maximum loan size without prior AID approval will be the equivalent of \$60,000. Loans of higher amounts could be approved after consultation with A.I.D., should the sub-project generate exceptional job-creation opportunities. Since this is the first effort of its kind in urban areas, the \$60,000 loan limit will be reassessed after the first year of Project implementation and may be adjusted depending on the findings of this review.

(iv) employment generation: Although a maximum loan/employment generation ratio will not be established under this Project, a general guideline of \$4,000 per job will be used, with appropriate consideration being given to sub-projects with slightly higher ratios but with other favorable attributes.

(v) economic benefits: Sub-projects will also be evaluated according to their overall economic impact, with particular emphasis given to those SSEs with a high value-added component.

c. Operating Procedures

(i) BIP interest rate structure: Presently, BIP's nominal interest rate structure for SSEs is: ^{1/} 38% for loans up to S/.3 million (\$5,555); 42 % for loans between S/.3 and S/.15 million (\$27,778); and 49.5% of loans above S/.15 million. ^{2/} Through interest rate discounting and other procedures, the effective rates of interest are greater than the stated nominal rates resulting in a BIP lending rate in excess of 50%. ^{3/} This rate is in line with the projected annual rate of inflation of 51% based on the previous six months experience. (August 1981-January 1982). It is also expected that the BIP's overall weighted interest rate structure will be increased within the next six months, although a decision has not been made with respect to the distribution of this increase on different levels of sub-loans. These rates are far from the highly subsidized rates of 18% and 22% under which the BIP operated during the past few years.

^{1/} Does not include commission.

^{2/} All sole figures here are converted at the exchange rate of \$1 = S/.540.

^{3/} The Bank's Board of directors has recently approved a proposal whereby interest is to be payable in advance on a quarterly basis thereby increasing the actual rate approximately 5% to the borrower and simplifying collection procedures.

The BIP will offer two alternative interest rate structures to sub-borrowers under the Project. The first will be a fixed rate. ^{1/} Currently, nominal rates in Peru are close to the forecasted inflation rate. As explained above, however, a number of procedures and charges will increase this rate several percentage points to an effective interest ^{2/} which will approximate the inflation rate, thereby assuring that decapitalization of the UEF does not take place.^{3/} Initially the effective rate will be based on the official inflation forecast for 1982, calculated by the Central Bank at approximately 50 percent. After Project implementation begins, the effective interest rate for new loans will be adjusted every six months, based on the inflation rate of the previous six month period. Using this procedure will allow the BIP staff to increase interest rates if necessary without confronting the administrative and political obstacles encountered in raising nominal rates. A.I.D. will require periodic reports from the BIP on its interest rate structures.

The second interest rate structure available to sub-borrowers under the Project will be based on the newly created indexation system. ^{4/} The Central Bank initiated this program in response to the limited availability of medium- and long-term credit in Peru in recent years. Most financial institutions, fearful of future inflation rates, had already stopped making long-term loans, when in the mid 70's the Government restricted all commercial bank loans to one-year terms because of concern about management of the banking system during periods of high inflation. The commercial banking system thus moved from medium - and long-term lending to overdrafts, discount operations, and payment guarantees.

1/ Although these rates are "fixed" it is common in Peru for interest rates to change through government decree as occurred in January 1981. At that time, borrowers who had taken out loans at low interest rate suddenly found themselves paying considerably higher rates.

2/ Effective interest rates refer to the rate actually paid by a borrower, whereas nominal rates refer to stated rates in a loan agreement.

3/ All charges and interest will be returned to the UEF with the exception of commission and fees.

4/ The "Sistema de Reajuste de Prestamo," as the indexation system is formally known in Peru, was recently unanimously passed by the Peruvian Congress. Annex II Exhibit E presents the official GOP decree on indexation. It is important to note that, under the indexation law, the program can only be offered as a lending alternative.

Financieras ^{1/} filled part of the gap by providing medium-term loans, but the high interest rates and repayment schedules reduced demand for such loans. In addition, financieras generally lend to a very select clientele able to meet rigorous guaranty requirements and make few loans of less than US\$100,000.

The decision to permit indexing is important to the future viability of Peruvian lending institutions. The indexation system could revitalize the moribund medium- and long-term financial markets in all sectors of the economy from agriculture to housing to industry. The system designed by the Central Reserve Bank and unique to Peru is an attractive lending alternative for Banks and borrowers, for the following reasons:

-- The amount of principal to be repaid by the borrower is adjusted yearly to offset the marginal cost of resources, i.e., the interest rates paid to mobilize funds through savings. Thus, the bank can limit the decapitalization caused by making long-term loans at fixed rates, which are financed with short-term deposits whose interest cost to the bank increases yearly with inflation. Indexation will reduce the capital erosion that the financial system has been experiencing by maintaining the value of the loan portfolio in real terms

-- The indexed system improves the borrower's cash flow by requiring lower payments during the first years than are required under the existing fixed-rate system. Higher payments will be made during the later years of the loan when the borrower should be in a better position to pay because his business is generating greater revenues. Another advantage for the borrower is that the lending institution will be willing to extend the loan over a longer period of time than under the fixed rate system, since the institution will receive substantially more principal in repayments as the principal amount is readjusted. Longer repayment periods will help to minimize the cash flow problems that higher payments in later years might otherwise cause.

An indexed loan consists of two parts: (1) the nominal fixed rate of interest (17%) applied to the principal, and (2) the adjustment factor (currently 40%) which is determined by the Central Reserve Bank based on a formula which as described above, incorporates the interest rates which must be paid to attract savings. i.e., the cost of mobilizing resources.

The composition of Peru's index factor was established after the Central Bank had examined indexation systems used in other countries. An inflation-based factor was ruled out because it was feared that such a system would "institutionalize" inflation by increasing credit costs automatically as the price index increased, thereby

^{1/} Financieras, or finance corporations, act in many cases as the medium-term lending arms of local banks, with which they are closely associated. They are subject to fewer restrictions on reserve and another requirements and interest rates than banks.

contributing to even higher increases in prices. The Central Reserve Bank believes that the system chosen, which is unique to Peru, is more equitable since the index changes only when the bank's cost of capturing savings increases. In addition, the Central Bank has expressed a commitment to keep the index from exceeding increases in national wages and salaries, through the incorporation of salary and wage factors in the formula, although this is not explicitly included in the law.

The nominal fixed interest rate is 17%, substantially higher than the 6% usually used as the cost of borrowing funds in a zero inflation economy. This rate was chosen to improve the cash flow of financial institutions by generating additional resources to help offset expected out-flows of interest earnings on savings. This cushion is particularly important under this indexed system since the financial institution receives lower repayments during the initial years than under the fixed rate system. Tables 2 and 3 illustrate cash flows for a conventional and for an indexed loan with and without grace period.

TABLE 2Comparison of Cash Outlays under Indexation and Fixed Rates Options

Loan amount under both systems: 1,000 units
 Terms: 6 years
 Interest rate: Fixed nominal rate: 57%
 Indexation: 40 index + 17% interest rate

Cash Outlays with indexation

<u>End of Year</u>	<u>Interest 1/</u>	<u>Principal Paid</u>	<u>Additional 2/ Principal</u>	<u>Total Payments</u>	<u>Year End Principal Balance</u>
1	170	200	400	370	1,000(loan)
2	204	300	480	504	1,200
3	235	450	552	685	1,380
4	252	675	593	927	1,482
5	238	1,013	560	1,251	947
6	161	1,326	379	1,487	---

TOTAL PAYMENTS: 5,224 units

Value of Payments: 1,152 ^{3/}
 =====

Cash Outlay under conventional system

<u>End of Year</u>	<u>Interest</u>	<u>Principal Paid</u>	<u>Additional Principal</u>	<u>Total Payments</u>	<u>Year End Principal Balance</u>
1	570	40	---	610	960
2	547	63	---	610	897
3	511	99	---	610	798
4	455	155	---	610	643
5	367	243	---	610	400
6	228	400	---	628	---

TOTAL PAYMENTS: 3,050 units

Value of Payments: 1,113 ^{3/}
 =====

1/ 17% of Year-End Principal Balance.

2/ Additional principal is based on 40 % (the index factor) of the previous year's principal balance. For the purposes of this example, the index factor is fixed at 40% throughout the life of the loan. Realistically, it could vary over the life of the loan.

3/ Discounted valued of units at the beginning of first year with 50 percent of inflation rate/year.

TABLE 3Comparison of Outlays under Indexation and Fixed Rates Options

Loan amount under both systems: 1,000 units
 Terms: 6 years
 Interest rate: Fixed nominal rate 57%
 Indexation 40 index + 17% interest rate

Outlays with indexation and two-year grace period for principal

<u>End of Year</u>	<u>Interest</u> ^{1/}	<u>Principal paid</u>	<u>Additional Principal</u> ^{2/}	<u>Total Payments</u>	<u>Year End Principal Balance</u> 1,000 (loan)
1	170	0	400	170	1,400
2	238	0	560	238	1,960
3	333	600	784	933	2,144
4	364	900	858	1,264	2,102
5	357	1,350	841	1,707	1,593
6	271	2,230	637	<u>2,501</u>	---

TOTAL PAYMENTS: 6,879 units

Value of Payments: 1,191 ^{3/}

Outlays under conventional system and two-year grace period for principal

<u>End of Year</u>	<u>Interest</u>	<u>Principal paid</u>	<u>Additional Principal</u>	<u>Total Payments</u>	<u>Year End Principal Balance</u>
1	570	0	---	570	1,000
2	570	0	---	570	1,000
3	570	112	---	682	888
4	506	176	---	682	712
5	406	276	---	682	436
6	248	436	---	<u>684</u>	---

TOTAL PAYMENTS: 3,870 units

Value of Payments: 1,120 ^{3/}
 =====

Note: Footnotes of Table 2 apply to this table as well.

As shown in the previous tables, the borrower under the indexation alternative must repay more over the life of the loan. However, discounting these amounts result in an insignificant difference in real payments under the two systems. Under the undexed system, the borrower has much lower repayments during the first two years, when his revenues are lowest and his ability to make loan repayments weakest. This liquidity schedule, tailored to the borrower's advantage, is one of the most favorable aspects of the system and, logically, one of the aspects being highlighted by banks and financieras promoting the indexation alternative. The lender, in return, recovers the value of the loan through higher payments in later years. ^{1/}

The indexation alternative is particularly important to promote medium- and long-term credit in an inflationary economy in which positive interest rates are charged. Because cash flow problems result from having to pay back an amount equivalent to over one half of any amount borrowed in a year (61% in the example above), borrowers are unable to financially manage such a loan when any delay in producing large profits is anticipated.

Both the BIP and USAID agree that the adoption of indexation on medium- and long-term loans under the Project is desirable, and the BIP will aggressively promote the system as a lending option. Since the borrower's option is between a positive rate with high repayment schedules in the first two years, and indexed loans, indexation should be viewed as an attractive alternative by most SSE borrowers.

Technical assistance to train BIP central and branch staff in the mechanism of the indexed system as well as an intensive promotional and educational campaign directed at sub-borrowers will be financed under the Project to help assist in the implementation of this innovative program. There are, of course, a number of unknowns regarding the indexation program. Indexation, although a financially sound concept, is new in Peru; because the particular plan proposed by the Central Reserve Bank is unique, one cannot predict with certainty how well it will work. The GOP believes, and the Mission agrees, that with adequate promotion and education campaigns it will be widely accepted as a preferably system to high fixed rates.

In countries where indexation has been implemented, the program has occasionally met opposition from those groups that have traditionally benefitted from subsidized credit program (often not the poor). Success of the program will ultimately depend on how committed the GOP is to revitalizing medium- and long-term lending and the financial system in general. Based on experience to date, we believe this commitment is firm and will support it through this Project.

^{1/} The discounted value of those repayments is, of course, much lower in the first example, with an inflation rate of 50% per year, the 1,487 unit payment at the end of the sixth year is worth only 131 units (value at the beginning of the loan period). Even in discounted units, however, the lender faces slightly better under the indexed system.

The BIP is committed to maintaining the value of its lending capital through the lending policies discussed above. The bank will finance the administrative costs of lending to SSEs, particularly the smallest, can be financed with the revenues generated by its lending operations to medium- and large-scale industry. The BIP considers some form of interest rate incentive -- even if minimal -- important to the BIP and GOP strategy of fomenting SSEs and promoting indexation. In addition, other variables, including higher Central Bank lending charges to the BIP and a maintenance-of-value clause for Project funds, will ensure that the BIP be held accountable for any lending incentives given to SSEs.

(ii) sub-loan terms: Maximum terms available will be ten years. As in other BIP lending programs, however, sub-loans will generally not exceed six years under the fixed rate alternative, but can be expected to be longer when indexation is selected as the repayment methods. Because of its interest in promoting indexation, the BIP will offer longer repayment periods to sub-borrowers than are available under the fixed-rate system. Grace periods for repayment of principal of two years will be authorized. Medium-term lending, in particular for the purchase of machinery and equipment, will constitute the bulk of the UEF lending program. Working capital loans, exclusive of capital purchases, may be made available for industrial sub-projects only in exceptional circumstances. For example, businesses requiring working capital to expand the production of previously purchased idle machinery would qualify for a loan. Determination of the necessary level of working capital will be part of each sub-project's appraisal. In such cases, terms will not exceed one year compared to the usual three years under current BIP policies.

(iii) collateral: Loans for the purchase of equipment and machinery will be covered by liens on the equipment or machinery. The actual filing of these liens is fairly simple and is performed by the sub-borrower prior to disbursement. In other cases, deeds on real estate or other property may be required from the sub-borrower. Alternatively, UEF sub-loans may be covered by guarantees from the Fondo de Garantia para Prestamos a la Pequena Industria (FOGAPI) a public fund set up in 1978 as a cooperative venture between the Government of West Germany, COFIDE, and the BIP and two national small enterprise associations. These loan guarantees have replaced those previously extended by the Banco de la Nacion and carry a commission of 2% per year. As for artisan projects, the new Artisan Law to be issued shortly will include an Artisan Guarantee Fund (Fondo de Garantia Artesanal) which could also be used to guarantee loans made under this Project. In addition, cosigners may guarantee sub-loans.

UEF loans will be made available for up to 90% of collateral compared to 60% to 70% under usual BIP guidelines, thereby requiring a 10% minimum contribution from the entrepreneur. This liberal collateral policy is considered essential since the amount of capital available to this Project's target population for collateral has been extremely limited.

(iv) leverage: The debt-to-equity ratio of 60/40 (leverage of 1.5), considered acceptable by the Peruvian banking system and rarely relaxed, has proven prohibitive in making credit accessible to the majority of SSEs. Based on the successful experiences under the rural enterprise projects, the BIP will not apply a rigid debt/equity ratio to loans made from the UEF, and will allow the ratio to reach 90/10 in cases where the sub-project appears feasible but the sub-borrower is not in a position to contribute a large initial share of the capital.

(v) loan application: The application is filled out by the applicant and the BIP loan officer. The application is designed as a technical assistance tool to assist the borrower in presenting a financially feasible sub-project. Separate application forms are presently used by the BIP for SSEs and for artisans. These forms (five and three pages in length, respectively) have proven fairly cumbersome due to the lack of typing services at branch levels. The BIP's Small Enterprise Division is presently testing a new form, to be used under this Project, which will be filled out by hand.

(vi) loan review, approval and processing: BIP personnel, who have considerable technical expertise and experience with small enterprise lending, will analyze all sub-projects thoroughly to ensure their financial and technical soundness as well as each applicant's credit-worthiness. BIP personnel will assist applicants in meeting legal requirements such as helping to obtain municipal permits, etc. In addition, all proposed sub-loans will be reviewed to ascertain whether all appropriate eligibility criteria, as previously outlined, are met. In 1981, the BIP instituted a new decentralized system for sub-loan approval which operates as follows:

-- Loans up to a certain level can be approved by the branch administrator. This level is determined on a branch-by-branch basis by the BIP's central branch level Management Division according to each branch administrator's technical expertise and experience.

-- Loans larger than this level are reviewed by the branch's Internal Credit Committee consisting of the branch administrator, the credit officer, the legal officer, and the operations manager.

-- Still larger credit requests go to the decentralized credit committee, still at branch level, consisting of the Internal Credit Committee plus two local non-BIP employees (economists, professors, President of the Local Chamber of Commerce, etc.).

-- A fourth level loan approval requires a review by the Regional Chief who visits each branch twice every three months and can be contacted by telex for approval.

-- Beyond this level, the sub-loan goes before the manager of the Branch Management Division, and the Board of Directors, all at the central level. Recourse to these last three levels is quite unlikely for approval of loans financed by the UEF under this Project.

The loan approval levels at the various branches participating in this Project are as follows: 1/

TABLE 4

Sub-loan Approval Levels
(as of December 1981)
(\$ equivalent)

	<u>Chiclayo</u>	<u>Trujillo</u>	<u>Chimbote</u>	<u>Ica</u>
1. Branch Administrator	\$4,000	\$6,000	\$6,000	\$2,000
2. Internal Credit Committee	20,000	20,000	16,000	6,000
3. Decentralized Credit Committee	30,000	30,000	24,000	10,000
4. Regional Chief			-----\$40,000-----	
5. Manager of Branch Management Division			-----\$55,000-----	
6. Credit Division			-----216,000-----	
7. Board of Directors			-----Above 216,000-----	

It is estimated that 95% of the UEF loans will be approved locally (levels 1, 2 and 3).

(vii) supervision: Loan officers will maintain regular contact with sub-borrowers in order to manage the loan portfolio, identify problems as they arise, follow up on delinquent accounts, and handle technical assistance referrals on a timely basis. Maintaining such contact should prove relatively easy under this Project as the BIP branches are situated in close vicinity of the pueblos juvenes. Each branch office will be responsible for supervision activities within its regions. 2/ Such activities vary from sub-borrower to sub-borrower and tend to be more intensive during the early stages of sub-loan implementation. After a given

- 1/ The BIP's Small Enterprise Division in Lima will be responsible for approving all sub-loans in the Lima area until the two new branches in the north and the south cones of the city are established and staffed, and branch approval authority levels are determined.
- 2/ In Lima, the Small Enterprise Division at the Central Office will initially supervise sub-loans directly.

enterprise has been successfully operating for a year, it normally requires little ongoing supervision. At the BIP central office, the UEF coordinator, who will report directly to the manager of the finance Division, will handle overall Project supervision and prepare regular status reports for USAID. USAID will, in turn, perform random portfolio audits concerning, among other things, the enforcement of the eligibility criteria, how indexation is being promoted by the BIP, and difficulties encountered by sub-borrowers in presenting loan applications to the BIP.

(viii) credit manual: The operational procedures governing use of the UEF funds, will be outlined in a credit manual to be distributed to all BIP personnel involved in Project implementation. Development of this manual will be a condition precedent to disbursement of Project funds.

2. Savings Mobilization

In an environment of increasing competition for dwindling contributions from the Central Bank and external donors, in July 1981 the BIP initiated, a savings mobilization campaign to generate resources. To date, the BIP has limited this campaign to the promotion of time deposits of one year or more. Since convenience is a determining factor in a saver's selection of a place to deposit small amounts of money accessible to withdraw as needed, and since the BIP does not have branch offices scattered throughout Lima and other cities, it seemed reasonable to promote only long-term deposits (one year and longer). The BIP offers the highest rates permitted by law of 55% per year, and has attracted sizeable death benefits and pension fund monies from other government institutions as well as from individual depositors. ^{1/}

During the first year of Project implementation, the BIP will open two new branches in the northern and southern sections of Lima, located close to pueblos juvenes. The offices will be staffed by a core of existing BIP professional branch personnel. Vehicle support and other resources necessary to undertake savings mobilization campaigns and loan supervision will also be provided. Passbook savings will be offered in these offices for the first time on a pilot basis and will probably also be offered in the main office in Lima and in the Callao branch office as well. The new offices will also serve as contact points for pueblo joven residents in the Lima area who are interested in obtaining loans for SSE projects.

^{1/} For the BIP, all savings mobilized are important to expanding its lending resources. However, pension funds and other types of large deposits generally do not represent "new" savings to the entire system since they most likely represent deposits transferred from other institutions. Savings mobilized from low-income individual depositors, however, are likely to be "untapped" savings, particularly in pueblos juvenes areas.

Both the establishment of two new offices and the introduction of passbook savings will facilitate mobilization of new savings from the target group and strengthen the financial capacity of the BIP as a lending institution. It is expected that once the savings mobilization program is expanded, nationwide existing BIP branches in other cities will be able to easily promote passbook savings within their communities due to the proximity of these branches to the pueblos jovenes areas. The BIP has also expressed its willingness to experiment with more innovative promotional efforts to the extent permitted by Peruvian law. For example, if the current law is changed to permit the offer of direct premiums and incentives other than interest, the BIP is willing to do so. ^{1/} At any rate, savings mobilization campaigns will be carried out through promoters and advertising through flyers and posters in the pueblos jovenes. Technical assistance will be offered under this Project to assist in the design of the savings campaign.

3. Technical Assistance Program

Technical assistance (TA) is crucial to Project implementation since the Project will be carried out in urban branches of the BIP which have relatively little experience in lending to smaller SSEs, and will be directed at small entrepreneurs with limited administrative skills. Project supported technical assistance will be provided to: (1) upgrade the BIP's capacity to carry out lending programs to SSEs; (2) institutionalize a system of technical assistance (including administrative, financial, and production-oriented assistance) to the sub-borrower; (3) effectively and aggressively implement policy initiatives such as the indexation program; and (4) mobilize savings.

a. Institutional Level

BIP operational staff at the branch level will receive training in lending to SSEs and in carrying out innovative lending policies being promoted by the GOP and supported under this Project. The

^{1/} The very successful A.I.D. savings mobilization program with BANCOOP used a number of incentives which are not presently allowed for the BIP since BANCOOP, as a cooperative institution, was not under the jurisdiction of the national Banking Law. With changes in the Banking Law, however, the experiences and lessons learned from the BANCOOP program could be implemented through the BIP. Changes to the Banking Law are presently under consideration.

training will complement and go beyond efforts begun through the provision of TA under the Rural Enterprises II Project. (Annex II, Exhibit F, details the BIP's use of technical assistance funds from the earlier projects.) Courses, some to be presented by BIP staff, will be held for target area branch managers, loan officers, lawyers, and other technical personnel. Fifty individuals at a cost of \$400 per participant will be trained. Based on the effectiveness of third-country training under the earlier project, A.I.D. will continue to co-finance with the Association of Latin American Development Banks (ALIDE) the costs of sending BIP staff for short-term training in Spain, Mexico and other countries with successful SSE programs. Approximately ten trips costing \$2,500 per trip are planned. Technical assistance activities for personnel will be coordinated with and complemented by the Bank's Personnel Training Office, and its capacity to provide assistance to BIP branch staff on a continuing basis will be strengthened.

Short-term TA (approximately one month) will be provided by AID at a cost of approximately \$10,000 to assist the BIP in initiating a savings mobilization campaign based on passbook savings. Six weeks of short-term TA at a cost of approximately \$15,000 will also be provided to assist the BIP in carrying out the technical assistance program at the branch level. Finally \$5,000 will be provided to procure local TA designed to assist the BIP with its indexation program. This TA will be complemented by Central Bank experts to be provided to the BIP on a short-term basis to assist them in the implementation of the indexation system

b. Enterprise Level

To carry out technical assistance programs at the enterprise level (beyond TA for loan processing), the BIP has successfully used its own internal capabilities and the relatively large number of agencies, institutions, and public consultancies in Peru which offer a wide range of services to SSEs. These include:

(i) The GOP's National Industrial Training service which runs vocational and management training and advisory programs with assistance from the German and Dutch Governments;

(ii) the GOP's National Industrial Technological Research and Standards Institute which provides technical information to SSEs, mostly on production and quality control problems;

(iii) the Pacific University which is setting up a management training institute, which is planning to set up a training program and advisory services for SSE owners/managers.

(iv) the Superior School of Business Administration, a management training institute, which is planning to set up a training program and advisory services for SSE owners/managers.

In the past, courses for sub-borrowers in administrative and vocational areas have been organized by the BIP using these sources. In many branch offices, these external resources and the BIP's internal capacity are used quite effectively. However, as discussed in the recent rural enterprises evaluation, the quality of technical assistance, content, and delivery capability appears to vary considerably. In part, this is due to differences in the technical capability of staff at the branch level, the lack of clear information on technical assistance needs of sub-borrowers, unfamiliarity with external resources in some branches, and the lack of a comprehensive approach to technical assistance for SSEs within the BIP. The Project will address these issues by providing resources to analyze these needs and to design a technically viable and cost-effective program of comprehensive technical assistance to the sub-borrower.

As a condition precedent to initial disbursement of loan funds, the BIP will present to USAID an operational plan for the use of TA funds. This plan will include a thorough analysis of the BIP's current assistance programs to sub-borrowers, identification of sub-borrower technical assistance needs, and a breakdown of proposed course content in areas, such as vocational training, administrative management, and financial assistance for sub-borrowers. As mentioned earlier, technical assistance funds will be provided to contract short-term assistance to help the BIP implement this activity.

Assistance will be provided to the sub-borrowers individually or in groups by BIP staff as well as by the numerous external resources cited earlier. As part of the loan approval process, loan officers will identify borrowers who require training in specific areas. If technical assistance is crucial to sub-project success, training will be made a prerequisite to loan approval. In those cases, part of the cost of this training will be added to the sub-borrower loan amount. By having the sub-borrower pay for at least part of their training costs, it is expected that scarce training resources will be better allocated (people will only attend training when they really feel the need) and the financial capacity of the BIP to provide this service will be improved.

The exact make-up of courses and assistance to sub-borrowers, will be determined by the operational plan that will be presented by the BIP. However, it is expected that the bulk of the TA for the sub-borrowers will be provided through short-term courses of approximately ten days on technical, administrative, and financial aspects of enterprise management. During the four-year Project implementation period, approximately 12 courses will be held in each of the participating cities for a total of 60 courses. Courses will cost an average of \$100 per participant or a total of \$210,000. ^{1/} They will be administered for the most part through contracts with outside services, such as the Servicio Nacional de Adiestramiento en Trabajo Industrial (SENATI), and will be

^{1/} Estimating approximately 35 people/course, some 2,100 people will participate in courses.

complemented by the BIP Training Division activities. The remaining US\$80,000 for sub-borrower TA will be used for individual skill upgrading in areas such as the use and maintenance of machinery, marketing techniques, etc. Discussions with BIP staff and the rural Enterprise evaluation team indicated that approximately 40% of the estimated sub-borrowers under the Project (1,000 people) may need complementary individual TA at a cost of US\$80 per sub-borrower. This technical assistance activity will be completed by supplier-provided assistance and maintenance, common in sales agreements for machinery

As in the previous projects, an important component of technical assistance at the enterprise level will be that provided during the loan approval stage. As part of the approval process, the branch loan office will prepare, in conjunction with the sub-borrower, a sub-project feasibility study including a review of the financial, economic, and marketing aspects of the sub-project. Along with the more routine functions of the loan process (definition and establishment of collateral, provision of information on administrative steps required), sub-project specific technical assistance will serve to orient the sub-borrower in the earliest phase of his new business undertaking.

C Project Inputs

A.I.D.'s \$10.0 million loan will contribute toward capitalization of the UEF as well as finance commodities, local and international training for BIP personnel and sub-borrowers, evaluation cost, and short term technical assistance to the BIP. The GOP will provide \$3.5 million in counterpart toward the capitalization of the Fund.

The following inputs will be provided:

Commodities

- 6 vehicles	\$90,000
- spare parts	10,000
- office equipment for two branches in the <u>pueblos jovenes</u> of Lima	10,000
Sub-total	<u>110,000</u>

Training

- Local training seminars for UEF branch office administrators and loan officers	20,000
- Short-term international training for branch staff	25,000

-Training courses to sub-borrowers, approximately 60 courses with 35 people each at a cost of \$100 per participant	210,000
-Industrial training to 1,000 sub- borrowers at a cost of \$80 per sub- borrower	80,000
Sub-Total	<u>335,000</u>
<u>Evaluations</u>	
- Two major Project evaluations <u>Short-term Local and International Technical Assistance</u>	25,000
- Assistance with implementing technical assistance program	15,000
-Assistance with savings mobilization campaign	10,000
-Assistance with indexation program (local)	<u>5,000</u>
Sub-Total	<u>30,000</u>
TOTAL	<u>\$500,000</u> =====

TABLE 5
Summary Input Costs
(US\$000)

<u>Item</u>	<u>A.I.D.</u>	<u>GOP</u>	<u>TOTAL</u>
Urban Credit Fund	9,500	3,500	13,000
Technical Assistance and Training	390	---	390
- Training for BIP Staff	(45)		
- Training for sub-borrowers	(290)		
- Evaluations	(25)		
- Short-term T.A.	(30)		
Commodities	110	---	110
TOTAL	<u>10,000(74%)</u>	<u>3,500(26%)</u>	<u>13,500 (100%)</u>

PART IV PROJECT ANALYSIS

A. Institutional Analysis

1. Peruvian Financial System Overview ^{1/}

a. The Peruvian financial system is dominated by the banking system which has historically held approximately 88% of the country's total financial assets. The banking system comprises the Central Bank; Banco de la Nacion; five specialized development banks, including the BIP; and 21 commercial banks, including eleven non-specialized commercial banks, six regional commercial banks, three construction banks, and one savings bank. The non-banking financial institutions include the GOP's development finance institution (COFIDE), finance companies or financieras, 16 savings and loan associations, 22 insurance companies, and over 500 small savings cooperatives and credit unions. During the early 1970's, the GOP took several steps to tighten its control over Peru's financial system. These measures included the establishment of a Council for Monetary Policy, the creation of COFIDE, the expansion of public sector development banks, the nationalization of three commercial banks, and the channeling of commercial bank credit in support of government priorities. In 1978, due to worsening economic conditions and severe credit shortages in the system, tight public sector control began to give way. This reversal process has been accelerated under the Belaunde administration by returning the responsibility for monetary policy to the Central Bank and by freeing commercial banks from compliance with GOP guidelines on credit allocation. Furthermore, a new banking law, the first since 1933, is presently under discussion and, if adopted, will further open up financial markets by removing legislation restricting the licensing of new banks and by encouraging foreign banks to enter local markets. Although these policy changes will have a liberalizing effect on Peru's financial system, the GOP will continue to influence financial policies and regulations through the Central Bank and public sector financial institutions which presently hold approximately 80% of the system's total financial assets.

b. Due to the economic crisis of the past years and the limiting legal and institutional environmental of the 1970's in which commercial banks were operating, the volume of commercial bank lending has decreased in real terms since 1975. For example, until recently, commercial banks were limited to lending at a maximum term of one year. To overcome this policy constraint, many banks created finance companies or financieras to extend medium-term loans. The banks, in turn, have concentrated in short-term lending of which approximately 50% of their credits are extended to the industrial sector, mostly for large loans. With passage of the new banking law, commercial banks could find themselves exposed to increased competition from domestic as well as foreign banks. Lower reserve requirements, also proposed under the law, should also increase competition, resulting in a more aggressive lending program.

^{1/} See also Section II C.2

To finance selected economic development activities, the GOP created four sector specific development banks in industry, agriculture, mining, and housing. To date, these development banks have almost exclusively relied on resource transfers from the Central Bank and foreign donors to capitalize their lending programs. Under the current situation of decreasing concessionary resources, certain of some of these banks are beginning to implement self-capitalizing operations such as positive interest rate lending and savings mobilization campaigns. This Project's implementing institution, the Banco Industrial del Peru (BIP), has taken the lead in this regard.

The GOP also established COFIDE with a broad mandate of financing economic activities across sectors. In 1980, 50% of the loans outstanding and 56% of the guaranties issued by COFIDE were to state enterprises. As part of the current reorganization of public financial institutions and policy shifts under the present administration, however, COFIDE will divest itself of its investments in nationalized companies, and will expand its lending to the private sector. COFIDE is becoming the major wholesaler of Government funds to the productive sector as well as the major recipient of loans negotiated by the GOP with international institutions. As a result, COFIDE is beginning to channel substantial foreign resources to other financial institutions such as commercial banks.

2. The Banco Industrial del Peru (BIP)

a. Rationale for BIP Selection

The BIP was established in 1933 as a public sector lending institution with administrative and operational autonomy, financed primarily by loans and lines of credit from international institutions and foreign governments as well as capital transfers from the Central Reserve Bank. According to its statutes, the fundamental purpose of the BIP is to promote and finance industrial development. Specifically, the BIP is charged with the organization of small industry by individual entrepreneurs, cooperatives, and other associative firms. It is the major source of medium- and long-term credit for the Peruvian private sector, and has a network of 28 branches and agencies throughout the country.

In spite of its special mandate to foster small enterprise development, the majority of BIP loans have traditionally gone to large- and medium-scale industry. In recent years, however, the BIP has begun to offer more credit to small enterprises, and has set up a Small Enterprise Division to oversee these lending activities. Half of all new loans are now made to small enterprises. Small enterprise lending is the fastest growing activity within the BIP. In 1980, new loans to SSEs increased by 188% (in dollar terms) compared to an increase of 31% in lending to medium and large enterprises.

In selecting the BIP as the implementing institution, the Mission considered other alternatives including the selection of COFIDE, since the GOP is promoting greater private sector participation for that institution. However, the Mission decided to concentrate the Project's

policy initiatives and institution-building efforts in the BIP because it is Peru's largest lender to SSEs. In addition, the World Bank's SSE program will work with COFIDE and will complement BIP's efforts by expanding SSE lending through other institutions. Finally, selection of the BIP permits a continuation of institution-building efforts begun under Rural Enterprises I and II.

b. Organization and Staffing

The BIP is controlled by a Board of Directors consisting of seven representatives: four from the Ministry of Economy, Finance and Commerce; one from the Ministry of Industry and Tourism; one from the the Ministry of Fishing; and one from the Ministry of Transportation and Communications. The chairman of the Board is elected from among the four representatives from the Ministry of Economy, Finance and Commerce. The Board of Directors is the policy-making body within the BIP and assures that the development objectives of the institution are carried out. The General Manager, appointed by the Board, is responsible for the internal administration of the Bank, and for the execution of institutional policies established by the Board of Directors. The BIP's organization chart is presented in Annex II, Exhibit G.

Currently, the BIP has a total staff of 1,588 employees of which 70% work in Lima and the remainder in branch offices. The BIP operates a network of 24 branches and four agencies divided into the four geographic regions of Peru, excluding Lima: North, South, Center and East. An office has been established in each region to coordinate and implement directives from Lima and to provide the necessary feedback from the field to the Lima Central Office. A staffing pattern by geographic regions is presented in the following table.

TABLE 6

Staff by Geographical Region

<u>Category</u>	<u>North</u>	<u>South</u>	<u>Center</u>	<u>East</u>	<u>Total</u>
Executives	12	13	13	3	41
Technicians (professionals)	100 (27)	80 (23)	85 (30)	30 (10)	295
Secretaries	23	17	22	6	68
Service	18	21	23	11	73
	<u>153</u>	<u>131</u>	<u>143</u>	<u>50</u>	<u>477</u>
Average personnel per branch	26	33	20	17	24

North: Chiclayo, Trujillo, Chimbote, Jaen, Cajamarca, and Piura.

South: Arequipa, Cuzco, Puno, and Tacna.

Center: Callao, Huancayo, Huaraz, Ica, San Ramon, Huanuco, and Ayacucho.

East: Iquitos, Pucallpa, and Tarapoto.

Annex II, Exhibit G presents the organizational structure of a typical BIP branch. There are three main functional divisions at the branch level: (1) legal, (2) credit, which promotes, processes, and evaluates loan applications; and (3) operations, which includes budgeting, cash transactions, and portfolio supervision. Table 6 presents the staffing patterns of BIP branches in Chiclayo, Chimbote, Ica, and Trujillo where it is anticipated that this Project will be implemented.

TABLE 7

Personnel Composition for Selected Branches

	<u>Chiclayo</u>	<u>Chimbote</u>	<u>Ica</u>	<u>Trujillo</u>
Chief of Region	1	--		
Administrator (Branch Manager)	1	1	1	1
Chief of Section	4	3	3	4
Other Professionals	3	1	3	3
Auxiliaries	12	11	11	12
Secretaries and Others	<u>7</u>	<u>4</u>	<u>5</u>	<u>7</u>
	28	20	23	27

The BIP is staffed with sufficient professionals and support technicians to implement its operations efficiently. Marginal increases in personnel may be required in order to carry out a non-traditional lending program and to meet the demand for credit that this Project is expected to generate. Additional staff may also be required later in the program for savings mobilization activities. Given the core of talented people now working for the BIP, meeting these additional personnel requirements is not expected to propose a problem.

As indicated above, the ability of the BIP to provide high quality technical assistance and service delivery at the branch level has been generally good. However, it has varied considerably from branch to branch and has often been highly dependent on the personal qualifications of branch managers. For this reason, Project technical assistance inputs will be directed primarily at the branch level to ensure consistency in high qualified staff management.

c. The Administrative Unit

(i) Organization. The Project will be coordinated by an UEF Coordinator who will report to the Manager of the Financial Division, who in turn reports to the General Manager. The UEF Coordinator will be responsible for coordinating and supervising urban branch office activities, and will serve as a main central office contact point for these branches.

At the field level, the UEF activities will be administered as part of normal lending operations. However, participating branches will receive special UEF support through staff training, technical assistance provided to the sub-borrowers, vehicles, and equipment.

(ii) Sub-loan Approval System. It is anticipated that approximately 95% of all sub-loans will be approved at the branch level. The applicant first presents a pre-qualification request containing basic information on his proposal. The branch technical staff then determines whether the sub-project is consistent with BIP policies and loan criteria. If so, an indication of interest will be expressed to the applicant within a matter of days, leading to drafting the formal loan application. The branch loan office will assist the applicant with this process. Once the application, together with other required documentation (legal, proforma invoices, etc.), is in hand, it goes to the appropriate approval body with the loan officer's recommendation. The completion of the application and obtaining the required documentation will be accomplished with assistance from BIP staff. As a result of the BIP's decentralization policy, the review process now takes an average of 30 days from the initial pre-qualification application to final approval.

(iii) Technical Assistance and Supervision. Technical assistance will include: (1) the training of BIP staff; (2) administrative, financial, management, and production advice to loan recipients as deemed necessary by the supervising branch loan officer; (3) promotion of the indexation option; and (4) technical and promotional assistance in savings mobilization. Sub-loan supervision will include site visits and personal contact between loan officers and their customers. Supervision should be managed easily, given the proximity of the bank branches to the targeted pueblos jovenes.

B. Financial Analysis

1. Project Financial Plan

The total cost of this four-year Project is estimated at US\$13,500,000, of which US\$10,000,000 will be loan-funded by AID and US\$3,500,000 will be contributed by the GOP. As shown in Table 8, Summary Costs Estimate and Financial Plan, approximately 96% of total funds to be provided to the Project will be applied toward the creation of an Urban Enterprise Development Credit Fund; the remainder will be used to finance local and foreign exchange costs of a technical assistance and training

package as well as commodities. ^{1/} The GOP, through the Banco Industrial del Peru, will finance the administration expenses of the Project, in addition to the 26% contribution to be made to the credit fund. The technical assistance component under the loan will finance the purchase of six vehicles with spare parts, office equipment for two branches in two pueblos jovenes of Lima, local and off-shore short-term training for BIP staff, approximately 60 training courses for sub-borrowers, two major project evaluations, and foreign and local short-term assistance for the savings mobilization campaign and for the indexation program. Table 9, Requirements of Foreign Exchange and Local Currency, reveals that the AID dollar share for the credit fund will be disbursed in local currency equivalent since the BIP, through its offices of exchange and of imports, will provide the necessary banking services for any imports. Less than US\$200,000 will be used to procure off-shore commodities and services. Table 10, Expected Disbursements by Calendar Year, shows the AID and GOP annual contributions to the UEF during the four-year life of the Project.

2. UEF Reflows

Table 11 presents cash flow projections for the UEF for a ten-year period. Using an average sub-loan size of \$8,500, over sixteen thousand sub-loans will be made during a ten-year period. Positive interest rates charged to sub-borrowers will ensure that reflows permit the expansion of the program to reach the largest number of beneficiaries.

^{1/} During the past year, USAID has encouraged BIP officials to pursue contacts with U.S. commercial banks with a view toward reaching agreement on co-financing for the proposed Project. The BIP has met with U.S. bankers on several occasions, but co-financing is not possible at this time because there was a reluctance on the part of both the BIP and the U.S. bankers to undertake what would have been a novel relationship for both parties. BIP officials, however, intend to actively continue discussions and as interest rates reach positive levels in the near future, the possibilities for securing commercial bank credit will improve greatly.

TABLE 8

Summary Cost Estimate and Financial Plan
(In US\$000)

APPLICATION	SOURCES		TOTAL
	AID	GOP	
Credit Fund	9,500	3,500	13,000
Technical Assistance			
- Training for BIP staff	45	-	45
- Training for Sub-borrowers	290	-	290
- Evaluations	25	-	25
- Short-term T.A.	30	-	30
Commodities			
- Vehicles and Office			
Equipment	110	-	110
TOTAL:	10,000	3,500	13,500
	74%	26%	100%

TABLE 9
Requirements of Foreign Exchange and Local Currency
(In US\$000)

APPLICATION	AID		GOP	TOTAL
	FX	LC	LC	
Credit Fund	-	9,500	3,500	13,500
Technical Assistance				
- Training for BIP Staff	25	20	-	45
- Training for Sub-borrowers	-	290	-	290
- Evaluation	25	-	-	25
- Short-term T.A.	25	5	-	30
Commodities				
- Vehicle and Office Equipment	100	10	-	110
TOTAL	175	9,825	3,500	13,500

TABLE 10
Expected Disbursements by Calendar Year
(In US\$000)

<u>Source/Application</u>	Year I	Year II	Year III	Year IV	Total
<u>AID</u>					
Credit Fund	1,000	2,500	3,500	2,500	9,500
Technical Assistance					
- Training for BIP Staff	10	20	15	---	45
- Training for Sub-borrowers	30	90	120	50	290
- Evaluation	---	10	---	15	25
- Short-term T.A.	20	10	---	---	30
Commodities					
- Vehicle and Office Equipment	110	---	---	---	110
<u>BIP</u>					
Credit Fund	370	920	1,290	920	3,500
TOTAL	1,540	3,550	4,925	3,485	13,500
=====					
Annual disbursement in Percentages	11%	26%	36%	27%	100%
Cumulative Percentages	11%	37%	73%	100%	

TABLE 11
Reflow Analysis

Terms: Interest rate: 60% (paid either by the borrower or the BIP under the M.O.V. clause)

Average repayment period: six years

Inflation Estimated at 60%/year

Sub-Loan Amount = $8,500 (1 + 0.2)^t$

t = 0 first year

t = 9 tenth year

	Yr-1	Yr-2	Yr-3	Yr-4	Yr-5	Yr-6	Yr-7	Yr-8	Yr-9	Yr-10
Beginning Balance	-	874	3,614	8,976	16,885	27,658	45,304	73,335	117,385	186,918
I. Receipts										
1.1 Sub-loans										
-A.I.D. Urban Loan	1,000	2,500	3,500	2,500	-	-	-	-	-	-
-BIP counterpart	370	920	1,290	920	-	-	-	-	-	-
1.2 Interest of Principal Collection	874	3,614	8,976	16,885	27,658	45,304	73,335	117,385	186,918	298,268
II. Disbursements										
2.1 Sub-loans Extended	1,370	4,294	8,404	12,396	16,885	27,658	45,304	73,335	117,385	186,918
III. Year-end Balance	874	3,614	8,976	16,885	27,658	45,304	73,335	117,385	186,918	298,268
Annual Sub-loans Extended	161	421	689	843	959	1,317	1,812	2,444	3,260	4,248
Cumulative Sub-loans Extended	161	582	1,271	2,114	3,073	4,390	6,202	8,646	11,906	16,154

3. BIP Financial Analysis

To examine the BIP's capabilities to carry out a self-sustaining lending program to SSEs, a detailed financial analysis of the BIP was undertaken to examine the present financial position of the BIP and provide greater detail on the BIP's financial structure. ^{1/}

a. Financial Structure

BIP's total assets remained stable in dollar terms during 1980 after 26% increase in 1979. Total assets, however, expanded by 37% in 1980 in sol terms, but were well below the 68% average increase achieved by development banks due to the crises of the Peruvian textile and fishing industries, which are seen as temporary, not structural, problems. The total loan portfolio increased by less than 1% in 1980 to \$282.6 million but net loans increased from 79% to 81.4% of total assets due to substantially lower provisions for doubtful loans. This, as well as a sharp \$8.2 million jump in non-current investment, helped offset a \$16.5 million drop in other assets (mainly related to foreign exchange operations), while short-term liquidity remained fairly stable.

BIP's capitalization increased sharply over the 1978/1980 period, to a point where the bank could be deemed to be over-capitalized in 1980. Leverage fell from 8.47 in 1978 to 6.21 in 1979 (very acceptable levels for development banks), to only 3.34% in 1980. Similarly, the capital ratio (total equity to total assets, including provisions) increased from 17.6% in 1978 to a high level of 26.4% in 1980. Bank debt alone represented only 2.7 times equity, down from 7.2 times in 1978. This resulted from large capital increases subscribe by the Treasury (\$5.8 million at average exchange rate) and by Customs (\$5.6 million which represents the 1% on all customs receipts payable to BIP under existing Decree) and from various IDB and USAID loans in the process of being capitalized. At the end of 1980, equity consisted of the following:

Capital	\$ 33.0
Contributions to be capitalized	36.1
Re-evaluation surplus	3.0
Legal reserve	0.6
Retained earnings	1.4
Net income for fiscal year	1.6
	\$ <u>75.7</u> million

^{1/} See Annex II, Exhibit H, for detailed financial tables (Comparative Balance Sheets, Comparative Income Statements, Statement of Resources & Application of Funds, and Comparative Ratios).

c. Loan Portfolio

BIP's net loan portfolio represented on the aggregate over 80% of total assets at the end of 1980 (\$267.7 million after provisions). The breakdown was the following:

TABLE 12
Breakdown of BIP's Loan Portfolio
by Type of Credit
(\$ million)

Regular loan portfolio	213.4	
o/w Ordinary credit		35.1
Export credit		102.8
IDB program		51.3
Supervised loans		2.4
Other (includes FDR)		21.8
Fishing Development Fund	26.1	
Discounted documents	14.5	
Housing loans	6.0	
Other	<u>22.6</u>	
	Total	<u>282.6</u>
(-) Provisions for doubtful accounts		<u>(14.9)</u>
Net loan portfolio		\$ <u>267.7</u> million
(Conversion rate: \$342.61 soles per \$)		

Apart from Banco de la Nacion (the GOP's bank and tax collector), this portfolio made the BIP Peru's second largest lending institutions slightly behind the Agricultural Bank.

As can be seen from the following table, 1980 was characterized by a very sharp increase in loans to the small enterprise and artisan sector, which jumped from 24.2% of loans extended in 1979 to 40.9% in 1980 (21.2% in 1978). Although loans to small enterprise represent today only about 30% of the aggregate loan portfolio, this percentage is rapidly increasing, and will continue to do so. For example, in December 1981, approximately 50% of all loans extended were to this particular sector and 4,773 loans to small enterprise were made in 1980, 35% of those to the consumer sector.

TABLE 13
Comparative Breakdown of Loans
Approved per Type of Enterprise (1979/1980)

	<u>1979</u>	<u>1980</u>
Medium/large enterprise	37.0%	28.2%
Small enterprise & artisan sector	24.2%	40.8%
Fishing & boat construction	8.7%	9.2%
Export financing	30.1%	21.8%
	<u>100.0%</u>	<u>100.0%</u>

Other developments to be noted are:

-- Loans made in the Lima/Callao metropolitan area fell from 65% in 1979 to only 50% in 1980 (on a marginal basis), reflecting BIP's strong support for the GOP's decentralization policy.

-- Working capital loans (26% of loans made in 1980) and loans for the acquisition of fixed assets (51%) increased vigorously in relatively terms against 1979, at the expense of pre-investment loans (22%).

As for the quality of the loan portfolio, total provisions for doubtful accounts fell from 7.3% of the total portfolio in 1979 to 5.3% in 1980. This encouraging drop resulted from substantially improved recovery procedures as well as the establishment at the branch level of committees responsible for follow-up actions on all over-due accounts. Of the total \$20.4 million (59%) was recovered in 1980--evidence of the effectiveness of these new policies. Year-end provisions of \$14.9 million are considered adequate, as they covered almost the entire \$15.5 million of overdue loans at that date.

Moreover, the breakdown of overdue loans shows that loans under court action and loans under liquidation represent only 7% and 2% respectively of the total.

TABLE 14
Breakdown of Overdue Loans at 12/31/81
(on basis of value)

Overdue since:	Less than 90 days	12%
	91 - 180 days	29%
	181 - 360 days	3%
	Over one year	47%
	In judicial proceedings	7%
	Loans under liquidation	2%
		<u>100%</u>

d. Profitability.

Return on equity has fallen regularly from 3.9% in 1978 to 3.2% in 1979 and 2.9% in 1980. While this level would not be considered satisfactory for a commercial bank, the BIP as a development bank is more interested in promoting industrial development than it is in maximizing profits. On the other hand, return on interest-earning assets improved slightly from 0.4% to 0.6% over the same period, as such assets have increased substantially less than equity over the past three years. Net income as compared to total income has been fairly constant at 2.4%. Return on loan portfolio inched up to 0.6% as net income for 1980 stood at \$1.57 million, or 45% higher than in 1979.

e. 1981 Third Quarter Statements.

The bank's unaudited, interim financial statements as of September 30, 1981, show no dramatic changes over the 1980 year-end position. Using the conversion rate as of that date (453.29 soles per US\$), total assets had increased by 21% in dollar terms to \$397.6 million, due mainly to a substantially higher loan portfolio (+ \$ 24 million on a net basis) and to larger adjustment accounts (pre-paid expenses, interest and commissions payable, and loans to share-holders and employees). However, erosion of the capital base due to high inflation was quite evident, with total equity falling from \$75.5 million to \$52.4 million. Consequently, leverage increased sharply to 6.48, still a quite acceptable level of indebtedness for a development bank.

Net earnings were behind the 1980 level, as they stood at \$1.0 million, or \$1.3 million on an annual basis, against \$1.6 million in 1980. This was due exclusively to a sharp drop in non-interest income, partly offset by a large drop in provisions for doubtful accounts.

f. Conclusion

Despite its reduced level of profitability, the BIP is in a sound financial position, as regular flow of capital resources has offset the negative effects of inflation and the decapitalization of BIP funds. The BIP is now preparing to adopt the new market-approach economic environment supported by the Belaunde administration, and to increase competition by shifting to a non-subsidized interest rate policy. The emphasis on savings mobilization and efforts to become more efficient through higher earning levels will be instrumental in making the BIP increasingly less dependent on outside transfers of resources.

C. Economic Analysis

1. The Small-Scale Enterprise Sub-Sector

Small-scale enterprises represent a large and dynamic sub-sector within Peru's industrial sector. Today, a conducive environment

for SSE development exists in Peru, as a result of supportive GOP policies and a current upward trend in economic activity within the industrial sector. 1/ The Belaunde government has explicitly emphasized the significant role to be played by SSEs in terms of employment and income generation. The new Industrial Law, currently being discussed in Congress, includes a small-scale industry section. The Law proposes more liberal labor legislation, simplified registration procedures, and a single tax to be levied on small firms as measures to increase the benefits to this sub-sector. Also, the current government has publicly encouraged the financial community to shift their lending focus from the public to the private sector. Cooperation by financial institutions, made evident in 1981 by the 23% real terms expansion in private sector credit compared to a 2.2% real terms increase in public sector credit, has instilled new life into the private sector. 2/

Information from the most recent industrial census, done in 1975, the SSE Registry, established in 1976, and a 1981 survey conducted by the Escuela Superior de Administracion de Negocios (ESAN) demonstrates the economic viability of the SSE sub-sector. 3/ The census data shows that in 1975, SSEs accounted for 87% of all manufacturing entities, 33.5% of total employment in the formal manufacturing sector, and 22% of value added. While more recent data has not been compiled on a national basis, the findings of the SSE Registry and ESAN survey are indicative of the continuing and expanding importance of the SSE sub-sector. 4/ Based on the estimated growth in the SSE sub-sector since that time to 40,000 firms and an average employment per firm of six, the SSE sub-sector provided 240,000 jobs or one-half the total industrial employment opportunities and one-third the value added in 1980. These contributions to the industrial sector have not been made at the expense of the economic efficiency of the SSE. In terms of gross returns to capital, estimates show little difference between SSEs and larger firms. 5/

1/ After a decline in industrial output and investment in 1977, industrial production recovered slightly in 1978 with a 4.1% increase and more strongly in 1980 with 5.9% increase.

2/ See Andean Report, February 1982.

3/ Census is taken nationwide. The Registry contains information on a total of 8,000 firms in the Lima-Callao area. The 1981 ESAN survey was conducted on 248 SSEs randomly selected from the firms included in the Registry, and therefore, limited as well to the Lima-Callao area.

4/ The survey data shows that, in 1980, about 74% of the SSEs in the Lima-Callao area had less than five employees and an additional 20% employed between five and ten people. Firms employing more than 30 employees comprised less than 1% of the total sample.

5/ See World Bank Appraisal Report. "Small Scale Enterprise Project," November 16, 1981.

2. Employment Generation

In light of Peru's high level of unemployment and underemployment, one of the most attractive attributes of the SSE sub-sector is its concentration on labor-intensive industries. Seventy-one percent of the SSEs surveyed in the ESAN study were involved in food processing, textiles, clothing products, and metal works, all labor-intensive activities. Based on 1980 values of SSE investment in machinery and equipment, and an average firm size of six employees, the average SSE capital investment per job is approximately \$4,000. ^{1/}

Given this very low cost per job created, it is calculated that under this Project, approximately 3,570 jobs will be generated. In terms of translating this employment into wage and salary benefits to SSE owners and employees, the ESAN survey found that the majority of SSE fulltime employees received the minimum legal wage. Using the present minimum wage of S/. 43,000 per month (approximately \$78.00), this Project will generate \$198 million in wage income, discounted over the first five years of returns. ^{2/} This statistic on job creation, however, underestimates the true employment impact of the program. Loans also helped to sustain employment or decrease the underemployment of owners, their family members, and employees working at the time of loan disbursement.

Another potential source of underestimation is the indirect employment generated through backward and forward linkages to the enterprise. The increased employment of suppliers of raw materials to the enterprise, marketing agents and retailers due to the expansion of UEF assisted firms, or those producing complementary goods, however, cannot be calculated.

3. SSE Demand for Credit

The majority of SSEs have traditionally operated outside the formal financial system. It is perceived by the BIP, and supported by USAID's experiences through other credit programs, that supply factors, rather than demand, explain much of the disassociation between the SSE sub-sector and formal financial institutions. However, this relationship is changing. Based on the shift in BIP lending from large- and medium-sized firms to small-scale enterprises and artisans over the last three years, and on the positive policy and economic environment for SSE development fostered by the current GOP, the BIP projects a continuing increase in SSE credit demand in the coming years. Between 1979 and 1980, for example, total BIP funds allocated to SSEs increased by more than 200%. In 1980, the BIP allocated \$61.4 million to SSEs. The BIP expects SSE demand for credit in

^{1/} ESAN found that the average investment by an SSE in machinery and equipment was the sol equivalency of \$23,000 at the 1980 end-of-year exchange rate. Therefore, \$23,000 divided by 6 produces an average investment (excluding land and buildings) per job of approximately \$4,000.

^{2/} This is a conservative estimate because (1) yearly wage increases are not incorporated into the analysis and (2) some employees will be earning more than the minimum wage. For example, the ESAN study estimated that owners of SSEs earn just under twice the minimum wage.

1982 to equal approximately \$74.0 million and projects a 10% annual increase in demand, in the coming years translating into \$109 million in SSE credit needs in 1986. ^{1/}

The BIP has not broken down this expected demand for credit by size of SSE. Projections have been broken down, however, by type of economic activity, including consumer goods, intermediate goods, capital goods, and other activities.^{2/} A potential demand for credit by this Project's target SSEs can be derived from the projected credit demand by the economic activities in which these smaller SSEs are concentrated. The majority of these activities fall within the consumer goods category and commerce and services category.^{3/} Table 15 presents the BIP's estimated credit demands by economic activity through 1986.

TABLE 15
Projected Credit Demand of Selected SSE Activities
1982 - 1986 ^{4/}
(millions of dollars)

	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>	
<u>Consumer Goods</u>	<u>23.5</u>	<u>25.7</u>	<u>28.1</u>	<u>31.2</u>	<u>34.0</u>	
Foods	11.5	13.0	14.7	17.0	19.0	
Shoes & leather products	4.5	5.0	5.6	6.2	6.8	
Textiles	2.9	3.0	3.1	3.2	3.0	
Furniture	1.8	1.9	1.9	1.9	2.0	
Others	2.8	2.8	2.9	2.9	3.0	
<u>Other Activities</u>	<u>8.9</u>	<u>10.4</u>	<u>12.1</u>	<u>14.2</u>	<u>16.1</u>	
Commerce	4.6	5.3	6.1	7.1	8.0	
Personal Services	4.3	5.1	6.0	7.1	8.1	
Total	32.4	36.1	40.2	45.4	50.1	204.2
	====	====	====	====	====	=====

As illustrated in the above Table, cumulative demand over the five year period by enterprises in these selected activities is expected to be approximately \$200 million.

^{1/} BIP loan solicitation document to IDB, 1981. These projections are consistent with the World Bank estimated of projected demand by SSEs of \$100.0 million over 1982 and 1983.

^{2/} Enterprises are broken down further within each category. For example, "Consumer Goods" includes foods, shoe making, textiles, furniture, printing and leather works.

^{3/} According to Ministry of Industry Statistics, 52% of SSEs are involved in the production of consumer goods.

^{4/} Banco Industrial del Peru 1981.

In addition to the studies and projections cited above, the assumption that demand for credit will exist under this Project is based on the experiences of other USAID credit programs to date. Two of the experiences from which this Project will benefit most are the Rural Enterprises I and II Projects. The evaluation of the latter demonstrates the substantial demand for credit that was generated as a result of the Project. One may partially discount the demand implications for this Project in light of the "cheap" funds that were made available to sub-borrowers at less than real rates of interest under the rural projects. However, current demand by rural enterprises under the BIP's new real interest rate lending policy exceeds available resources. BIP officials estimate that in 1982, under the new program of real interest rate lending and indexation, demand for credit by SSEs will reach \$3.2 million in Cajamarca alone. ^{1/}

Further evidence of the feasibility of lending at real interest rates--and demand for credit under such terms among small-scale enterprises--is provided by USAID's BANCOOP Project. The purpose of the BANCOOP Project was to assist agriculture and credit cooperatives to satisfy an unmet demand for rural production credit by upgrading BANCOOP's lending and savings mobilization program. To survive within Peru's inflationary economy, BANCOOP, in 1978, began to service individual small businessmen in addition to cooperatives. Today, individual loans including small enterprises account for approximately 80% of its lending portfolio. BANCOOP is successfully lending to these low-income entrepreneurs at rates that exceed 70% per annum.

The BANCOOP Project has demonstrated that provision of credit at real interest rates is affordable by low income individuals, similar in economic status to this Project's targeted beneficiaries. An 1981 evaluation of the BANCOOP Project states that BANCOOP is now in a stronger financial position than it was before it implemented its savings mobilization program and real interest rate lending policies. ^{2/} As of December 31, 1981, BANCOOP's total credit services averaged \$5.0 million per month.

In sum, in view of the limited data on economic activities in pueblos jovenes, an estimate of the potential demand for credit under this Project could not accurately be determined. However, based on the referenced studies on small-scale enterprises, the experience of other AID-financed credit programs, and the numerous public inquiries for credit received by the BIP's Small Enterprises Division each month, the BIP

^{1/} See Rural Enterprises II Evaluation.

^{2/} See BANCOOP Evaluation by Donald Larson and Dale Adams, May 8, 1981.

and USAID are convinced that the demand for credit will far exceed available funds once the UEF is established and disbursing. 1/

4. Benefit-Cost Analysis

The following benefit-cost analysis measures the discounted value of economic costs against the discounted value of economic benefits to the society as a whole resulting from this Project.

Capitalization of the UEF and the income generated as a return on the investments made to approximately 2,800 SSEs make up the bulk of the Project's economic costs and benefits, respectively. Without this Project, those 2,800 potential sub-borrowers, most of them at the smaller end of the SSE spectrum, will either not establish the enterprise (in the case of creating a new SSE) or not increase its production and productivity (in the case of expanding an established SSE) due to the continuation of scarce long- and medium-term credit available to this particular entrepreneurial class. Whereas, as mentioned earlier, through other international donors and domestic sources, increased credit resources are being made available to the private sector, most of these resources are channelled to larger-scale industries than those targeted under this Project. This Project is crucial in that it is a pilot effort to establish a self-sustaining credit mechanism through sound financial policies and to demonstrate to other formal lending institutions the financial viability of lending to this Project's urban target group.

a. Economic Costs

To evaluate the discounted cost stream, it is assumed that approximately 10% of Project funds will be disbursed in the first year, 25% in year two, 40% in year three, and 25% in year four. This disbursement schedule is shown below:

TABLE 16

Project Expenditure Flow 2/

Year 1	10%	\$ 1,350,000
Year 2	25%	3,375,000
Year 3	40%	5,400,000
Year 4	25%	3,375,000
Year 5-10	0	-0-
	Total:	<u>\$13,500,000</u>

1/ The BIP reports that its Small Enterprise Division is presently responding to over 1,000 inquiries per month regarding its lending program for Lima alone.

2/ Expenditures include costs of capitalizing the UEF and \$500,000 for commodities and technical assistance. Flow projections are derived from "Expected Disbursement by Calendar Year" presented in Table 10 of the Financial Analysis.

In addition to these costs, the analysis takes into consideration the costs to the SSE entrepreneurs receiving sub-loans under this Project and the administrative costs to the BIP of providing these loans. ^{1/} UEF loans will be made available for up to 90% of collateral, compared to a maximum of 60 to 70% under usual BIP guidelines, thereby requiring a minimum 10% contribution from the sub-borrower. Adding this 10% to the yearly expenditure flows presented above results in the following cost table:

TABLE 17

Expenditure Flows and Beneficiary Contribution

Year 1	10%	\$ 1,485,000
Year 2	25%	3,712,500
Year 3	40%	5,940,000
Year 4	25%	3,712,500
Year 5-10	0	0
	Total:	\$ <u>14,850,000</u>

Finally, added to the \$14,850,000 are the BIP's administrative costs of implementing this Project which, based on the Rural Enterprises II Project Evaluation, equal \$54 per loan. Applied to the expected yearly sub-loans to be made as a result of this Project, BIP administrative costs equal:

^{1/} Cost estimates were not imputed for factors such as time required by entrepreneurs to visit the BIP, fill out loan applications, etc. These "costs" are considered insignificant in light of the significant operational measures taken by the BIP to streamline the application process under the Project. These measures include the (1) general decentralization of BIP operations to the branch level including increased delegation of authority to approve loans; (2) location of new branches in areas convenient to pueblos jovenes residents; and (3) introduction of new simplified loan applications forms.

TABLE 18

BIP Administrative Costs

<u>Year</u>		<u>No. of SSE Investments</u> <u>1/</u>	<u>BIP Administrative</u> <u>2/</u> <u>Costs/Year</u>
1	10%	280	\$ 15,120
2	25%	700	37,800
3	40%	1,120	60,480
4	25%	700	37,800
	TOTAL	<u>2,800</u>	<u>\$ 151,200</u>

Adding annual administrative costs to Table 17 produces the following total cost table:

TABLE 19

Total Project Costs

Year 1	\$ 1,500,120
Year 2	3,750,300
Year 3	6,000,480
Year 4	3,750,300
Year 5-10	---
TOTAL:	<u>\$ 15,001,200</u> <u>3/</u>

1/ Based on an average loan size of \$5,300. Whereas the average size of loan under the rural project was about \$5,000, 60% of all loans disbursed between January 1978 and September 1980 were less than \$2,500.

2/ It is assumed that most of the administrative costs are incurred in the first year of loan disbursement. Whereas some administrative costs may be incurred afterwards, particularly in the case of delinquent payments, it is assumed that these follow-up costs will on average be minimal per loan and therefore are not incorporated into the analysis.

3/ Maintenance costs are not included in the analysis due to lack of any cost information. However, it is expected that maintenance costs will increase over the life of the investment, but will not make a significant difference in total costs. Likewise, it is assumed that entrepreneurs receiving loans will have the financial resources to cover the minimal costs of maintenance.

b. Economic Benefits

The average size of loan under this Project will be approximately \$5,300. Therefore, it is estimated that approximately 2,800 urban SSEs will receive credit. The benefit stream, as a result of capital investment in the SSE, is calculated assuming a 29% return on borrowed funds under the Project. This 29% return assumption is based on the findings of the Rural Enterprises II Evaluation which showed that the ratio of yearly increase in value added to loan amount averaged 29% among 80 small entrepreneurs surveyed in four rural market towns. ^{1/}

Given an average loan size of \$5,300, it can be calculated that the annual benefit per loan disbursed will be \$1,537 (29% of \$5,300). Benefits earned over a ten-year period are shown below:

TABLE 20
Total Benefits

<u>Year</u>	<u>No. of SSE Investments 2/</u>	<u>Increase in Value added</u>
1	280	---
2	980	430,360
3	2,100	1,506,260
4	2,800	3,227,700
5	2,800	4,303,600
6	2,800	4,303,600
7	2,800	4,303,600
8	2,800	4,303,600
9	2,800	4,303,600
10	2,800	4,303,600
11	2,520	4,303,600
12	1,820	3,873,240
13	700	2,797,340
14	---	1,075,900
	TOTAL:	43,036,000
		=====

^{1/} Figured into this 29% is the business failure of one surveyed entrepreneur, causing a dramatic decrease in net income. It is estimated that had that SSE not failed, the annual return on the loan would have been as high as 40%. However, for purposes of analysis, the more conservative figure is being used.

^{2/} Assuming an average ten-year life of equipment, requiring no or minimal maintenance. Based on this assumption, equipment purchased in the first year of this Project will be fully depreciated by year eleven, equipment purchased in second year will be fully depreciated by year twelve, etc.

c. Ratio of Benefits to Costs

At a 15% per year social discount rate, ratios of benefits to costs are stated below:

TABLE 21

DISCOUNTED COSTS AND BENEFITS

<u>Year</u>	<u>Benefits</u>	<u>Costs</u>
1	---	1,305,104
2	325,352	2,835,227
3	991,119	3,948,316
4	1,846,244	2,145,172
5	2,138,889	
6	1,859,155	
7	1,618,154	
8	1,407,277	
9	1,222,222	
10	1,062,989	
11	925,274	
12	724,296	
13	455,966	
14	151,702	
Total:	\$ 14,728,639	\$10,233,819

Benefit/Cost = 1.44

d. Sensitivity Analysis

The following sensitivity analysis incorporates incidences of business failures and calculates the benefit-cost ratios assuming an annual 3% and 5% rate of business failure of SSEs receiving loans under this Project. ^{1/}

^{1/} The 3% failure rate was chosen based on the assumption that 9% of the sub-borrowers will be delinquent in their loan repayments (based on the findings of the Rural Enterprises II Evaluation) and that one-third of this 9% will default. A 5% failure rate is considered extremely high in light of a 9% delinquency rate.

THREE PERCENT FAILURE RATE

<u>Year</u>	<u>No. of SSE Investments</u> <u>1/</u> (cumulative)	<u>Increase in Value Added</u> <u>2/</u> \$
1	272	---
2	951	316,056
3	2,037	961,790
4	2,716	1,790,857
5	2,716	2,074,723
6	2,716	1,803,381
7	2,716	1,569,609
8	2,716	1,365,059
9	2,716	1,185,556
10	2,716	1,031,100
11	2,444	897,516
12	1,801	702,452
13	679	451,206
14	---	147,151
TOTAL:		14,296,456 =====

Benefit/Cost + \$14,296,456/\$10,233,819= 1.40.

FIVE PERCENT FAILURE RATE

<u>Year</u>	<u>No. of SSE Investments</u> (cumulative)	<u>Increase in Value Added</u>
1	266	---
2	931	309,085
3	1,995	941,563
4	2,660	1,753,932
5	2,660	2,031,945
6	2,660	1,766,197
7	2,660	1,537,246
8	2,660	1,336,913
9	2,660	1,161,111
10	2,660	1,009,840
11	2,394	879,010
12	1,729	688,081
13	665	433,268
14	---	144,117
TOTAL:		13,992,208

Benefit/Cost = 13,992,208/10,233,819 = 1.37

1/ Assumes that purchased equipment by entrepreneur whose businesses fail is of no economic worth to the society.

2/ Discounted.

D. Social Soundness Analysis

1. Target Population

The Project's target group comprises an estimated three million pueblo joven residents around the cities of Lima (north and south cones), Ica, Chimbote, Chiclayo, and Trujillo. These pueblos juvenes are characterized by high population density, minimal social services, limited employment opportunities, and little or no access to formal income-generating inputs such as credit, machinery, or skills training. Pueblos juvenes make up the fastest growing sections of Peru's sprawling urban centers. The growth of the six Project areas is largely the result of massive rural-to-urban migration which has characterized Peru's demographic patterns over the past thirty years.

Despite the extensive literature on pueblos juvenes, the heterogeneous make-up of the migrants makes a "typical" characterization of its residents superficial. A number of studies provide, however, a general insight into the pueblo joven dweller permitting the following observations. Although the majority of migrants are the peasant background, most have lived in small cities and market towns in the sierra or jungle before migrating to the coast. In the case of Lima residents, many have also previously lived in secondary coastal cities. Most pueblo joven residents have received some formal education training, however the majority have not gone beyond primary school. Employment profiles are characterized by a predominance of blue-collar workers and independent service workers including street vendors and other individual types of jobs.

The family unit plays an important socio-economic role. Many economic decisions are made within the context of the family rather than the individual. For example, income generation is seen as a family task. Usually all family members are engaged in some form of income generating activity regardless of the low earnings characteristic of many of these jobs. Individual receptivity to low-paying, part-time, minimal labor is heightened by this family-oriented approach. Therefore, whereas individual earnings may be minimal, they are considered as a contribution to the larger and more important variable of total family income. In most SSEs women are integrally involved in the many facets of running the business. In the areas of food processing, textiles, and artisanry, women usually share equal responsibility with the men in production and marketing of the product. In other less women-oriented businesses such as metal works, women assume administrative, bookkeeping, and marketing responsibilities. Recognition of this family orientation is important to understanding the response of pueblo joven residents to the many difficult social and economic decisions facing them on the daily basis.

Based on the experience of the Rural Enterprises Projects and information available on Peruvian SSEs, a general picture can also be derived of pueblo joven entrepreneurs, providing greater insight into the

- Project's direct beneficiaries--entrepreneurs operating and residing in target pueblos jovenes and the workers that they will hire. Entrepreneurs are, by definition, risk takers relative to other pueblos jovenes residents. They are usually economically better off than their neighbors due to previous work experience. In many cases, this relative economic well-being has afforded the pueblo joven entrepreneur flexibility as witnessed by his moving to more established, although marginal, communities.

The Project sub-borrower will usually have some experience in a technical field. A 1980 survey demonstrates that roughly 18% of all SSE owners possess technical skills passed down through family generations and 66% acquired skills on the job in other workplaces. ^{2/} Although experience varies with the size of the firm, pueblo joven entrepreneurs generally will have had little access to and experience with credit; some, perhaps 15% or fewer, will have secured a short-term loan from a commercial bank. According to a 1978 survey of the smaller SSEs, only 10% of the firms had any contact with financial institutions or received any technical assistance. ^{3/} Also, it was found in an earlier study that 71% of the surveyed firms had been capitalized through the entrepreneurs' savings and an additional 17% by informal loans from family and friends. ^{4/} This reliance on personal savings and informal credit channels is due to the lack of formal sources of medium- and long-term credit in Peru in general, and to small entrepreneurs in particular. It is also indicative of the strong family/friend orientation of these entrepreneurs.

As in practically all other aspects of pueblo joven life, the family unit plays a significant role in the SSE. In over two-thirds of the enterprises registered with the Ministry of Industry and Tourism, the majority of family members worked in the SSE. A study of 250 SSEs conducted by the Escuela Superior de Administracion de Negocios (ESAN) found that approximately 42% of the enterprises surveyed were in the owner's home and that 17% of the SSE owners made business decisions jointly with other family members. ^{5/}

^{1/} At least 80% of the SSE entrepreneurs receiving loans under this Project will reside in pueblos jovenes.

^{2/} As cited in "La pequeña industria: Para sacarla del olvido", Actualidad Economica, November 1980.

^{3/} Ibid.

^{4/} Minkarier. "Klimindustrie in Peru" 1976. (Also cited in Actualidad Economica, November 1980).

^{5/} These figures are probably higher among this Project's beneficiaries since the ESAN study surveyed a number of SSE at the larger end of the spectrum which would not be considered eligible for funding under this Project.

Indirect beneficiaries, equally important in terms of the Project strategy, are the pueblo joven residents that will be hired by the newly created or expanded SSE. In firms with less than five employees, immediate and extended family members will provide most of the labor. One study shows that of all SSEs registered in 1975, 62% employed four workers or less and family members made up the majority of those employed. ^{1/} As might be expected, slightly larger industries (up to 14 employees) employed only a small number of family members in the work place. ^{2/} This is due not only to an obvious requirement for more labor, but perhaps also to the relative wealth of these entrepreneurs, which permits other family members to carry out non-income generating activities. Recruitment of additional personnel is usually made through personal contacts and wages are negotiated on an individual basis. The ESAN study shows that over 50% of those hired by SSEs had little or no technical training or experience when they were hired. However, it also shows a low turnover rate among these employees, indicating that many gain valuable skills and experience on the job.

2. Socio-Cultural Feasibility

At the enterprise level, a number of socio-cultural constraints have been previously identified. ^{3/} The entrepreneur's lack of familiarity with the formal banking system, unknowns in undertaking a business enterprise, and the problems often encountered in dealing with a government bureaucracy present potential obstacles to obtaining credit through formal channels and initiating or expanding a small-scale enterprise. ^{4/}

As with the Rural Enterprises lending program, the proposed Project--through technical assistance and new operational procedures--has been designed to respond to these constraints. At the enterprise level, a simplified credit procedure, including faster processing of the credit application, is a key operational component of the Project. Technical assistance to the sub-borrower during preparation of the loan application will be important to expedite the process and to build confidence in the entrepreneur in his dealings with formal financial institutions. The evaluation of the Rural Enterprises II Project shows that BIP branch personnel that participate in the program are dedicated to their tasks and culturally sensitive to their clients, and that they closely monitor the progress of their sub-loans to ensure their success.

^{1/} TABINI-ALACORTA, 1979.

^{2/} Minkarer found that this size SSE employed on the average two family members. See previous citation.

^{3/} See Section II.C. of the Project Paper.

^{4/} Likewise, lack of experience in dealing with the limited resource entrepreneur is also an important constraint at the institutional level.

At the institutional level, BIP personnel will be trained to assist the sub-borrower in lending procedures and options. The indexed system, for example, will be presented in a way that is comprehensible to the loan applicant who is not well-versed in financial matters. To encourage the high performance standard displayed by the BIP's rural branch loan offices among lower level urban branch personnel, a substantial portion of technical assistance funds will be reserved for the branch level. This effort will increase the quality of performance as well as provide incentives for branch personnel who often resent what they perceive to be preferential treatment afforded to central BIP personnel.

Initiating or expanding a business involves a number of risks and unknowns that determine enterprise success. By assisting in the preparation of the loan application, BIP staff will work with sub-borrowers and in some cases identify training needs. A basic assumption for providing assistance, however, is that the entrepreneur does not need to be coddled or protected. By definition, he is energetic, self-reliant, and innovative. Furthermore, he will possess a number of traits that may minimize the risks involved. As described above, he will usually have had experience in a previous market endeavor (even if this simply involves street vending); he will be investing in a field where he has past experience; and he will usually be undertaking his efforts with considerable family support. ^{1/} Family members, for example, are more likely to participate in all enterprise functions--including management and decision making--than are other workers. Hence, benefits to this group not only consist of wages but also business management experience. This attribute is particularly important with respect to the promotion of women as entrepreneurs. Although the experience of the Rural Enterprises Projects indicates that the number of women taking out loans may be small, many actively participate in all functions of the enterprise. Available data indicates a labor absorption problem for women in many formal sector activities. In this regard, the promotion of SSEs presents a viable strategy for incorporating women into the labor force.

With respect to the introduction of new BIP lending policies, BIP personnel should deal with the entrepreneur as an assured and self-reliant individual. Indexation of loans, for example, may be a complicated procedure involving the financial risk of unknown future payments. Indeed, as discussed earlier, some BIP personnel question the receptivity of this option among "unsophisticated" borrowers; yet experience

^{1/} In addition, the SSE and its functions are familiar to pueblo joven residents. It is estimated, for example, that 25% of the registered SSEs in the Lima-Callao area are located in pueblos juvenes. This is a relatively high number considering the traditional concentration of industry in the center urban areas. Including unregistered SSEs, the percentage becomes higher.

has demonstrated that the target sub-borrower, like his rural counterpart, has considerable intuitive understanding of the potential benefits of financial transactions, and is more sophisticated than expected.

Given the experience of the Rural Enterprises Projects, and the socio-cultural constraints analyzed during PP preparation and incorporated in the Project design, the Project Development Committee concludes that the Project is socially sound and feasible.

3. Beneficiaries and Spread Effects

Approximately 2,800 urban entrepreneurs will receive sub-loans under the Project and approximately 3,570 jobs will be generated as a result of the initiation or expansion of these SSEs. Reflows from Project funds will also rapidly increase the total number of direct beneficiaries. Over 16,000 people will receive sub-loans during a ten-year period. In addition, spread effects anticipated from the Project will enhance the number of total beneficiaries. These spread effects are due to increased business activities through both backward and forward linkages and demonstration effects on other potential entrepreneurs and financial institutions. Although the number of indirect jobs is difficult to calculate, it is estimated that as many as 10,000 jobs could be created (or maintained) through increased economic activity. ^{1/}

Another important spread effect of the Project will be demonstrating the financial feasibility of lending to SSEs and of savings mobilization in marginal urban areas. The result will be the expansion of banking services in the pueblos juvenes, a financial sector objective of this Project. Policy measures taken by the GOP will stimulate this objective by increased competition. Lastly, innovation and new methods of production will be indirectly stimulated. A substantial number of pueblo joven residents, although having rudimentary business skills, have a traditional risk-aversion attitude. A primary manifestation of this is a tendency not to undertake new procedures until they observe the positive results of an innovator. To the extent that the more innovative and aggressive urban entrepreneurs receive credit from the UEF, the Project will provide significant incentives for sub-project duplication.

^{1/} As cited in Rural Enterprises II PP, experiences in Latin America show a 3:1 employment multiplier per new job created.

PART V. IMPLEMENTATION ARRANGEMENTS

A. Administrative Arrangements

1. Industrial Bank (BIP)

The UEF coordinator and participating branch offices of the BIP will be responsible for administering the fund.

After the Project Agreement is signed, the BIP will: (1) draft the UEF Credit Operations Manual; (2) draft the UEF Technical Assistance Plan; (3) train the staff designated to implement the Project; and (4) begin the development and distribution of promotional materials in the target urban areas.

Once the Conditions Precedent are met, implementation will focus on the identification, appraisal, approval, and execution of sub-projects financed by the fund, and the monitoring and collection of outstanding credits.

2. AID

a. Monitoring

The Project will not involve unusual administrative features for AID or additional AID staff. AID personnel will work closely with the BIP's implementation unit during the stage of meeting Conditions Precedent. Thereafter, USAID's role will principally be one of monitoring Project performance.

Monitoring will be exercised by the USAID Project Committee with the following responsibilities.

i. A Project Manager will be assigned from Mission's Office of Development Resources to maintain contact with the BIP, to ensure that the provisions of the AID Loan Agreement and Implementation Letters are met, and to approve all vouchers for disbursement.

ii. The Mission Controller will review disbursement requests for conformity with AID Regulations, and will ensure that adequate financial controls are exercised.

iii. Other Mission offices may be called upon to review sub-loan requests above the BIP's authorized amount, and to assist with sub-project inspections.

b. Reporting

BIP records on sub-projects and sub-borrowers will be open to AID. The BIP will submit the following reports:

i. A Quarterly Progress Report showing the status of UEF commitments, disbursements, and recuperations, detailed by sub-project and region. The report will analyze sub-borrowers' effective interest rate structure and ensure that it is in accordance with the Central Bank's annual inflation estimate for the previous six months. It will also include technical assistance activities and overall Project status.

ii. Quarterly Shipping Reports (to be required only in the event of, and after the initiation of, ocean shipping).

iii. An annual audit report on the UEF prepared by an independent auditor acceptable to AID.

c. Disbursement Procedures

No deviation from established AID disbursement procedures is anticipated. Materials and equipment procured in the United States or other Code 941 countries and the foreign exchange costs of technical assistance contracts may be paid through AID's standard procedures regarding Letters of Commitment/Letters of Credit. Requests to open Letters of Commitment will contain certification that the items listed are required for the Project and are eligible for financing under the Loan. Disbursement for local currency costs will likewise be made in an established manner acceptable to AID. An advance will be made to the fund to cover planned lending for a three-month period, and will be replenished as needed.

d. Procurement Procedures

The source and origin of goods and services procured under the Loan and the procurement procedures followed under sub-loans will be in accordance with AID requirements applicable to intermediate credit institutions projects (see AID Handbook 1, Supplement B, Chapter 19). Procurement of goods and services by the BIP for its own account will be in accordance with host country contracting rules and will be carried out by the BIP.

B. Implementation Plan

The \$10 million Project Agreement will be executed by the Ministry of Economy, Finance and Commerce. The BIP will be designated as implementing agency under the Project, and the UEF Unit of the BIP will have overall responsibility for Project planning, credit administration, evaluations, and coordination of other inputs such as technical assistance and training.

The implementation schedule allows for a three-month start-up period following signature of the Project Agreement to fulfill all

Conditions Precedent, and a four-year disbursement period to fully commit and disburse the UEF to eligible sub-projects:

1. Loan Authorized	March 30, 1982 .
2. Project Agreement signed	June 30, 1982
3. Conditions Precedent met	October 15, 1982
4. Disbursement of Credit Fund begins	November 1, 1982
5. First Project Evaluation	November 1, 1983
6. Final Project Evaluation	September 30, 1986

C. Evaluation Plan

The Project will be continually monitored by the BIP and USAID, and regular joint USAID/BIP reviews will be held.

In addition to the periodic reviews, two major Project evaluations are planned. The first evaluation will be made approximately 12 months after the first Loan disbursement to permit early identification and solution of implementation problems. Following the PACD, a second in-depth evaluation will be undertaken to assess the impact of the Project at both the enterprise and institutional levels. Topics to be reviewed will include:

1. Target Enterprises

- income and assets generated
- employment generated
- value added
- productivity
- socio-economic groups benefitted
- technological change
- effects of optional interest rate policy

2. Industrial Bank

- integration of Project concept within the Bank
- cost of credit
- cost and effectiveness of technical assistance
- bad debt management
- implementation of optional interest rate policy

D. Negotiating Status

This Project proposal has been prepared in close collaboration with BIP management and staff, and with the endorsement of the Minister of Economy, Finance and Commerce and the President of the Republic. Given BIP familiarity with the two previous AID-financed Fondo de Desarrollo Rural projects, and their similarity to this proposal, negotiation and execution of the Project Agreement should proceed rapidly.

E. Environmental Consideration

The USAID/Peru Project Committee has undertaken a complete Initial Environmental Examination (IEE) of the Project's environmental impact and has arrived at a recommendation for a negative determination with which the AA/LAC has concurred.^{1/}

1/ See Annex I, Exhibit G for IEE.

ANNEXES

COUNTRY CHECKLIST

A. GENERAL CRITERIA FOR COUNTRY ELIGIBILITY

1. FAA Sec. 116.(a) Has the Department of State determined that this government has engaged in a consistent pattern of gross violations of internationally recognized human rights?
(b) If so, can it be demonstrated that contemplated assistance will directly benefit the needy? No
2. FAA Sec. 113. Has particular attention been given those programs, projects, and activities which tend to integrate women into the national economies of developing countries, thus improving their status and assisting the total development effort? Yes
3. FAA Sec. 481. Has it been determined that the government of the recipient country has failed to take adequate steps to prevent narcotic drugs and other controlled substances (as defined by the Comprehensive Drug Abuse Prevention and Control Act of 1970) produced or processed, in whole or in part, in such country, or transported through such country, from being sold illegally within the jurisdiction of such country to U.S. Government personnel or their dependents, or from entering the U.S. unlawfully? No
4. FAA Sec. 620(b). If assistance is to a government, has the Secretary of State determined that it is not dominated or controlled by the international Communist movement? Yes
5. FAA Sec. 620(c). If assistance is to a government, is the government liable as debtor or unconditional guarantor on any citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) the debt is not denied or contested by such government? No.

6. FAA Sec. 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 to 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? No

7. FAA Sec. 620(a), 620(f), 620D; Continuing Resolution Sec. 511, 512 and 513; ISDCA of 1980 Secs. 717 and 721. Is recipient country a Communist country? Will assistance be provided to Angola, Cambodia, Cuba, Laos or Vietnam? (Food and humanitarian assistance distributed directly to the people of Cambodia are excepted). Will assistance be provided to Afghanistan or Mozambique without a waiver? Are funds for El Salvador to be used for planning for compensation, or for the purpose of compensation, for the confiscation nationalization, acquisition or expropriation of any agricultural or banking enterprise, or property or stock thereof? No

8. FAA Sec. 620(i). Is recipient country in any way involved in (a) subversion of, or military aggression against, the United States or any country receiving U.S. assistance, or (b) the planning of such subversion or aggression? No

9. FAA Sec. 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? No

10. FAA Sec. 620(k). Does the program furnish assistance in excess of \$100,000,000 for the construction of a productive enterprise, except for productive enterprises in Egypt that were described in the Congressional Presentation materials for FY 1977, FY 1980 or FY 1981? No

11. FAA Sec. 620(1). If the country has failed to institute the investment guarantee program for the specific risks of expropriation, inconvertibility or confiscation, has the AID Administrator within the past year considered denying assistance to such government for this reason? Yes
12. FAA Sec. 620(m). Is the country an economically developed nation capable of sustaining its own defense burden and economic growth, and if so, does it meet any of the exceptions to FAA Section 620(m)? No
13. FAA Sec. 620(o); Fishermen's Protective Act of 1967, as amended, Sec. 5. If country has seized, or imposed any penalty or sanction against, any U.S. fishing activities in international waters,
- a. has any deduction required by the Fishermen's Protective Act been made? No
- b. has complete denial of assistance been considered by AID Administrator? Yes
14. FAA Sec. 620(q); Continuing Resolution Sec. 518.
(a) Is the government of the recipient country in default for more than six months on interest or principal of any AID loan to the country? (b) Is the country in default exceeding one year on interest or principal on any U.S. loan under a program for which the Continuing Resolution appropriates funds? No
15. FAA Sec. 620(s). If contemplated assistance is development loan or from Economic Support Fund, has the Administrator taken into account the percentage of the country's budget which is for military expenditures, the amount of foreign exchange spent on military equipment and the amount spend for the purchase of sophisticated weapons systems? Yes, taken into account by the Administrator at time of approval of Agency OYB.

16. FAA Sec. 620(t). Has the country severed diplomatic relations with the United States? If so, have they been resumed and have new bilateral assistance agreements been negotiated and entered into since such resumption? No
17. FAA Sec. 620(u). What is the payment status of the country's U.N. obligations? If the country is in arrears, were such arrearages taken into account by the AID Administrator in determining the current AID Operational Year Budget? Payment status is up to date.
18. FAA Sec. 620A; Continuing Resolution Sec. 521. Has the country aided or abetted, by granting sanctuary from prosecution to, any individual or group which has committed an act of international terrorism? Has the country aided or abetted, by granting sanctuary from prosecution to, any individual or group which has committed a war crime? No
19. FAA Sec. 666. Does the country object, on the basis of race religion , national origin or sex, to the presence of any officer or employee of the U.S. who is present in such country to carry out economic development programs under the FAA? No
20. FAA Sec. 669, 670. Has the country, after August 3, 1977, delivered or received nuclear enrichment or re-processing equipment, materials, or technology, without specified arrangements or safeguards? Has it detonated a nuclear device after August 3, 1977, although not a "nuclear-weapon State" under the nonproliferation treaty? No

B. FUNDING SOURCE CRITERIA FOR COUNTRY ELIGIBILITY

1. Development Assistance Country Criteria

- a. FAA Sec. 102(b)(4). Have criteria been established and taken into account to assess commitment progress of the country in effectively involving the poor in development, on such indexes as: (1) increase in agricultural productivity through small-farm labor intensive agriculture, (2) reduced infant mortality, (3) control of population growth, (4) equality of income distribution, (5) reduction of unemployment and (6) increased literacy.

Yes, the evidence of this commitment and progress is Peru's counterpart contributions to AID projects carrying out the goals stated herein.

b. FAA Sec. 104(d)(1) If appropriate, is this development (including Sahel) activity designed to build motivation for smaller families through modification of economic and social conditions supportive of the desire for large families in programs such as education in and out of school, nutrition, disease control, maternal and child health services, agricultural production, rural development, assistance to urban poor and through community-based development programs which give recognition to people motivated to limit the size of their families?

Yes

2. Economic Support Fund Country Criteria

a. FAA Sec. 502B. Has the country (a) engaged in a consistent pattern of gross violations of internationally recognized human rights or (b) made such significant improvements in its human rights record that furnishing such assistance is in the national interest?

N.A.

b. FAA Sec. 532(f). Will ESF assistance be provided to Syria?

N.A.

c. FAA Sec. 609. If commodities are to be granted so that sale proceeds will accrue to the recipient country, have Special Account (counterpart) arrangements been made?

N.A.

d. FAA Sec. 620B. Will ESF be furnished to Argentina?

N.A.

PROJECT CHECKLIST

A. GENERAL CRITERIA FOR PROJECT

1. Continuing Resolution Unnumbered;
FAA Sec. 634A; Sec. 653(b).

(a) Describe how authorizing and appropriations Committees of Senate and House have been or will be notified concerning the project;

(b) is assistance within (Operational Year Budget) country or international organization allocation reported to Congress (or not more than \$1 million over that amount)?

(a) A description of this project was included in the Congressional Presentation for FY 1982 and 1983.

(b) Yes.

2. FAA Sec. 611(a)(1). Prior to obligation in excess of \$100,000, will there be (a) engineering, financial other plans necessary to carry out the assistance and (b) a reasonably firm estimate of the cost to the U.S. of the assistance?

(a) Yes

(b) Yes

3. FAA Sec. 611(a)(2). If further legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of purpose of the assistance?

No further legislative action necessary.

4. FAA Sec. 611(b); Continuing Resolution Sec. 501. If for water or water-related land resource construction, has project met the standards and criteria as set forth in the Principles and Standards for Planning Water and Related Land Resources, dated October 25, 1973.

N.A.

5. FAA Sec. 611(e). If project is capital assistance (e.g., construction), and all U.S. assistance for it will exceed \$1 million, has Mission Director certified and Regional Assistant Administrator taken into consideration the country's capability effectively to maintain and utilize the project?

611(e) certification is included in the project paper

6. FAA Sec. 209. Is project susceptible of execution as part of regional or multilateral project? If so, why is project not so executed? Information and conclusion whether assistance will encourage regional development programs.
- The project is not susceptible to regional multilateral execution.
7. FAA Sec. 601(a). Information and conclusions whether project will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; and (c) encourage development and use of cooperatives, and 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.
- The project will contribute to:
(a) increased production of some exportable items - mainly artesanía
(b) increase private initiative and competition - through the establishment of new, generally privately owned, urban small businesses; (c) increase incomes of urban populace - making more money available for savings; (d) discourage monopolistic practices through providing heretofore scarce credit to new enterprises; (e) Technical assistance under the project will improve the technical efficiency of some participating small enterprises; (f) the strengthening of free labor to a marginal extent (though it will create employment).
8. FAA Sec. 601(b). Information and conclusion on how project will encourage U.S. private trade and investment abroad and encourage private U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise).
- The project may encourage more private U.S. trade in small exportable items from Peru but will not significantly increase trade or foster private U.S. participation in foreign assistance programs.
9. FAA Sec. 612(b), 636(h); Continuing Resolution Sec. 508. 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 in lieu of dollars.
- The GOP will contribute the equivalent US\$3.5 million to the credit fund on a pari passu basis and therefore helps finance each subloan made. The U.S. owns no Peruvian currency available for use in financing this project.
10. FAA Sec. 612(d). Does the U.S. own excess foreign currency of the country and, if so, what arrangements have been made for its release?
- No

11. FAA Sec. 601(e). Will the project utilize competitive selection procedures for the awarding of contracts, except where applicable procurement rules allow otherwise?

Yes

12. Continuing Resolution Sec. 522. If assistance is for the production of any commodity for export, is the commodity likely to be in surplus on world markets at the time the resulting productive capacity becomes likely to cause substantial injury to U.S. producers of the same, similar or competing commodity?

N.A.

B. FUNDING CRITERIA FOR PROJECT

1. Development Assistance Project Criteria

a. FAA. Sec. 102(b), 111, 113, 281(a). Extent to which activity will (a) effectively involve the poor in development, by extending access to economy at local level, increasing labor intensive production and the use of appropriate technology, spreading investment out from cities to small towns and rural areas, and insuring wide participation of the poor in the benefits of development on a sustained basis, using the appropriate U.S. institutions; (b) help develop cooperatives, especially by technical assistance, to assist rural and urban poor to help themselves toward better life, and otherwise encourage democratic private and local governmental institutions; (c) support the self-help efforts of developing countries; (d) promote the participation of women in the national economies of developing countries and the improvement of women's status; and (e) utilize and encourage regional cooperation by developing countries?

This project will (a) involve the poor by targetting into urban slums of Peru where the majority of the urban poor live, generating employment for them in small urban business concerns; (b) not involve cooperative development.

b. FAA Sec. 103, 103A, 104, 105, 106, 107. Is assistance being made available: (include only applicable paragraph which corresponds to source of funds used. If more than one fund source is used for project, include relevant paragraph for each fund source).

(1) [103] for agriculture, rural development or nutrition; if so (a) extent to which activity is specifically designed to increase productivity and income of rural poor; 103A if for agricultural research, full account shall be taken of the needs of small farmers and extensive use of field testing to adapt basic research to local conditions shall be made; (b) extent to which assistance is used in coordination with programs carried out under Sec. 104 to help improve nutrition of the people of developing countries through encouragement of increased production of crops with greater nutritional value, improvement of planning, research, and education with respect to nutrition, particularly with reference to improvement and expanded use of indigenously produced foodstuffs; and the undertaking of pilot or demonstration of programs explicitly addressing the problem of malnutrition of poor and vulnerable people; and (c) extent to which activity increases national food security by improving food policies and management and by strengthening national food reserves, with particular concern for the needs of the poor, through measures encouraging domestic production, building national food reserves, expanding available storage facilities, reducing post harvest food losses and improving food distribution.

N.A.

(2) [104] for population planning under sec. 104(b) or health under sec. 104(c); if so, (i) extent to which activity emphasizes low-cost, integrated delivery systems for health, nutrition and family planning for the poorest people, with particular attention to the needs of mothers and young children, using paramedical and auxiliary medical personnel, clinics and health posts, commercial distribution systems and other modes of community research

N.A.

(3) [105] for education, public administration, or human resources development; if so, (i) extent to which activity strengthens nonformal education, makes formal education more relevant, especially for rural families and urban poor, or strengthens management capability of institutions enabling the poor to participate in development; and (ii) extent to which assistance provides advanced education and training of people in developing countries in such disciplines as are required for planning and implementation of public and private development activities.

N.A.

(4) [106; ISDCA of 1980, Sec. 304] for energy, private voluntary organizations, and selected development activities; if so,, extent to which activity is: (i) (a) concerned with data collection and analysis, research on and development of suitable energy sources, and pilot projects to test new methods of energy production; (b) facilitative of geological and geophysical survey work to locate potential oil, natural gas, and coal reserves and to encourage exploration for potential oil, natural gas, and coal reserves; and (c) a cooperative program in energy production and conservation through research and development and use of small scale, decentralized, renewable energy sources for rural areas;

(ii) technical cooperation and development, especially with U.S. private and voluntary or regional and international development organizations;

N.A.

(iii) research into, and evaluation of economic development process and techniques;

N.A.

(iv) reconstruction after natural or manmade disaster;

N.A.

(v) for special development problems, and to enable proper utilization of earlier U.S. infrastructure, etc. assistance;

N.A.

(vi) for programs of urban development especially small labor intensive enterprises, marketing systems, and financial or other institutions to help urban poor participate in economic and social development.

The purpose of the project is to institutionalize through new policy and operational initiatives, a self sustaining credit and technical assistance program for small urban enterprises in slum areas.

c. [107] is appropriate effort placed on use of appropriate technology? (relatively smaller, cost-saving, labor using technologies that are generally most appropriate for the small farms, small businesses, and small incomes of the poor).

Yes

d. FAA Sec. 110(a). Will the recipient country provide at least 25% of the costs of the program, project, or activity with respect to which the assistance is to be furnished (or has the latter cost-sharing requirement been waived for a "relatively least developed" country)?

Yes

e. FAA Sec. 110(b). Will grant capital assistance be disbursed for project over more than 3 years? If so, has justification satisfactory to Congress been made, and efforts for other financing, or is the recipient country "relatively least developed"?

N.A.

f. FAA Sec. 281(b). Describe extent to which program recognizes the particular needs, desires, and capacities of the people of the country; utilizes the country's intellectual resources to encourage institutional development; and supports civil education and training in skills required for effective participation in governmental processes essential to self-government.

The project will assist in meeting the needs of the urban poor by creating opportunities for employment and increasing incomes through the provision of credit to small business enterprises located in urban slums. Peru's intellectual resources will be utilized to assist in the institutionalization of a self sustaining system for delivering credit and technical assistance to small business

in urban slums. The project will not directly support civil education and training in skills required for participation in processes essential to self-government.

g. FAA Sec. 122(b). Does the activity give reasonable promise of contributing to the development of economic resources, or to the increase of productive capacities and self-sustaining economic growth?

Yes

2. Development Assistance Project Criteria (Loans Only)

a. FAA Sec. 122(b). Information and conclusion on capacity of the country to repay the loan, at a reasonable rate of interest.

Peru now has the capacity to repay the loan and there is no reason to expect that in the future Peru will not be able to do so.

b. FAA Sec. 620(d). If assistance is for any productive enterprise which will compete with U.S. enterprises, 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?

N.A.

3. Project Criteria Solely for Economic Support Fund

a. FAA Sec. 531(a). Will this assistance promote economic or political stability? To the extent possible, does it reflect the policy directions of FAA Section 102?

N.A.

b. FAA Sec. 531(c). Will assistance under this chapter be used for military, or paramilitary activities?

N.A.

STANDARD ITEM CHECKLIST

A. Procurement

1. FAA Sec. 602. Are there arrangements to permit U.S. small business to participate equitably in the furnishing of commodities and services financed? Such arrangements will be included in Loan Agreement.
2. FAA Sec. 604(a). Will all procurement be from the U.S. except as otherwise determined by the President or under delegation from him? Yes.
3. FAA Sec. 604(d). If the cooperating country discriminates against U.S. marine insurance companies, will commodities be insured in the United States against marine risk with a company or companies authorized to do a marine insurance business in the U.S.? Yes
4. FAA Sec. 604(e); ISDCA of 1980 Sec. 705(a). If offshore procurement of agricultural commodity or product is to be financed, is there provision against such procurement when the domestic price of such commodity is less than parity? (Exception where commodity financed could not reasonably be procured in U.S.) N.A.
5. FAA Sec. 603. Is the shipping excluded from compliance with requirement in Section 901(b) of the Merchant Marine Act of 1936, as amended, that at least 50 per centum of the gross tonnage of commodities (computed separately for dry bulk carriers, dry cargo liners, and tankers) financed shall be transported on privately owned U.S.-flag commercial vessels to the extent that such vessels are available at fair and reasonable rates? No.
6. FAA Sec. 621. If technical assistance is financed, to the fullest extent practicable will such assistance, goods and professional and other services be furnished from private enterprise on a contract basis? If the facilities of other Federal agencies will be utilized, are they particularly suitable, not competitive with private enterprise, and made available without undue interference with domestic programs? Yes.

7. International Air Transport.
Fair Competitive Practices
Act, 1974 If air transportation of persons or property is financed on grant basis, will provision be made that U.S. carriers will be utilized to the extent such service is available? Yes.
8. Continuing Resolution Sec. 505
If the U.S. Government is a party to a contract for procurement, does the contract contain a provision authorizing termination of such contract for the convenience of the United States? Yes.
- B. Construction
1. FAA Sec. 601(d). If capital (e.g., construction) project are engineering and professional services of U.S. firms and their affiliates to be used to the maximum extent consistent with the national interests? N.A.
2. FAA Sec. 611(c). If contracts for construction are to be financed, will they be let on a competitive basis to a maximum extent practicable? Yes.
3. FAA Sec. 620(k). If for construction of productive enterprise, will aggregate value of assistance to be furnished by the U.S. not exceed \$100 million? Yes
- C. Other Restrictions
1. FAA Sec. 122(b). If development loan, is interest rate at least 2% per annum during grace period and at least 3% per annum thereafter? Yes.
2. FAA Sec. 301(d). If fund is established solely by U.S. contributions and administered by an international organization, does Comptroller General have audit rights? N.A.
3. FAA Sec. 620(h). Do arrangements exist to insure that United States foreign aid is not used in a manner which, contrary to the best interests of the United States, promotes or assists the foreign aid projects or activities of the Communist-block countries? Yes.

4. Continuing Resolution Sec. 514
If participants will be trained in the United States with funds obligated in FY 1981, has it been determined either (a) that such participants will be selected otherwise than by their home governments, or (b) that at least 20% of the FY 1981 fiscal year's funds appropriated for participant training will be for participants selected otherwise than by their home governments? N.A.
5. Will arrangements preclude use of financing:
- a. FAA Sec. 104(f). To pay for performance of abortions as a method of family planning or to, motivate or coerce persons to practice abortions; to pay for performance of involuntary sterilization as a method of family planning, or to coerce or provide financial incentive to any person to undergo sterilization? Yes.
- b. FAA Sec. 620(g) To compensate owners for expropriated nationalized property? Yes
- c. FAA Sec. 660. To provide training or advice or provide any financial support for police, prisons, or other law enforcement forces, except for narcotics programs? Yes.
- d. FAA Sec. 662. For CIA activities? Yes.
- e. FAA Sec. 636(i). For purchase, sale, long-term lease, exchange or guaranty of the sale of motor vehicles manufactured outside U.S., unless a waiver is obtained. Yes.
- f. Continuing Resolution Sec. 504. To pay pensions, annuities retirement pay, or adjusted service compensation for military personnel? Yes.
- g. Continuing Resolution Sec. 506. To pay U.N. assessments, arrearages or dues. Yes.
- h. Continuing Resolution Sec. 507: To carry out provisions of FAA section 209(d) (Transfer of FAA funds to multilateral organizations for lending.) Yes.

i. Continuing Resolution Sec. 509.

To finance the export of nuclear equipment fuel, or technology or to train foreign nationals in nuclear fields?

Yes.

j. Continuing Resolution Sec. 510

Will assistance be provided for the purpose of aiding the efforts of the government of such country to repress the legitimate rights of the population of such country contrary to the Universal Declaration of Human rights?

No.

k. Continuing Resolution Sec. 516

To be used for publicity or propaganda purposed within U.S. not authorized by Congress?

Yes.

DRAFT

PROJECT AUTHORIZATION

Name of Country: Peru
Name of Project: Urban Small Enterprises Development
Number of Project: 527-0241
Number of Loan: 527-W-

1. Pursuant to Section 106 of the Foreign Assistance of 1961, as amended, I hereby authorize the Urban Small Enterprises Development Project for Peru (the "Cooperating Country") involving planned obligations of not to exceed Ten Million United States Dollars (\$10,000,000) in loan funds ("Loan") over a four (4) year period from date of authorization, subject to the availability of funds in accordance with the A.I.D. OYB/allotment process, to help financing foreign exchange and local currency costs for the project.

2. The project ("Project") consists of the establishment and operation of a system within the Banco Industrial del Peru (BIP) for providing loans to small scale urban enterprises located in or hiring persons from the slum areas of Lima and other Peruvian cities and for mobilizing savings in these areas through the provision of capital for lending operations, technical assistance and training for BIP staff and subborrowers, and vehicles and equipment for participating BIP offices.

3. The Project Agreement, which may be negotiated and executed by the officer to whom such authority is delegated in accordance with A.I.D. regulations and Delegations of Authority, shall be subject to the following essential terms and covenants and major conditions, together with such other terms and conditions as A.I.D. may deem appropriate.

a. Interest Rate and Terms of Repayment

The Cooperating Country shall repay the Loan to A.I.D. in U.S. Dollars within twenty-five (25) years from the date of first disbursement of the Loan, including a grace period of not to exceed ten (10) years. The Cooperating Country shall pay to A.I.D. in U.S. Dollars interest from the date of first disbursement of the Loan at the rate of (i) two percent (2%) during the first ten (10) years, and (ii) three percent (3%) per annum thereafter, on the outstanding disbursed balance of the Loan and on any due and unpaid interest accrued thereon.

b. Source and Origin of Goods and Services

Goods and services, except for ocean shipping, financed by A.I.D. under the Loan shall have their source and origin in the Cooperating

Country or in countries included in A.I.D. Geographic Code 941, except as A.I.D. may otherwise agree in writing. Ocean shipping financed by A.I.D. under the Loan shall be financed only on flag vessels of the Cooperating Country or of countries included in A.I.D. Geographic Code 941, except as A.I.D. may otherwise agree in writing.

c. Conditions Precedent to Initial Disbursement

(1) Prior to any disbursement or to the issuance of commitment documents under the Project Agreement, the Cooperating Country shall, except as A.I.D. may otherwise agree in writing, furnish to A.I.D., in form and substance satisfactory to A.I.D., a technical assistance plan for training of BIP staff in participating branch offices in the technical and promotional aspects of the program including indexation of subloans and mobilizing savings and for providing technical assistance and training to subborrowers before and during the execution of their subprojects.

d. Condition Precedent to Disbursement to Finance Lending Activities

Prior to any disbursement, or to the issuance of commitment documents under the Project Agreement, to finance lending activities under the Project, the Cooperating Country shall, except as A.I.D. may otherwise agree in writing, furnish to A.I.D., in form and substance satisfactory to A.I.D., a BIP credit operations manual for the Project.

e. Condition Precedent to Disbursement to Finance Procurement of Vehicles and Equipment for BIP Offices

Prior to any disbursement, or the issuance of commitment documents under the Project Agreement, to finance procurement of vehicles and equipment for BIP offices under the Project, the Cooperating Country shall, except as A.I.D. may otherwise agree in writing, furnish to A.I.D., in form and substance satisfactory to A.I.D. a procurement plan for purchasing vehicles and equipment for participating BIP branch offices.

g. Covenants

The Cooperating Country shall covenant, except as A.I.D. may otherwise agree in writing, that:

(1) BIP shall open and staff adequately two offices in Lima, one in the southern cone and one in the northern cone within six months of the signing of the Project Agreement;

(2) BIP shall deposit to the Urban Enterprises loan fund during the Loan repayment period all reflows of principal and interest received (less commissions and fees) from all sub-loans for

relending consistent with purpose of the Project;

(3) BIP shall maintain the value of the Urban Enterprises loan fund in an amount of soles equivalent to the dollar value of the fund upon initiation of activities, and will make annual capital contributions to the Fund to compensate for any losses in value due to uncollectable loans during the previous year; and

(4) BIP shall initiate a passbook savings campaign in its two offices in the southern and northern cones of Lima.

Marshall Brown

Acting Assistant Administrator
for Latin America and the Caribbean

Date

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

I, Malcolm Butler, the principal officer of the Agency for International Development in Peru, having taken into account, among other factors, the maintenance and utilization of projects in Peru previously financed or assisted by the United States, do hereby certify that in my judgment Peru has both the financial capability and human resources capability to effectively maintain and utilize the proposed Project: URBAN SMALL ENTERPRISE DEVELOPMENT.

3/5/82

Date

Malcolm Butler

Malcolm Butler
Director
USAID/Peru



MINISTERIO DE ECONOMIA, FINANZAS Y COMERCIO

USAID/LIMA
MAIL ROOM

5 MAR 1982

RECEIVED

ANNEX I
Exhibit D

Lima, 3 de marzo de 1982

Oficio N° 028-82/EFC-15.01

Señor
Malcolm Butler
Director - Agencia Internacional
para el Desarrollo (A.I.D.)
Avda. España N° 386
Lima.-

due date 3/15

ACTION COPY	
ACTION TAKEN:	<i>N/A</i>
DATE:	
INITIALS:	<i>EL</i>

Tengo el agrado de dirigirme a usted con el objeto de someter a su consideración una solicitud formal del Gobierno Peruano para el financiamiento del Proyecto que hemos denominado "Desarrollo de Pequeñas Empresas Urbanas," mediante un préstamo de la A.I.D. de US\$ 10'000,000 a fin de constituir, juntamente con recursos de contrapartida nacional, un fondo de crédito para satisfacer la creciente demanda por los recursos monetarios, con el objeto de financiar la creación de pequeños negocios urbanos a ser localizados en los pueblos jóvenes de Lima, Trujillo, Chimbote, Chiclayo e Ica. El Proyecto contempla como Agente de Ejecución al Banco Industrial del Perú, el cual cuenta con amplia experiencia en la administración crediticia de este tipo de programas. Se desea capitalizar la capacidad institucional del Banco Industrial del Perú, obtenida en los programas rurales de crédito, financiados básicamente por la A.I. D., con recursos de los préstamos No. 527-T-057 y No. 527-T-062.

Desearíamos que el préstamo solicitado sea a un plazo de 25 años, con un período de gracia de 10 años, con tasas de interés del 2% para el período de gracia y de 3% para los años restantes. La contrapartida nacional ascenderá a US\$ 3,500,000 para la capitalización del Fondo, más los recursos necesarios para la administración del mismo.

Aprovecho la oportunidad para expresarle los sentimientos de mi mayor consideración.

ACTION:	<i>DL</i>
Info:	<i>CA</i>
	<i>CAIF</i>
	<i>S</i>
	<i>DL</i>

Atentamente,

Manuel Ulloa Elías

DR. MANUEL ULLOA ELIAS
Ministro de Economía, Finanzas.
y Comercio

UNCLASSIFIED

ANNEX I
Exhibit F
Page 1 of 3

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U.S. ACTION AID 2
MAIL ROOM AMB DCM GHR

ACTION COPY
ACTION TAKEN: *NA*
DATE: *6/22*
INITIALS: *W*
Will date 6/22

AIDAC

ACTION: DR (FILES)

INFO: *CD*
PROG *PLA*

E.G. 12065: N/A

TAGS:

SUBJECT: URBAN ENTERPRISES PID

1. THE DAEC REVIEWED AND APPROVED SUBJECT PID ON JUNE 5, 1981. THE FOLLOWING COMMENTS AND GUIDANCE ARE OFFERED FOR PREPARATION OF THE PROJECT PAPER. THE MISSION'S REQUEST FOR PROJECT APPROVAL AUTHORITY WAS NOT APPROVED; THEREFORE PP MUST BE SUBMITTED TO AID/W FOR REVIEW.

1. ANALYSIS OF BIP POLICY AND PDR; FOLIO: CONCERN WAS EXPRESSED THAT THE JUSTIFICATION FOR THIS LOAN MAY INDICATE A FUNDAMENTAL WEAKNESS IN THE NATURE OF THE INDUSTRIAL BANK OF PERU (BIP) AS A FINANCIAL ORGANIZATION AND DEVELOPMENT BANK. ESSENTIALLY, AS PRESENTLY CONSTITUTED, BIP IS A RETAILING WINDOW OF THE CENTRAL BANK, DEPENDENT FOR ITS LENDING RESOURCES ON: A) TRANSFERS OF TAX RESOURCES FROM THE CENTRAL GOVERNMENT; B) CREDIT CREATED BY THE CENTRAL BANK; C) FOREIGN BORROWINGS (SUCH AS THIS); AND D) REFLWS WHOSE REAL VALUE IS BEING RAPIDLY ERDED BY INFLATION. THE BIP APPEARS TO COMPETE WITH THE COMMERCIAL BANKING SECTOR FOR BUSINESS, AS WELL. THE LIMITED ABILITY OF THE GOV TO GENERATE PUBLIC SECTOR SAVINGS AND COMPETING DEMANDS FOR SUCH RESOURCES ALSO GIVES BIP A LIMITED SCOPE FOR FUTURE EXPANSION. NOR IS IT CLEAR THAT BIP'S CUSTOMERS ARE BEING

- institutional analysis

SYSTEMATICALLY WEANED FROM LOW COST NON-COMMERCIAL FINANCING. THE PP SHOULD THOROUGHLY ANALYZE THE QUESTION OF THE EVOLUTION AND FUTURE OF BIP LENDING, ESPECIALLY TO SMALL AND MEDIUM ENTREPRENEURS. THE MISSION IS REQUESTED TO EXPLORE THE FEASIBILITY OF BIP'S TAPPING PRIVATE CAPITAL MARKETS OR OTHER SOURCES OF VOLUNTARY SAVINGS, CO-FINANCING WITH PRIVATE U.S. FINANCIAL INSTITUTIONS, AND OTHER MECHANISMS FOR BROADENING THE FINANCIAL BASE OF BIP IN ORDER TO ASSURE THE VIABILITY AND CONTINUATION OF THE SMALL BUSINESS FUNDS FOR BOTH URBAN AND RURAL AREAS. WE ARE INTERESTED OVER THE LONGER TERM IN USING AID RESOURCES AND POSSIBLE CO-FINANCING FROM THE U.S. PRIVATE SECTOR TO MOVE THE BIP'S PORTFOLIO MORE INTO SMALL AND MEDIUM ENTERPRISE LENDING AND OUT OF COMPETITION WITH THE COMMERCIAL BANKING SECTOR."

12/21/81

FINALLY, THE ANALYSIS OF THE EVOLUTION OF BIP STRUCTURE AND POLICY SHOULD ALSO REFER TO THE ROLE OF COMMERCIAL BANKS' SMALL/MEDIUM BUSINESS LENDING, INCLUDING EXAMINATION OF COMMERCIAL BANKS' SMALL BUSINESS PORTFOLIOS, AS A MEANS OF JUSTIFYING AID SUPPORT TO THE BIP.

2. INTEREST RATES: THE ISSUE OF POSITIVE SUBLOAN INTEREST RATES WHICH INCLUDE THE COSTS OF FUND ADMINISTRATION SHOULD BE CAREFULLY ANALYZED IN THE PP. INCLUDED IN SUCH AN ANALYSIS SHOULD BE A DESCRIPTION OF PREVAILING EFFECTIVE BANK LENDING RATES FOR BUSINESS IN OTHER SECTORS. THE PROJECT SHOULD CLEARLY ESTABLISH THAT THE RATES WILL BE SET INITIALLY AT COMMERCIAL MARKET RATES AND THAT POSITIVE INTEREST RATES WILL BE CHARGED PRIOR TO PROJECT TERMINATION. THE RATIONALE FOR SUBSIDIZED INTEREST RATES VIS A VIS OTHER FORMS OF LOAN CONCESSIONS (E.G. LONGER TERMS OR GRACE PERIODS) SHOULD ALSO BE EXPLORED AND JUSTIFIED.

3. BIP CAPABILITY TO PROVIDE TA; THE PP SHOULD FULLY ASSESS BIP'S CURRENT CAPABILITY TO PROVIDE TECHNICAL ASSISTANCE TO SUB-BORROWERS FOR SUB-PROJECT DEVELOPMENT. THE ESTABLISHMENT OF ADEQUATE BIP OUTREACH IN THE PUEBLOS JOVENES IS CRUCIAL TO PROJECT SUCCESS; THEREFORE, THE PROJECT SHOULD PROVIDE TA TO THE BIP EARLY DURING IMPLEMENTATION TO ENSURE THAT ADVISORY SERVICES WILL BE AVAILABLE TO SUB-BORROWERS. MISSION IS REFERRED TO THE APPROPRIATE TECHNOLOGY INFORMATION SERVICES PROVIDED BY THE NATIONAL TECHNICAL INFORMATION SERVICE (NTIS) AND ITS PERUVIAN CONTACT, NOVDA INGENIEROS CONSULTORES, AS A POTENTIAL SOURCE FOR INFORMATION THAT MIGHT SUPPLEMENT TA OFFERED TO BIP SMALL/MEDIUM BUSINESS LOAN APPLICANTS.

4. TRAINING: ENTREPRENEURIAL AND PRODUCTION SKILLS TRAINING NEEDS OF THE KINDS OF SMALL BUSINESSES AND EMPLOYEES OF SMALL ENTERPRISES WHICH ARE LIKELY TO PARTICIPATE IN THE

PROJECT SHOULD BE SURVEYED DURING PROJECT PREPARATION, AND APPROPRIATE TRAINING PROGRAMS BUILT INTO THE PROJECT DESIGN IF REQUIRED. SUCH AN ASSESSMENT AND TRAINING COMPONENT ARE ESSENTIAL GIVEN THE PROBABILITY THAT MANY PUEBLOS JOVENES RESIDENTS SEEKING EMPLOYMENT POSSESS PRIMARILY RURAL-BASED SKILLS. FURTHERMORE, THE BIP SHOULD ENSURE THAT ITS LOAN AGENTS ARE ADEQUATELY TRAINED TO CAREFULLY SCREEN POTENTIAL SUB-BORROWERS SO THAT SUB-PROJECT ELIGIBILITY CRITERIA (SEE BELOW) ARE MET, AND THAT ONLY LEGITIMATE AND VIABLE URBAN ENTERPRISES ARE ASSISTED.

5. ELIGIBILITY CRITERIA: THE CAPABILITY OF SMALL URBAN ENTERPRISES TO GENERATE EMPLOYMENT SHOULD BE A MAJOR FACTOR IN ESTABLISHING ELIGIBILITY CRITERIA FOR FDU FINANCING. THE MISSION SHOULD THEREFORE CAREFULLY CONSIDER APPROPRIATENESS OF THE MAXIMUM LOAN/EMPLOYMENT GENERATION RATIO OF DOLS 4,000 ESTABLISHED IN THE PID, AS WELL AS THE STIPULATION FOR A MINIMUM VALUE ADDED COEFFICIENT.

6. AVAILABILITY OF FUNDING: WHILE MISSION'S ABS ALLOCATES

UNCLASSIFIED PAGE 3 of STATE 156510

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PP RJESLM
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UNCLAS SECTION 02 OF 02 STATE 156510

ADAC

FUNDING FOR THE PROJECT IN BOTH FY 82 AND 83, AND LAC
BURFAJ'S BUDGET SUBMISSION TO PPC IS LIKELY TO REFLECT
THIS ALLOCATION, WE WOULD CONSIDER AVAILABILITY OF FUNDING
FOR THE PROJECT DOUBTFUL AT LEAST THROUGH FY 82 GIVEN
TIGHT SDA BUDGET AND COMPETING WORLDWIDE AND REGIONAL
PRIORITIES. THEREFORE, PROJECT SHOULD BE VIEWED AS A
SHELF ACTIVITY AT THIS POINT. IF ADDITIONAL PD AND S
FUNDING IS REQUIRED FOR PROJECT DEVELOPMENT TO DEAL WITH
CONCERNS EXPRESSED IN ABOVE PARAGRAPHS, IT IS UNLIKELY
THAT WE WILL BE ABLE TO MAKE SUCH FUNDING AVAILABLE IN
FY 81. STDESSEL

BT
#6510

LAC/DR-IEE-81-24

ENVIRONMENTAL THRESHOLD DECISION

Project Location : Peru

Project Title and Number : Urban Small Enterprises
527-0241

Funding : FY 1981 - \$10,000,000

Life of Project : Two years

IEE Prepared by : Edilberto Alarcon, USAID/Peru
Environmental Coordinator

Recommended Threshold Decision : Negative Determination

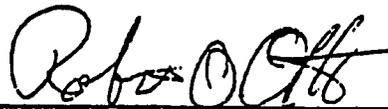
Bureau Threshold Decision : Concurrence with Mission
Recommendation

Action : Copy to Leonard Yaeger,
Director, USAID/Peru

: Copy to Edilberto Alarcon

: Copy to Norma Parker, LAC/DR/SA

: Copy to IEE file



Date 3 June 81

Robert O. Otto
Chief Environmental Officer
Bureau for Latin America
and the Caribbean

INITIAL ENVIRONMENTAL EXAMINATION

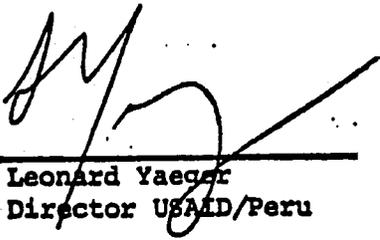
Project Location : Peru
Project Title : Urban Small Enterprises
Funding : FY ~ 1981 \$ 10,000,000
Life of Project :
IEE Prepared by : Edilberto Alarcón, USAID/Peru
Environmental Coordinator
Date Prepared : May 1981

Environmental Action Recommended:

The USAID/Peru Project Committee has undertaken a complete Initial Environmental Examination (IEE) of the project's environmental impacts and has arrived at a recommendation for a Negative Determination as indicated in the Threshold Decision Section of the IEE.

Concurrence:

I have reviewed the Initial Environmental Examination for the Rural Enterprises II Program and concur in the recommendation for a Negative Determination.



Leonard Yaeger
Director USAID/Peru

INITIAL ENVIRONMENTAL EXAMINATION

URBAN SMALL ENTERPRISE LOAN

I. PROJECT DESCRIPTION

1. General:

The goal of the Project is to generate and increase urban incomes in Peru. The purpose of the Project is to institutionalize a program which will develop and expand urban small enterprises by improving the access of such firms to credit, appropriate technologies, and technical assistance, thereby increasing urban employment opportunities.

It is envisioned that the Project will be implemented in the Pueblos Jovenes of Lima and seven other major coastal cities. The Project activities will contribute to:

- development and strengthening of urban enterprises;
- generation of new employment opportunities;
- generation and improved distribution of income; and
- increased and self sustaining levels of economic activity which will interalia, reduce investment risk, provide a business infrastructure conducive to attracting larger scale industrial investment to the region, support agricultural development and improve general quality of life making the urban area a more attractive place to live.

Project implementation will include the development of a revolving urban credit fund, urban enterprise promotion, expanded technical assistance capacity, greater outreach capability, further reduction in credit barriers, and the institutionalization of urban small enterprise development lending concepts within the BIP. Nearly all of the A.I.D. loan will be used to capitalize the urban credit fund with a small portion of A.I.D. money set aside to provide technical assistance and commodities to the BIP. The BIP will provide counterpart funding to capitalize the urban credit fund as well as implement the program and provide technical assistance to sub-borrowers.

The total cost of the proposed three-year Project is estimated at \$14.0 million of which \$4.0 will be provided as counterpart contribution by the GOP, and \$10.0 will be loan funded by A.I.D.

The BIP will be the Project's implementing institution. The Urban Development Fund Office will have direct responsibility for Project implementation and will coordinate the activities of the Lima Offices' technical and managerial divisions. The regional branch

offices will be the focus of Project promotion, sub-project analysis, technical assistance, sub-loan approval (within their authorized limits) and individual sub-loan monitoring.

The major beneficiaries of this Project are the estimated 3 millions inhabitants of pueblos juvenes in the Project area who have little or not access to credit. Given experience under the Rural Enterprise I and II loans, the Mission estimates that approximately 2,800 sub-borrowers will obtain credit and 14,000 new jobs will be created during the implementation period.

2. Eligible Enterprises Classification

Existing or proposed enterprises eligible to receive financing from the fund will be from the following basic categories:

- cottage industries (including artisan)
- small-scale industry/manufacturing
- services/commerce
- small-scale agribusiness

II. DISCUSSION OF IMPACTS:

This is an Intermediate Credit Institution Loan which will provide sub-loans of an average amount of \$5,000 to selected urban enterprises through the Industrial Bank of Peru. Most of the sub-loans will support cottage and small scale manufacturing industries. Some will be related to services and commerce and some to small scale agribusiness. In view of the relatively small size of the sub-loans, no significant environmental changes are expected from any individual project. However, the Program as a whole will improve socio economic conditions through employment generation and increased production of goods and services.

In the following paragraphs, a brief discussion is presented on the minor environmental effects that may result from the anticipated project activities.

A. Land Use:

The Program activities will not produce any major changes in the character of the land. Land clearing and extraction of natural resources will be reduced to a minimum. Since the Loan will not finance any major infrastructure work, there will be no danger of altering natural defenses, foreclosing any important land uses or jeopardizing man or his works.

B. Water Quality:

None of the anticipated Program activities will make an extensive use of water. This precludes any impacts on the ecological balance or the physical state of water. On the other hand, the nature and size of the small industry which is likely to be financed under the Loan introduces very little possibilities of originating pollution or changes in the chemical and biological states.

C. Atmospheric Impacts:

Since no major industrial activities will be financed under the Loan, there will be no significant atmospheric impacts. Nevertheless, some minor air and noise pollution may result from certain activities or from enterprises using small gas or diesel equipment units.

D. Natural Resources:

Expenditure of natural resources will be minimal due to the anticipated small volume of operations. Their extraction will not endanger the natural resource base.

E. Cultural Impacts:

Improved living conditions will bring about a positive effect in the cultural level of the families benefited by the Program. No alteration of physical symbols nor dilution of cultural traditions are anticipated.

F. Socio-economic Impacts:

The most significant positive impacts of the Program will be on the socio-economic field. Expansion of existing enterprises and establishment of new ones, will create approximately 14,000 new jobs. Many of the beneficiaries will have the opportunity to build capital investments and become self employed. Artisans and small town specialists such as shoemakers, blacksmiths and carpenters will make better and more productive use of their skills. Additional income will improve their living conditions and their cultural patterns.

The Program will also have a positive effect on the overall economy of the areas where the small enterprises are located. The capital generated by the production activities will generally be spent locally and will in turn generate additional economic activities.

G. Health Impacts:

Although no direct health impacts will result from the Program activities, it is expected that the improvement of living conditions will have positive side effects in creating an environment conducive to improved health conditions.

III. RECOMMENDATION FOR ENVIRONMENTAL ACTION:

The nature and scope of this Intermediate Credit Institution Program has been thoroughly considered in the light of the established criteria for conducting an Initial Environmental Examination. The conclusion is that the Program will have very favorable socio-economic impacts with little if any potential negative impact on the environment.

THRESHOLD DECISION: For the reasons cited above, the Mission believes that no further study is necessary and therefore recommends a NEGATIVE DETERMINATION.

IMPACT IDENTIFICATION AND EVALUATION FORM

ANNEX I
 Exhibit G
 Page 7 of 9
 Impact
 Identification
 and
 Evaluation 2/

Impact Areas and Sub-areas 1/

A. LAND USE

1. Changing the character of the land through:

- a. Increasing the population _____ N
- b. Extracting natural resources _____ L
- c. Land clearing _____ N
- d. Changing soil character _____ N

2. Altering natural defenses _____ N

3. Forclosing important uses _____ N

4. Jeopardizing man or his works _____ N

5. Other factors _____

B. WATER QUALITY

1. Physical state of water _____ N

2. Chemical and biological states _____ N

3. Ecological balance _____

4. Other factors _____

1/ See Explanatory Notes for this form.

2/ Use the following symbols: N - No environmental impact
 L - Little environmental impact
 M - Moderate environmental impact
 H - High environmental impact
 U - Unknown environmental impact

IMPACT IDENTIFICATION AND EVALUATION FORM

C. ATMOSPHERIC

1. Air additives _____
2. Air pollution _____
3. Noise pollution _____
4. Other factors _____

N

L

L

D. NATURAL RESOURCES

1. Diversion, altered use of water _____
2. Irreversible, inefficient commitments _____
3. Other factors _____

N

N

E. CULTURAL

1. Altering physical symbols _____
2. Dilution of cultural traditions _____
3. Other factors _____

N

N

F. SOCIOECONOMIC

1. Changes in economic/employment patterns _____
2. Changes in population _____
3. Changes in cultural patterns _____
4. Other factors _____

N

N

N

IMPACT IDENTIFICATION AND EVALUATION FORM

G. HEALTH

- | | | | |
|-------------------------------------|-------|-------|---|
| 1. Changing a natural environment | _____ | _____ | N |
| 2. Eliminating an ecosystem element | _____ | _____ | N |
| 3. Other factors | _____ | _____ | |
| | _____ | _____ | |
| | _____ | _____ | |

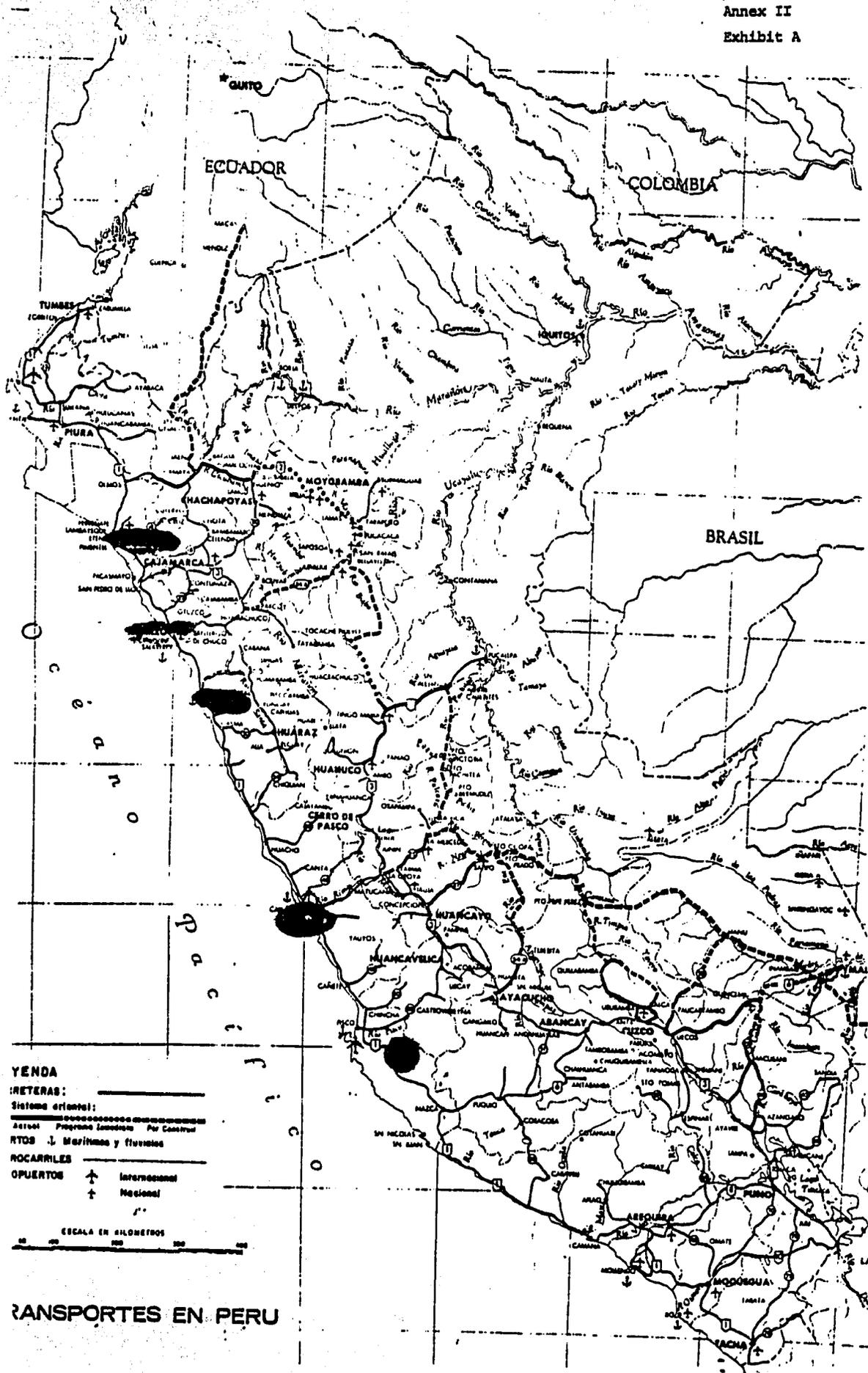
H. GENERAL

- | | | | |
|---------------------------|-------|-------|---|
| 1. International impacts | _____ | _____ | N |
| 2. Controversial impacts | _____ | _____ | N |
| 3. Larger program impacts | _____ | _____ | N |
| 4. Other factors | _____ | _____ | |
| | _____ | _____ | |
| | _____ | _____ | |

I. OTHER POSSIBLE IMPACTS (not listed above)

- | | | | |
|-------|-------|-------|--|
| _____ | _____ | _____ | |
| _____ | _____ | _____ | |
| _____ | _____ | _____ | |

See attached Discussion of Impacts



TRANSPORTES EN PERU

EXECUTIVE SUMMARY

EVALUATION FINDINGS

The Rural Development Fund Program of the Industrial Bank of Peru (IBIP) funded by the Government of Peru and USAID, has had considerable positive impact since its inception in 1975. It has fostered income generation, created employment opportunities and contributed to economic development in the sierra and high jungle departments serviced by bank branches. The small enterprise lending program deserves further support and expansion.

Small enterprise lending has now been institutionalized within the BIP. Such loans grew from 3.4% to over 50% of all new loans extended in 1975 and the first nine months of 1981 respectively. Although delinquency rates are relatively low, negative interest rates caused the complete decapitalization of the Fund by 1981.

The FDR was a key factor simulating the decentralization of authority to branch offices since increased branch approval authority was a condition precedent set by AID.

Loans are well diversified geographically with none of the 19 participating branches accounting for over 16.5% of total lending in 1980. Sixty percent of loans disbursed from 1978-81 were less than about \$2600 and only ten percent were over \$12,400, indicating that the bank is fulfilling its objective of serving as a source of smaller loans despite temptations to make fewer, larger loans.

DAI sample survey results of 85 entrepreneurs interviewed in four FDR branches indicates that, on average, between the time of the first FDR loan and the present:

- o sales increased overall by 160% or 28% per year,
- o gross income increased by \$16,000,
- o net income grew by over 50% per year,
- o total assets increased by 260%, or 72% per year,
- o net worth almost quadrupled, representing a yearly increase of over 56%,

- o level of indebtedness fell from 2.39 to .49

In addition:

- o the average payback period per FDR loan was three and one half years in terms of economic value added,
- o loan repayments represented 31% of total net income before interest costs at current prevailing interest rates,
- o current return on sales was 29% for industrial, artisan commercial and agricultural firms while service enterprises showed a healthy 43% return.

Extrapolations from these surveyed results indicate that total loan funds disbursed since program inception have helped to generate each year about

- o \$60 million in net profits and salaries to owners,
- o \$19 million in income to new employees,
- o \$50 million in sales to Peruvian suppliers.

Each dollar of loan funds, thus, has contributed to about \$3.00 in estimated new income.

Approximately \$7,000 of loan funds helped to generate one additional full time job; thus the entire program has helped to create about 6150 jobs. On average, about \$2700 of loans funds helped to sustain jobs existing at time of first loan disbursement or create new jobs. Thus, approximately 15,700 jobs have been sustained or created.

RECOMMENDATIONS:

Some suggestions to improve the small enterprise lending program further are:

- o to computerize branches to free staff from tedious paperwork and improve the bank's management information system,
- o to improve the current filing systems within branches,
- o to report on the sources and applications of FDR funds in soles on an annual basis to AID,
- o to include information on actual sales, gross and net profits and employment at time of loan application within feasibility studies.
- o to update the credit manual so that it may serve a useful management function,
- o to require each branch to report on total number of loans disbursed, delinquencies and defaults with an aging of overdue accounts on an annual basis,
- o to create an automatic mechanism by which loans may retain their real value if processing time remains an average of three months or streamline current disbursement policies,
- o to select a higher proportion of field staff for future overseas training courses,
- o to charge branches for the cost of funds and services provided by the central branch, but not penalize unprofitable branches,
- o to clarify to sub-borrowers that interest rates may change automatically with an estimate of the potential increase during loan period,
- o to increase efforts to capture the business of FDR clients who have graduated to commercial loan level,
- o to expand technical assistance to sub-borrowers but charge a subsidized for such services.

Capital para sus proyectos

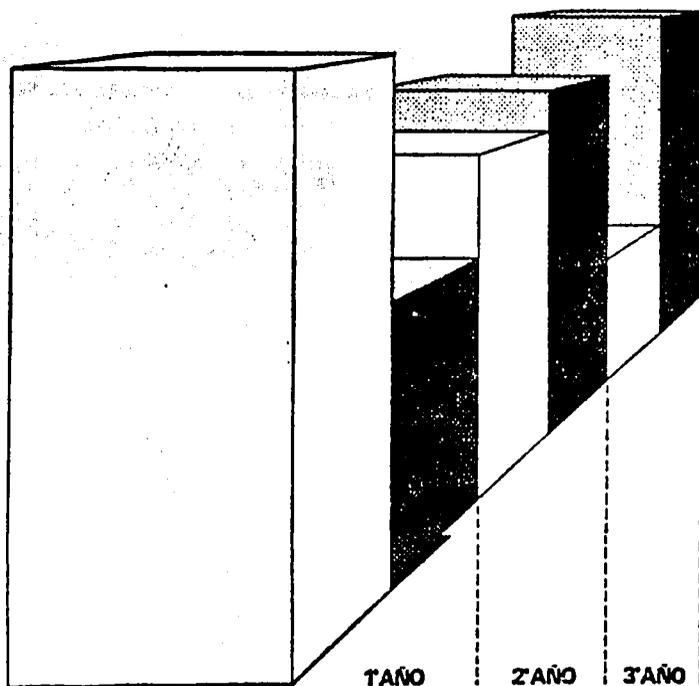
Annex II

Exhibit D
Page 1 of 1

Tenemos una nueva alternativa financiera

Dos modalidades de amortización

FINANCIACION CONVENCIONAL 
FINANCIACION CON REAJUSTE DE DEUDA 



Financiera de Crédito le asegura que, con el financiamiento convencional o con el reajuste de deudas, el costo del dinero será el mismo, lo que varía es la oportunidad y los montos correspondientes a los intereses. Para mayor seguridad de que una modalidad de financiamiento no resulte más cara que la otra, siempre será posible optar por el sistema más conveniente en el curso de la operación.

- Hasta ahora, su empresa estaba limitada a las modalidades tradicionales de financiamiento, no siempre convenientes para usted.
- Desde hoy, Financiera de Crédito le da la oportunidad de escoger. Para que su programa de amortizaciones se ajuste a su flujo de caja. Y no a la inversa.
- Así, en un proyecto de maduración rápida puede convenirle una financiación convencional, en la que los pagos de intereses se reducen progresivamente.
- Pero si su proyecto requiere inicialmente de más recursos o si su empresa necesita de capital de trabajo permanente, le interesará el nuevo sistema de Reajuste de Deudas que proporciona mayor liquidez inicial.
- Financiera de Crédito le puede brindar ahora y sin demora ambas alternativas. Por algo somos la Financiera que más recursos ha captado y más crédito ha otorgado en 1981 y siempre con rapidez profesional.
- Consúltenos cuanto antes en nuestras oficinas de Jirón Huallaga 320, tercer Piso, Lima, o en cualquier sucursal del Banco de Crédito.

Comercio

LIMA, LUNES 11 DE ENERO DE 1982

FINANCIERA DE CREDITO

La Financiera

**Capital para sus proyectos
en una nueva alternativa Financiera.**

ANNEX II
Exhibit D
Page 2 of 3

Damos más liquidez a su empresa cuando más lo necesita

Ejemplo: las primeras amortizaciones de un crédito de 50'000,000

SISTEMA CONVENCIONAL DE FINANCIACION

Préstamo Neto	1° Trimestre	2° Trimestre	3° Trimestre	4° Trimestre *
S/. 42'875,	S/. 7'125,	S/. 7'125,	S/. 7'125,	S/. 11'889,

Con el nuevo sistema de reajuste de deuda, la liquidez de su empresa crece enormemente en el período inicial de amortización. Nuestras cuotas cuatrimestrales (cada 120 días) son menores que las cuotas trimestrales (cada 90 días) de la financiación convencional. En términos globales, sin embargo, el costo del dinero resulta igual en cualquiera de los dos sistemas. Y se lo asegura la Financiera de Crédito.

FINANCIACION CON REAJUSTE DE DEUDA

Préstamo Neto	1° Cuatrimestre	2° Cuatrimestre	3° Cuatrimestre *
S/. 45'750,	S/. 4'747,	S/. 5'302,	S/. 15'031,

Mayor liquidez para el prestatario S/. 11'059,

*Incluyen las primeras amortizaciones de capital.

- Si su empresa requiere inicialmente el máximo posible de capital piense en Financiera de Crédito.
- Financiera de Crédito ha reducido sustancialmente las amortizaciones de sus clientes en el período inicial del crédito, a la vez que ha incrementado el monto neto de los préstamos.
- Financiera de Crédito puede apoyar a su empresa ahora y sin demora. Por algo somos la Financiera que más recursos ha captado y más crédito ha otorgado en 1981, y siempre con rapidez profesional.
- Financiera de Crédito le da la opción de escoger ahora entre la modalidad convencional de financiación y el sistema de Reajuste de Deudas promulgado por la Ley 23327
- Consúltenos cuanto antes en nuestras oficinas de Jirón Huallaga 320, tercer piso, o en cualquier sucursal del Banco de Crédito

**FINANCIERA
DE CREDITO**

La Financiera

BANCO INDUSTRIAL

ANNEX II
Exhibit D
Page 3 of 3

**Paga los más altos
intereses del mercado
por certificados
de depósito**

55%

El Banco Industrial
le da ahora el 55% anual
por certificados de depósito
y le paga sus intereses trimestralmente.
Si usted reinvierte sus intereses obtiene una
rentabilidad anual del 67.42%.
Los certificados de depósito ofrecen el interés más
alto del mercado financiero y están libres del impuesto a
la renta.

Visítenos en Jr. Lampa 535 y en todas las sucursales del Perú.

Una mano para la mano que trabaja

DIARIO OFICIAL

El Peruano

NORMAS LEGALES

"AÑO BICENTENARIO DE LA REBELION EMANCIPADORA
DE TUPAC AMARU Y MICHAELA BASTIDAS"

Lima, Miércoles 25 de Noviembre de 1981

Director: Jesús Mimbela Pérez

AÑO. I — No. 344

LEY

AMPLIAN ARTICULOS, MODIFICAN
INCISOS Y SUSTITUYEN PARRAFO
DEL CODIGO CIVIL, LEY DE TITU-
LOS VALORES, LEY DE SOCIEDA-
DES MERCANTILES Y DEL CODIGO
DE COMERCIO

LEY Nº 23237

EL PRESIDENTE DE LA REPUBLICA

POR CUANTO:

El Congreso ha dado la ley siguiente:

El Congreso de la República del Perú:

Ha dado la Ley siguiente:

Artículo 1º.— Ampliase el Artículo 1573º del Código Civil, con el siguiente párrafo:

"Tratándose de préstamos de dinero a plazo no menor de un año, las partes podrán convenir, por escrito, que el importe dado en mutuo y sus saldos, se reajusten con el índice correspondiente, conforme a lo previsto en el Artículo 1581º."

Artículo 2º.— Ampliase el Artículo 1581º del Código Civil, con el siguiente texto:

"Las partes podrán convenir, por escrito, que el pago de deudas provenientes de préstamos de dinero en moneda nacional, a plazo no menor de un año, sea referido al índice de reajuste de deudas correspondientes que fije el Banco Central de Reserva del Perú para las clases de operaciones que esta determine.

El pago de las deudas a que se refiere el párrafo anterior se efectuará en moneda nacional, en monto equivalente al valor de referencia, al día del vencimiento de la obligación.

Si el deudor retardara el pago, el acreedor podrá exigir, a su elección, que la deuda sea pagada al valor de referencia del día del vencimiento de la obligación o del día en que se efectuó el pago."

Artículo 3º.— Modifícase el inciso 2) del Artículo 1013º del Código Civil, el cual tendrá el siguiente texto:

"2) Que el gravamen sea de cantidad determinada o determinable en los casos de reajuste de capital legalmente admitidos y que se inscriba en el Registro de la Propiedad Inmueble."

Artículo 4º.— Modifícanse los incisos 2) y 3) de los Artículos 61º y 129º respectivamente, de la Ley de Títulos Valores, los cuales tendrán el siguiente texto:

"2) La orden incondicional de pagar una cantidad de dinero determinada o determinable en los casos de reajuste de capital legalmente admitidos."

"3) La promesa pura y simple de pagar una cantidad de dinero determinada o determinable en los casos de reajuste de capital legalmente admitidos."

Artículo 5º.— Modifícase el inciso 3) del Artículo 232º de la Ley de Sociedades Mercantiles, el cual tendrá el siguiente texto:

"El valor nominal, intereses, vencimiento, primas si las hubiera, y el modo y lugar de pago,

Podrá expresarse, asimismo, indicación de reajuste del valor nominal en aplicación del sistema previsto para los préstamos de dinero en el segundo párrafo del Artículo 1573º del Código Civil."

Artículo 6º.— Sustitúyase el primer párrafo del Artículo 307º del Código de Comercio, el cual tendrá el siguiente texto:

"Los préstamos en moneda nacional serán pagados por el deudor en la misma moneda, y salvo que las partes acuerden por escrito lo contrario, de conformidad con lo dispuesto en el segundo párrafo del Artículo 1573º del Código Civil, en cantidad igual a la recibida.

Lima, Miércoles 25 de Noviembre de 1981

En los que hubieren sido concertados en moneda extranjera, el pago podrá hacerse en moneda nacional al tipo de cambio de venta del día y lugar del vencimiento de la obligación.

Si el deudor, en el caso previsto en el párrafo anterior, retardare el pago, el acreedor podrá exigir a su elección, que la deuda sea pagada en moneda nacional, según el tipo de cambio de venta de la fecha de vencimiento de la obligación o el que rija el día del pago."

Artículo 7º.— Para fines tributarios, el monto del reajuste de capital se considerará como ingreso neto o gasto deducible, según corresponda.

El reajuste de capital, para gozar de la exoneración del impuesto a la renta, requerirá que la ley expresamente así lo establezca.

Sin perjuicio de lo dispuesto en el párrafo anterior, en caso que la legislación vigente a la fecha de dación de la presente ley, prevea la exoneración del impuesto a la renta por los intereses generados en operaciones de crédito, dicha exoneración también alcanzará al reajuste de capital que se efectúe en aplicación de este dispositivo legal.

Artículo 8º.— Facúltase al Banco Central de Reserva del Perú para que, periódicamente, establezca un índice conforme al cual sea factible convertir el monto del saldo principal de los créditos concertados o que se concerta a plazo mayor de un año, así como de los compromisos cuando el plazo que resta para su expiración fuese no menor del indicado.

Artículo 9º.— La presente ley entrará en vigencia el día siguiente de su publicación en el diario Oficial "El Peruano".

DISPOSICION TRANSITORIA

Las operaciones celebradas al amparo del Decreto Supremo N° 136—81—EF del 26 de Junio de 1981, modificado por el Decreto Supremo No. 150—EF del 3 de Julio de 1981, quedarán convalidadas. A los efectos de la convalidación señalada en el párrafo anterior les serán aplicables las disposiciones de la presente ley.

DISPOSICION FINAL

Deróganse todas las disposiciones legales que se opongan a la presente Ley.
Comuníquese al Presidente de la República para su promulgación.

Que, del Congreso, en Lima, a los veintidós días del mes de Noviembre de mil novecientos ochenta y uno.

JAVIER ALVA ORLANDINI, Presidente del Senado.
LUIS PEROVICH ROCA, Presidente de la Cámara de Diputados.
MARIO BERRANO SOLIS, Senador Secretario.
FRIDA OSORIO DE RICALDE, Diputado Secretario.

Al señor Presidente Constitucional de la República.

POR TANTO:

Mando se publique y cumpla

Dado en la Casa de Gobierno, en Lima, a los veinticuatro días del mes de Noviembre de mil novecientos ochenta y uno.

FERNANDO BELAUNDE TERRY, Presidente Constitucional de la República.

MANUEL ULLOA ELIAS, Presidente del Consejo de Ministros y Ministro de Economía, Finanzas y Comercio.

**PRESIDENCIA DE
CONSEJO DE MINISTROS**

DECLARAN INADMISIBLE ACCION DE AMPARO DE LA EMPRESA DE TRANSPORTES DE SERVICIO URBANO "CONDORCUNCA" S. R. L."

RESOLUCION MINISTERIAL N° 0153-81-FC

Lima, 24 de Noviembre de 1981.

Visto, el recurso del Presidente de la Empresa de Transportes de Servicio Urbano Condorcunca S.R.L., interponiendo Acción de Amparo contra los actos administrativos del Director General y el Jefe de Circulación Vial de Transportes y Comunicaciones de Ayacucho, dependientes del ORDE AYACUCHO;

CONSIDERANDO:

Que, la Constitución del Estado en su Art. 205º, párrafo segundo, establece que la Acción de Amparo cautela los derechos constitucionales distintos de la Libertad Individual, cautelada por la Acción de Habeas Corpus;

Que, el Decreto Ley 17083, en sus Arts. 1º y 2º señala el procedimiento aplicable a la Acción de Amparo, conforme se expone en el considerando precedente y que deberá seguirse ante el Poder Judicial;

De conformidad con lo opinado por la Dirección General de Asuntos Jurídicos.

SE RESUELVE:

Artículo Único.— Declárese Inadmisible la Acción de Amparo de la Empresa de Transportes de Servicio Urbano Condorcunca S.R.L., contra los actos administrativos del Director Regional y Jefe de Circulación Vial de Transportes y Comunicaciones.

GERENCIA

US.
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R L

SYSTEM

Señor
Malcolm Butter
Director
Agencia para el Desarrollo Internacional
PRESENTE

De nuestra consideración :

Nos es grato dirigirnos a usted, para presentarle el proyecto de aplicación de US\$300,000, con cargo a la partida de Asistencia Técnica del Convenio 527-T-062, que detallamos a continuación para la consiguiente aprobación :

Miles de Soles

Dólares *

1. Adiestramiento interno

Cursillos de capacitación para el personal del BIP, preferentemente para los que operan en zonas donde se aplica el Fondo de Desarrollo Rural.

Contadores

Se estudiará el nuevo plan de cuentas y su aplicación (60 personas 7 de Sucursales y 40 de Lima) una semana.

Analistas de Crédito

Se actualizará sus conocimientos sobre evaluación de proyectos de inversión (40 personas de Sucursales y 10 de Lima) una semana.

ACTION:	AR	file
date:	CA	
	A	
	AA	

8'500

18,900

4'160

9,250

Abogados

Nuevos criterios para agilizar la tramitación legal de los créditos concedidos (30 personas de Sucursales y 10 de Lima) una semana.

3'400,

7,600

2. Programa de Becas

Para administradores y otros funcionarios de Sucursales, al extranjero, para apreciar programas de asistencia financiera y no financiera a favor de la Pequeña Empresa en otros países. (10 personas por un mes cada una).

13'500

30,000

3. Campanas de Divulgación

Publicidad, asesoría en organización de ferias regionales, conferencias y charlas en Pucallpa, San Ramón, Jaén, Huaráz, Cuzco, Puno e Ica

6'150

13,700

4. Asistencia Técnica

Programa de capacitación a favor de prestatarios metal mecánicos, zapateros y otros de Huancayo, Huarás, Ica y Cusco, en colaboración con SENATI (500 pequeños prestatarios).

12'200

27,200

Programa de capacitación para el aprovechamiento de frutas, a realizarse en los valles de Sierra Central y Sur.

12'200

27,200

5. Programas Especiales

Llave en Mano

Estudios de factibilidad, promoción y asistencia técnica a favor de los nuevos empresarios que participen con su inversión y su curso en la implementación de pro

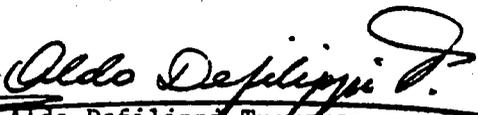
yectos a base de perfiles elab/ borados por el Banco y puestos a disposición de los promotores	45'000	100,000
--	--------	---------

Organización del Centro de Aprendizaje Artesanal

Aporte del BIP para formar un Patronato para la formación de un centro de aprendizaje en coordinación con el MITI, FOPEX y Artesanías del Perú.	29'890	66,150
---	--------	--------

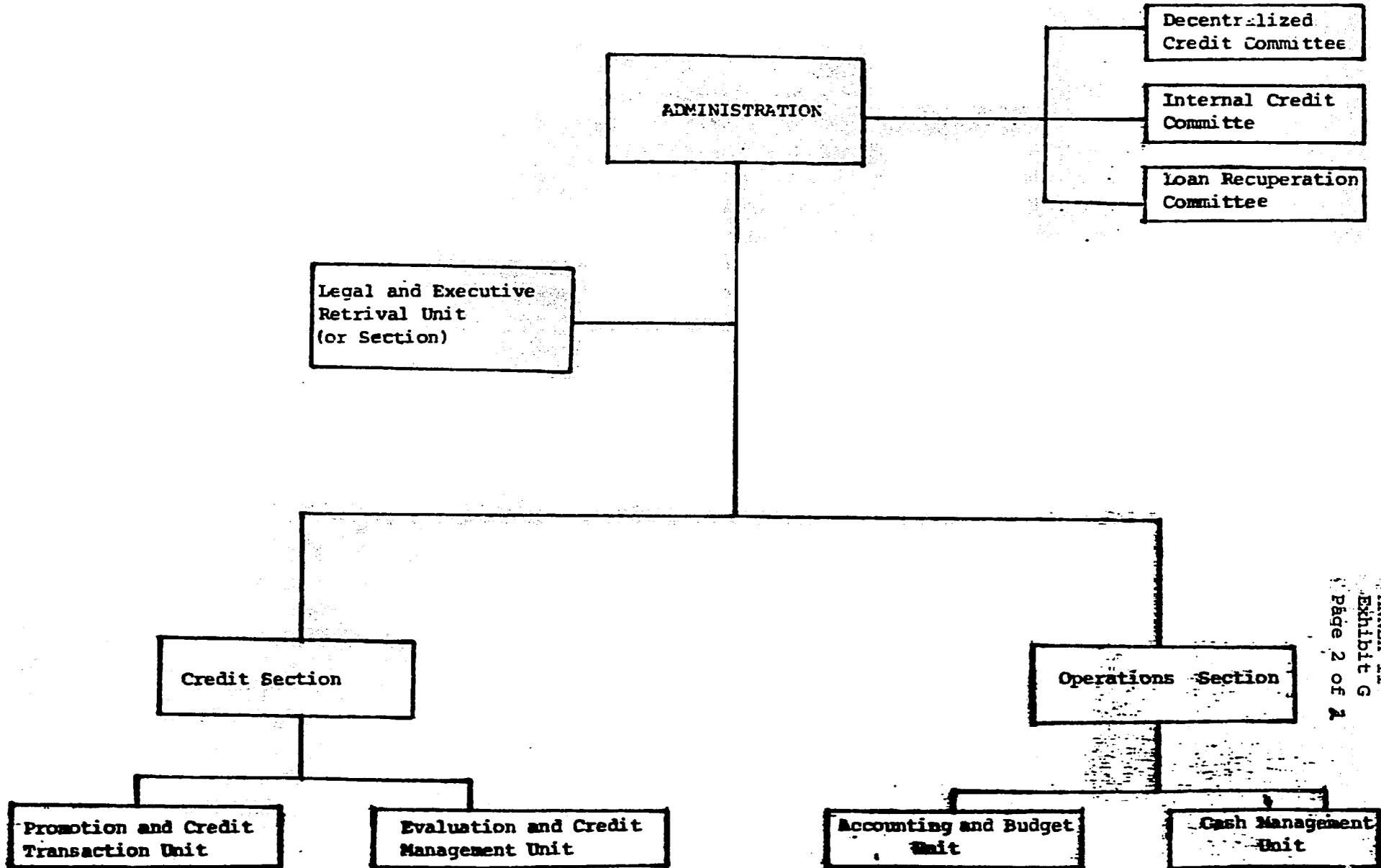
Hacemos propicia la oportunidad, para reiterar a usted los sentimientos de nuestra consideración.

Atentamente,


Aldo Defilippi Traverso
Gerente Financiero

ADT/888.

CHART 1
INDUSTRIAL BANK OF PERU
Branch Organizational Chart



INSTITUTIONAL BREAKDOWN OF THE PERUVIAN FINANCIAL SYSTEM
Situation as of 12/31/80

	Number of Institutions	Number of Offices	Total Assets Million US\$ (1)	
A. <u>Central System</u>				
Central Bank	1	6	4,361.8	28.5
Banco de la Nación	1	456	2,780.9	18.2
B. <u>Development Banks</u>	5	162	1,708.7	11.2
of which Industrial (BIP)	1	21	413.5	2.7
Housing	2	47	781.9	5.1
Agricultural	1	79	377.1	2.5
Mining	1	15	136.2	0.9
C. <u>Commercial Banks</u>	21	803	4,532.3	29.5
o/w Private	4	330	1,963.5	12.8
State	3	347	1,776.2	11.6
Foreign	4	11	164.2	1.1
Regional	6	82	440.8	2.9
Construction & Savings Banks	4	34	187.6	1.2
D. <u>Non-Banking System</u>	49	215	1,924.6	12.6
o/w COFIDE	1	6	839.2	5.5
Insurance companies	22	101	441.5	2.9
Savings & Loan	16	95	255.1	1.7
Financieras	10	13	299.9	2.0
Other	h.a.	h.a.	88.9	0.5
TOTAL	77	1,643	15,308.3	100.0

(1) Conversion Rate: 342.61 Soles per US\$

Source: Superintendent of Banks and Insurance Companies Bulletin

BIP - COMPARATIVE BALANCE SHEETS - 1978/1980

(in US\$,000 equivalent)

	12/31/1978		12/31/1979		12/31/1980	
	US \$,000	%	US \$,000	%	US \$,000	%
ASSETS						
Cash (incl. Banks)	8,743	3.3	20,269	6.2	19,282	5.9
Total loans	254,670		280,083		282,619	
(-) Provisions	(22,220)		(20,368)		(14,907)	
Net loans	232,450	89.2	259,715	79.0	267,712	81.4
Investments	2,025	0.8	6,492	2.0	14,703	4.5
Fixed assets	1,346	0.5	4,464	1.3	5,613	1.7
Other assets	16,094	6.2	37,735	11.5	21,226	6.5
Total assets	260,658	100.0	328,675	100.0	328,536	100.0
LIABILITIES						
Current liabilities	17,451	6.7	17,343	5.3	18,732	5.8
Correspondent banks	59,436	22.8	61,278	18.6	78,934	24.0
Central Bank of Peru	115,665	44.4	123,015	37.4	109,442	33.3
Banco de la Nación	22,070	8.5	18,191	5.5	16,988	5.2
Other liabilities	15,508	5.9	61,440	18.7	28,019	8.5
Provisions and Deferred Income	2,995	1.1	1,804	0.6	753	0.2
Total liabilities	233,125	89.4	283,071	86.1	252,868	77.0
Shareholder's Equity	27,533	10.6	45,604	13.9	75,668	23.0
Total liabilities and net worth	260,658	100.0	328,675	100.0	328,536	100.0
Conversion Rate (soles per \$)	196.68		250.75		342.61	

BIP - COMPARATIVE INCOME STATEMENTS - 1978/1980

	1/1 to 12/31/1978		1/1 to 12/31/1979		1/1 to 12/31/1980		1/1 to 9/30/1981 (9 months unaudited)	
	US \$,000	% (1)	US \$,000	% (1)	US \$,000	% (1)	US\$,000	% (1)
Interest and Commissions on loans	27,624	75.4	44,920	87.5	52,774	80.3	57,503	93.6
(-) Interest and Commissions paid	(20,287)	(55.4)	(35,802)	(69.7)	(33,644)	(51.2)	(38,549)	(62.8)
Net interest & commission income	7,337	20.0	9,118	17.8	19,130	29.1	18,954	30.8
Income from investment	584	1.6	420	0.8	812	1.3	3,905	6.4
Fees from banking services	1,456	4.0	1,034	2.0	1,372	2.1		
Income from foreign exchange	5,237	14.3	-	-	1,850	2.8		
Other Income	1,743	4.7	4,999	9.7	8,890	13.5		
Total income from banking activities	16,357	44.6	15,571	30.3	32,054	48.8	22,859	37.2
Salaries	4,756	13.0	5,285	10.3	8,543	13.0	8,868	14.4
General expenses	1,664	4.6	5,183	10.1	2,967	4.5	2,586	4.2
Provisions on investment and loan portfolio	8,698	23.7	2,882	5.6	15,032	22.9	8,227	13.4
Taxes and other	164	0.4	23	0.0	2,379	3.6	1,171	1.9
(-) Total expenses	(15,282)	(41.7)	(13,373)	(26.0)	(28,921)	(44.0)	20,852	(33.9)
Pre tax income	1,075	2.9	2,198	4.3	3,133	4.8	2,007	3.3
(-) Income taxes	(165)	(0.4)	(1,116)	(2.2)	(1,566)	(2.4)	968	1.6
Net Income	910	2.5	1,082	2.1	1,567	2.4	1,039	1.7
Conversion (soles per \$)	196.68		250.75		342.61		453.29	

(1) Percent of total income

BIP - STATEMENT OF SOURCES AND APPLICATION OF FUNDS-1979/1980
 (in US\$ equivalent)

	<u>1979</u>	<u>1980</u>
<u>RESOURCES</u>		
Loan repayment	237,874	249,637
Capital contributions (incl. reserves)	11,411	13,533
Borrowings from Peruvian banks	145,066	160,103
Borrowings from Foreign banks	89,102	121,846
Borrowings from Foreign Government & Institutions	19,899	3,307
State contribution	7,434	9,986
Pre-tax income	2,198	3,133
Other	28,033	62,216
Total Resources	<u>\$ 540,927</u>	<u>\$623,761</u>
 <u>APPLICATIONS</u>		
Increase in loan portfolio	293,734	303,994
Additions to Fixed & other assets	9,839	22,623
Amortization of Peruvian bank debt	125,082	140,728
Amortization of Foreign bank debt	86,336	116,975
Amortization of Foreign institutions debt	5,818	2,084
Other	20,118	37,357
Total Applications	<u>\$ 540,927</u>	<u>\$623,671</u>
 Conversion Rate (soles per \$)	 250.75	 342.61

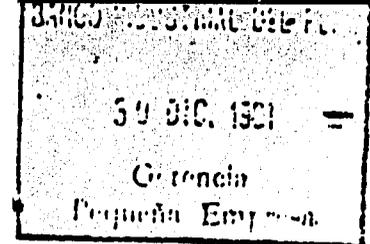
BIP - COMPARATIVE RATIOS-1978/1980

	<u>1978</u>	<u>1979</u>	<u>1980</u>
Ratios Measuring:			
1. Capitalization			
Capital ratio (1)	17.6%	18.9%	26.4%
Leverage (Total liabilities to Equity)	8.47x	6.21x	3.34x
Indebtedness ratio (Bank debt to Equity)	7.16x	4.44x	2.71x
2. Solvency and Liquidity			
Solvency (Equity to deposits & current liabilities)	1.58	2.63	4.03
Liquidity (Cash plus short-term investment to deposits plus current liabilities)	50.1%	116.8%	103.0%
3. Profitability			
Return on Average Equity	3.9%	3.2%	2.9%
Return on Average interest-earnings Assets	0.4%	0.4%	0.6%
Profitability of operations (net income to total income)	2.5%	2.1%	2.4%
Interest spread on loans (net interest and commissions (2) to average loan portfolio)	3.4%	3.8%	7.8%
Return on loan portfolio (net income to average loan portfolio)	0.4%	0.5%	0.6%

(1) defined as total equity (including provisions for doubtful accounts) to total assets (including the same provision)

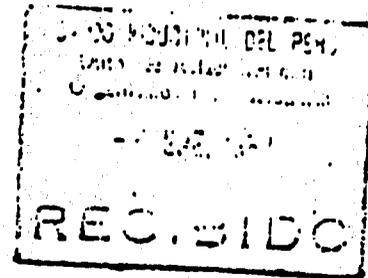
(2) defined as total interest and commission income minus total interest & commission expense

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Annex II
Exhibit J
Page 1 of 10

Lima, 24 de Diciembre de 1981



Señor
Carlos Lecca Arrieta
Gerente Adjunto, Jefe del Area de
Promoción y Desarrollo
PRESENTE

De acuerdo a lo solicitado por la Gerencia Financiera de realizar una encuesta a pueblos jóvenes en las ciudades de Chiclayo, Ica y Lima, se adoptó la siguiente metodología:

1. Elaboración de la encuesta.- De acuerdo al planteamiento presentado por la Gerencia Financiera se elaboró la encuesta, Anexo N°1,

2. Acciones de coordinación.-

En LIMA : Se tomó contacto con la Dirección de Promoción del MITI, de donde se nos informó de los pueblos jóvenes más significativos en cuanto a su población y capacidad de trabajo en los conos norte y sur,

Los pueblos jóvenes señalados fueron: Tahuantinsuyo, Payet, Villa María del Triunfo y San Juan.

En ICA : Se coordinó con la Dirección Regional de Vivienda y Construcción, informando la existencia de 12 pueblos jóvenes con una población general de 19,646 personas.

La encuesta se realizó en los pueblos jóvenes: La Esperanza, San Carlos, Botifería de Angulo, Acomayo A, José de la Torre Ugarte, Pasaje Valle y Pasaje Tinguina,

En CHICLAYO : Se realizó coordinaciones con la Oficina de Participación de los Vecinos de la Municipalidad Provincial de Chiclayo, Oficina de Valores y Licencias, ORDELAM, Oficinas de Redes de Electro Perú.
Los pueblos jóvenes entrevistados fueron: La Victoria, Muro, San Antonio, San Francisco,

3. Tamaño de la Muestra

El tamaño de la muestra fué preseleccionado por la División Financiera habiéndose realizado un total de 120 encuestas, (Anexo # 2).

Su selección se basó en el 83% en pueblos jóvenes de tipo A (agua, desagüe, luz eléctrica); el 4 % del tipo B (luz eléctrica) y 23% del tipo C (no cuentan con ningún tipo de servicio).

4. Resultados de la Encuesta

Referente al lugar de nacimiento de los encuestados se observa que:

Chiclayo : el 75% son de origen del mismo departamento y el saldo de Cajamarca.

Ica : el 50% son de origen del mismo departamento.

Lima : el 4% es de origen de Lima, siendo el saldo procedentes de Ayacucho, Ancash, La Libertad, Cajamarca.

En cuanto a las edades de los encuestados, estas fluctúan entre 20 y 50 años, el 52.5% laboran en talleres y el 44% se dedica a sus trabajos dentro del hogar.

~~Las compras las realizan al contado un 45% y a los minoristas 38%, siendo su producción lograda en forma individual (74%), dedicándose 93% a la artesanía, utilizando la comercialización directamente al consumidor (66%),~~

Referente a la Asistencia Técnica el 84% no ha recibido ninguna capacitación y el 87% lo desearía.

Los sectores que desean una mayor capacitación y adiestramiento son:

Confecciones	:	16%
Ebanistería	:	13%
Calzados	:	6%
Repostería	:	6%

CONCLUSIONES :

1. Se observa la falta de infraestructura en los pueblos jóvenes para un mejor desarrollo de sus actividades - salvo Lima que se encuentra en una mejor situación.

- 2. Realizar programas de Asistencia Técnica y Adiestramiento con el propósito de mejorar su nivel socio-económico. (Referente a comercialización, producción, tecnología, etc.).
- 3. Difundir los beneficios del BIP en apoyo a estos sectores: artesanía, pequeña empresa.

Atentamente,

Maria Eugenia Tuesta H.
 Maria Eugenia Tuesta H.
 Ejecutivo Adjunto
 Jefe Dpto. de Divulgación

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mvd

4
1/1/77
Para a la Dir.
Financiera
[Signature]

Comente Don. P. Sup.

La encuesta (entrevista) fue programada para el viernes 11 de octubre de 1977 para dar cuenta de los resultados de la encuesta y para dar cuenta de los resultados de la encuesta y para dar cuenta de los resultados de la encuesta...

30/12/81

[Signature]
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LUGAR : _____

FECHA : _____

ENCUESTA

Concejo Provincial de: _____
Distrital

1. Prioridades de Desarrollo Urbano de los Pueblos Jovenes

Especificación del Pueblo Joven:

Tipo "A": <input type="checkbox"/> Tiene agua, de sague y luz - eléctrica.	Tipo "B": <input type="checkbox"/> Tienen luz eléc trica solamente.	Tipo "C": <input type="checkbox"/> No cuentan con servi cios básicos.
---	---	---

Nombre del Pueblo Joven: _____

Ubicación Geográfica: _____

Localización Urbana: _____

2. Datos Personales del Encuestado

Nombre del entrevistado (a): _____

Dirección del Taller o Empresa: _____

Domicilio Particular: _____

Lugar de nacimiento y edad: _____

Tiempo que vive en la zona: _____

3. Actividad Económica de la Empresa en la localidad.

Especificación de la Actividad Económica:

Industria Artesanía Turismo Pesquería Servicios

Comercio

Dedicación del Giro o Negocio: _____

Tiempo de experiencia como Empresario y/o Artesano: _____

Grado de Instrucción y/o Especialización: _____

Cursos de capacitación o Adiestramiento recibidos ultimamente: _____

4. Función Empresarial de la Empresa en el Medio Ambiente:

Especificación del medio ambiente:

Hogar Taller Fábrica Centro Comunal Complejo

Area del Ambiente de Trabajo Total: _____

Número de Equipos o Maquinarias que utiliza: _____

Los Equipos o Máquinas son de su propiedad: Sí No

Los equipos ó máquinas han sido cancelados o se encuentran pagándose.

Para la adquisición de los equipos o maquinarias que tipo de crédito utilizó: Crédito Bancario Crédito Comercial

En que organismo: _____

Para la Adquisición de las materias primas principales que modalidad de compra empleó: A la Fábrica Al contado
Al Mayorista Al Crédito
Al Minorista

Número de trabajadoras que emplea actualmente: _____

5. Características sobre el sistema de Producción de la Empresa

Especificación de la Producción:

Producción Individual Producción en Serie

Número de Unidades Producidas: _____

Costo de Operación Promedio de la Unidades: _____

Precio Promedio de venta de cada Unidad: _____

6. Características Sobre el Sistema de Servicios de la Empresa

Especificación del Servicio:

Servicio Domiciliario Servicio en Talleres Maestranza General

Número promedio de clientes atendidos: _____

Costo promedio por cada servicio: _____

Honorarios promedios sobre los servicios prestados: _____

7. Características sobre el Sistema de Comercialización de la Empresa

Especificación del nivel del mercado:

Consumidor Minorista Mayorista Fábrica

Modalidad de venta que realiza directa y/o indirectamente: _____

8. Características sobre los Sistemas de Enseñanza Profesional o Técnica.

Especificación de los centros educativos:

Senati Centros Privados Escuelas Técnicas Otros

Ha recibido usted Asistencia Técnica en el último año: Sí No

En que centro de enseñanza: _____

Y en que especialidad: _____

Desearía recibir Asistencia Técnica en la Modalidad de:

Cursos Asesoría Otros Sí No

Descripción de la Especialidad: _____

9. Datos sobre los Servicios Crediticios, Bancarios y otros del BIP.

Conoce los servicios del BIP.:

Radial Televisiva Periodística Referencia de amigos
Visita al local del Banco

Ha solicitado usted crédito al Banco: Sí No

Cual fué su resultado: _____

10. Reporte del Encuestador del Banco

Opinión sobre la persona entrevistada: _____

(Nombre)

(Firma)

INFORME

Lima, 21 de diciembre de 1981

Sra. María Eugenia Tuesta H.
Ejecutivo Adjunto, Jefe del
Dpto. de Divulgación
PRESENTE.-

Referencia : Descripción Analítica de las Encuestas de los Pueblos Jóvenes Realizadas en las Ciudades de Ica, Lima y Chiclayo

En atención a lo dispuesto por su despacho, informamos a usted lo siguiente :

1. Prioridades de Desarrollo Urbano de los Pueblos Jóvenes en Ica, Lima y Chiclayo.-

	<u>No. de Encuestados</u>
1.1. <u>Pueblo Joven de Tipo "A"</u> Tienen agua, desagüe y luz eléctrica	88
1.2. <u>Pueblo Joven de Tipo "B"</u> Tienen luz eléctrica solamente	5
1.3. <u>Pueblo Joven de Tipo "C"</u> No cuentan con servicios básicos	27
Total :	<u>120</u>

2. Lugares de donde provienen los encuestados en las ciudades de Ica, Lima y Chiclayo.-

2.1. Huancavelica	8 personas
2.2. Ayacucho	10 personas
2.3. Ica	20 personas
2.4. Arequipa	5 personas
2.5. Apurímac	3 personas
2.6. La Libertad	8 personas
2.7. Ancash	8 personas
2.8. Cajamarca	12 personas
2.9. Cuzco	1 persona
2.10. Junín	2 personas
2.11. Lambayeque	30 personas
2.12. Lima	8 personas
2.13. Puno	1 persona
2.14. Piura	2 personas
2.15. San Martín	2 personas
Total :	<u>120 personas</u>

3. Edades de los Encuestados en las ciudades de Ica, Lima y Chiclayo.-
- | | | |
|---------|----------------------|---------------------|
| 3.1. | De 20 años a 30 años | = 30 personas |
| 3.2. | De 31 años a 40 años | = 30 personas |
| 3.3. | De 41 años a 50 años | = 35 personas |
| 3.4. | De 51 años a 60 años | = 19 personas |
| 3.5. | De 61 años a 70 años | = <u>6 personas</u> |
| Total : | | 120 personas |
4. Ambiente de Trabajo que Emplean los Encuestados en las ciudades de Ica, Lima y Chiclayo.-
- | | | |
|-------|---------------|---------------------|
| 4.1. | En el hogar | = 53 personas |
| 4.2. | En el taller | = 63 personas |
| 4.3. | En la Fábrica | = <u>4 personas</u> |
| Total | | <u>120 personas</u> |
5. Adquisición de Equipos y Maquinarias de los Usuarios de las Ciudades de Ica, Lima y Chiclayo.-
- | | | |
|-------|-------------------|----------------------|
| 5.1. | Crédito Bancario | = 4 personas |
| 5.2. | Crédito comercial | = 19 personas |
| 5.3. | Compra al contado | = 55 personas |
| 5.4. | Ninguna compra | = <u>42 personas</u> |
| Total | | <u>120 personas</u> |
6. Adquisición de Materias Primas de los Usuarios de las Ciudades de Ica, Lima y Chiclayo.-
- | | | |
|-------|----------------|----------------------|
| 6.1. | A la Fábrica | = 8 personas |
| 6.2. | Al mayorista | = 35 personas |
| 6.3. | Al minorista | = 45 personas |
| 6.4. | Ninguna compra | = <u>32 personas</u> |
| Total | | <u>120 personas</u> |
7. Sistema de Producción que aplican los encuestados de las ciudades de Ica, Lima y Chiclayo.-
- | | | |
|---------|-----------------------|----------------------|
| 7.1. | Producción Individual | = 89 personas |
| 7.2. | Prod. en serie | = 0 personas |
| 7.3. | Ninguna producción | = <u>31 personas</u> |
| Total : | | <u>120 personas</u> |

8. Fuentes de Trabajo que emplean los encuestados en las ciudades de Ica, Lima y Chiclayo.-

8.1 En Artesanía	=	111 personas
8.2. En Pequeña Industria	=	62 personas
8.3. En el comercio	=	21 personas
8.4. En servicios	=	28 personas
Total :		<u>222 personas</u>

9. Sistema de Comercialización utilizado en las ciudades de Ica, Lima y Chiclayo .-

9.1. Venta al consumidor	=	79 personas
9.2. Venta al minorista	=	6 personas
9.3. Venta al mayorista	=	2 personas
9.4. Venta en fábrica	=	0 personas
9.5. Ninguna venta (servicios)	=	33 personas
Total	=	<u>120 personas</u>

10. Sistema de Enseñanza recibido en las ciudades de Ica, Lima y Chiclayo.-

10.1 Enseñanza en Senati	=	1 persona
10.2 Enseñanza en Centros Privados	=	8 personas
10.3 Enseñanza en escuelas técnicas	=	10 personas
10.4 Ninguna enseñanza	"	<u>101 personas</u>
Total		<u>120 personas</u>

11. Asistencia Técnica solicitada por los encuestados en las Ciudades de Ica, Lima y Chiclayo.-

11.1. Curso sobre Telares	1 Persona (s)
11.2 Curso sobre bordados	4 "
11.3 Curso sobre Tejidos	3 "
11.4 Curso sobre Confecciones	17 "
11.5 Curso sobre Repostería	6 "
11.6 Curso sobre Ebanistería	14 "
11.7 Curso sobre Cocina	1 "
11.8 Curso sobre Pastelería	1 "
11.9 Curso sobre Motores	5 "
11.10 Curso sobre Calzados	6 "
11.11 Curso sobre Electrónica	4 "
11.12 Curso sobre Comercio	3 "
11.13 Curso sobre Cosmetología	1 "
11.14 Curso sobre Panificación	5 "

