LATIN AMERICA

REGIONAL RURAL AGRIBUSINESS DEVELOPMENT

PROJECT NO. 596-0069

LOAN AGREEMENT NO. 596-T-016

ROCAP

AUDIT REPORT NO. 1-596-83-12

JUNE 13, 1983

This $25 million has provided funds for agribusiness activities of the type that should increase markets for small farmer production, job alternatives for the underemployed, and institutional capabilities. Although all funds have now been disbursed, the benefits to these target groups were delayed because of project implementation problems.

The impact that the project has had or may have on the intended beneficiaries was not known because an evaluation which covered this aspect had not been made. Because of the continuing nature of this project, we have recommended that an evaluation be made to determine impact and what changes should be made to improve effectiveness.

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Regional Rural Agribusiness Development

Project No. 596-0069

Loan Agreement No. 596-T-016

ROCAP

EXECUTIVE SUMMARY

This is a report covering our audit of the Regional Rural Agribusiness Development Project being implemented by the Central American Bank for Economic Integration (CABEI). The project totals about $25.0 million and was financed by A.I.D., CABEI, and the participating Intermediate Credit Institutions (ICIs) of five Central American countries. The purpose of the project was to provide long-term financing and technical assistance for the promotion, development, and expansion of agribusiness enterprises in Central America. The goal of the project was to improve the well-being of the rural poor by making agricultural inputs, markets and employment opportunities more readily available.

The audit was made in connection with the normal schedule of audits of this office and had the purpose of determining if the project was being implemented in the most effective, efficient, and economic manner. In brief, we found that progress had been made in providing funds for agribusiness activities. By July 31, 1982, a total of 22 subloans had been made to 17 ICIs and 94 subprojects had been approved or were in the process of approval. Some of these subprojects were of the type that could promote activities and offer markets for small farmer production and job alternatives to the underemployed. However, project implementation had been slow - only half of the funds had been disbursed at that time - and an evaluation had not been made to determine what impact the project had on the intended beneficiaries.

There were several interrelated reasons that impeded the implementation of activities. For example, difficulties were encountered in adapting existing procedures to a different environment, little priority was given to project activities, delays were experienced on reimbursement requests and the economic and political tensions of the area created additional problems.

The Regional Office for Central American Programs (ROCAP), AID's monitoring office, reported that subsequent to our field work significant changes were made in CABEI's operations. These changes reportedly resulted from several months of intense efforts by ROCAP's staff. By March 1983, all funds committed to the project by AID, $15 million, had been disbursed. ROCAP also advised that an evaluation of this activity was planned to determine how a follow-on project (if one materializes) would be designed in order to avoid the operational problems encountered in this project.

Under the terms of the AID loan (596-T-016) financing this project, principal repayments from the subloans (rollover funds) are to be used to finance additional agribusiness activities during the remaining life of the 30-year loan. Thus, the rollover funds may be several times greater than the original amount of funds provided. Therefore, we believe it is essential for the planned evaluation to determine what has been accomplished, what impact project activities have had on the target groups, and what changes should be made to improve the use of rollover funds.

BACKGROUND AND SCOPE

Background

Loan agreement No. 596-T-016 for the Regional Rural Agribusiness Development Project No. 596-0069 was signed on February 2, 1977, and provided an amount not to exceed $15 million to the Central American Bank for Economic Integration (CABEI). The purpose of the project was to provide long-term financing and technical assistance through Intermediate Credit Institutions (ICIs) for the promotion, development, and expansion of agribusiness enterprises in Central America.

Agribusiness activities pertain to all operations involved in the manufacture and distribution of farm commodities and items made from them. This included all participants in the production, processing and marketing of a single farm product, from initial inputs to final consumer sales.

The goal of the project was to improve the well-being of the rural poor. A subgoal was to increase the participation of the rural poor in the benefits to be derived from agribusiness activities. Project plans called for participation in the program by five countries: Guatemala, El Salvador, Honduras, Nicaragua, and Costa Rica. Project implementation was planned to be accomplished over a four-year period with a completion date of December 2, 1981. The completion date was extended twice, first to December 2, 1982 and subsequently to March 31, 1983.

The project was designed: (a) to develop agribusiness activities in Central America; and (b) to improve the institutional capability of CABEI and the ICIs to implement agribusiness activities. Agribusiness activities were to provide significant benefits to the rural poor. An estimated $25 million in project funds (comprised of the $15 million AID loan, $5 million from CABEI, and $5 million from participating ICIs) were to be used to finance: (a) capital goods, e.g., plant equipment, storage facilities, and transportation equipment; (b) technical assistance; (c) production and/or purchase of raw materials for processing; and (d) agribusiness working capital requirements.

Loan funds were being channeled through CABEI for relending to ICIs. The ICIs relend the funds to support five categories of agribusiness activities which:

1. contribute to improve small farm agricultural production, such as suppliers of inputs, financing of improved technologies, etc.;

2. process raw materials purchased from small producers, such as fruit and vegetable processing plants, canneries, etc.;

3. relate to permanent non-traditional crops grown by small farmers to supply agribusiness processors;

4. assist in the marketing of small farmer agricultural products; and,

5. generate extraordinary employment benefits, even though there may be little or no small farmer production participation.

As of July 31, 1982, only $8.8 million of the project funds committed by AID and CABEI had been disbursed (Exhibit A). In its comments on a draft of this report, ROCAP reported that all $20 million committed to this project by AID and CABEI had been disbursed by March 25, 1983. The amount of funds contributed to finance project activities by the ICIs was not available. A profile of the subprojects approved or in the process of approval as of July 1982 is shown in Exhibit B.

Scope of Audit

This audit covered project activities from inception of the loan agreement on February 2, 1977, through August 31, 1982. (Certain information has been updated based on data presented in ROCAP's comments.) The purposes of the review were: to determine if the project was being implemented in an effective, efficient, and economical manner; and to make an overall assessment of project accomplishments versus the goals and objectives. Our efforts were directed towards identifying significant problem areas, and their causes, in planning, implementing, and monitoring the project.

The review was made in accordance with generally accepted auditing standards adopted by the U.S. Government. Taking into account the problem areas identified during the survey phase of our audit, we included such tests of the records, procedures, and operations as we deemed necessary in the circumstances. We reviewed project documentation maintained by ROCAP and CABEI, and examined the loan funds channeled through CABEI for relending to ICIs in Guatemala, Honduras, Costa Rica, El Salvador, and Nicaragua. We discussed project progress and problems with ROCAP and CABEI officials.

Field work was done in Guatemala, Honduras, and Costa Rica. The primary focus of our review was to determine if the subprojects financed by the loan met the project purpose and provided the impact intended. We did not visit El Salvador because of the security situation outside of San Salvador, and we did not visit Nicaragua because significant activity had not taken place there under this project.

The results of our audit were discussed with ROCAP officials and their comments were considered in the preparation of this report.

FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

An Overall Assessment of Project Goals and Accomplishments

Some progress had been made toward the achievement of the objectives of this project. At the time of our field work, CABEI had made a total of 22 subloans to 17 ICIs in five Central American Countries (Honduras, Guatemala, Costa Rica, El Salvador, and Nicaragua). The ICIs had either approved or were in the process of approving a total of 94 subprojects. In its comments, ROCAP reported that by March 1983, 29 subloans had been made to 21 ICIs and 141 subprojects had been approved. These subprojects were for a variety of activities, such as, poultry processing, dairy and milk production, foodstuff, grain commercialization, rubber production, and incubators (Exhibit B). Some of the subprojects were the type that could promote activities and offer markets for small farmer production and job alternatives to the underemployed. However, project implementation was slow and evaluations had not been made to determine the impact made by these subprojects. Therefore, benefits to the rural poor have been delayed and facts needed were not available to determine the extent that project goals and objectives had been accomplished.

Implementation of the project was originally planned to take place over a four-year period ending December 2, 1981. As of December 1979, two years after the loan was signed, a total of $5.7 million had been approved for subprojects and less than $900,000 had been disbursed. Implementation continued at a slow pace over the next two years. By October 1981, just two months short of the original termination date, less than half of the funds under the project had been approved for subprojects and only about $6.9 million had been disbursed. By July 1982, $13.8 million had been approved for subprojects and $8.8 million had been disbursed.

Various factors contributed to the delays in the approval and disbursement of funds under the project:

- CABEI's staff had difficulty in adapting its procedures to financing small development-type activities through regional ICIs.

- CABEI gave little priority to activities under this project and thus, subprojects.

- Some delays were caused because ICIs did not submit reimbursement requests in a timely manner.

- The economic and political tensions in the countries participating in the project -- fluctuating exchange rates, substantial inflation, civil unrest, and repayments required in U.S. dollars -- have also affected the implementation of activities.

In its comments on our draft report, ROCAP advised us that it had worked closely with CABEI on various corrective measures which enabled planned disbursements to be completed by the revised terminal disbursement date. Among these actions were the establishment of improved coordination among its offices and the revision of subproject approval procedures for fund disbursements. Promotion activities were expanded considerably to assist the ICIs in collecting necessary documentation and presenting it to CABEI. Thus, $11.2 million were disbursed to the ICIs between July 1982 and March 1983. All funds provided by AID and CABEI under the project have now been made available to the ICIs according to ROCAP.

Project Impact and Evaluations

Required Evaluations Have Not Been Conducted.

Although the project has been underway for more than five years, its actual social and institutional development impact had not been determined. Only one comprehensive evaluation had been made and the recommendations made had not been fully implemented. A comprehensive evaluation is needed to review project accomplishments and to determine corrective action needed in future operations involving the use of rollover funds.

The project was designed to develop agribusiness activities, and to improve institutional capabilities of CABEI and participating ICIs. By making these improvements, the rural poor were to receive significant benefits. To measure the changes, the project paper emphasized three types of evaluations:

- Joint AID/CABEI reviews after each $2.5-million commitment of loan funds. These reviews were to focus on subproject compliance with the Congressional Mandate and impact on the target group, as well as, on problem subprojects;

- An annual evaluation of subproject progress based on the baseline data included Project Assessment Forms (PAFs) and yearly updates of this information; and

- Special assessments involving intensive analysis of selected subprojects using outside technical personnel.

Evaluation activity was very limited. There were no joint AID/CABEI reviews because of the slow pace of disbursements. The annual evaluations related to subproject baseline data were not done due to a lack of data provided by the ICIs. There was only one special assessment which was made by consultants in February 1980. The assessment made a number of recommendations to improve project implementation, to address the priorities needed in subproject selection and to measure impact on the target group. However, the recommendations were not fully implemented.

The original Project Assessment Forms submitted by the ICIs at the time the subproject was proposed contain selection criteria to determine whether proposed subprojects were eligible for financing. The baseline data in these Forms was to be updated annually to enable ready evaluation of the impact on target groups. If updated, the Forms would include the situation existing when subproject was proposed plus projected and actual results at the end of each year of operation. Among the quantitative impacts to be measured were small farmer participation, new jobs created, and farmer income generated. Qualitative effects to be determined included new technologies introduced, new inputs created, and market development.

CABEI procedures included a requirement that the ICIs submit annually an updated Project Assessment Form, and a progress report for each subproject. We found no evidence that the original Forms were updated or that the progress reports were submitted by the ICIs. Lack of such information limits ready analysis of progress achieved and the degree of loan impact. This data should be developed as a prerequisite to a project evaluation. We were informed by ROCAP in its comments on our draft report that CABEI was in the process of updating the Project Assessment Forms for use in a scheduled project evaluation of the project.

Recommendation No. 1

ROCAP should obtain from CABEI an updated Project Assessment Form for each subproject and Progress Report for 1982 as prerequisites to the scheduled evaluation.

CABEI Did Not Implement Recommendations Made In An Evaluation Report

The recommendations made in the 1980 Evaluation were not fully implemented by CABEI. Procedures should be establish to make better use of such studies.

The 1980 Evaluation Report recommended making a special impact assessment of four or five subprojects. It noted resistance to the use of baseline data in Project Assessment Forms and that annual updates of the data had not been required. The evaluators considered this data a critical element in the implementation process. Another important element to be examined was the feasibility of using a regionally-based, credit-banking mechanism to identify/fund agribusiness activities directly benefiting the rural poor. They recommended that CABEI examine its review procedures to focus on social impact requirements unique to the program, and shift feasibility review to ICIs with demonstrated ability to perform these studies, thus speeding up the approval and disbursement process.

The evaluation further recommended that priority guidelines be established on subproject proposals, and on social and economic impact. First priority was suggested for subprojects raising incomes of small producers, with ranking based on increased income per dollar of investment and proportion of increase

going to the small farmer. Second priority would be given to employment generation, with ranking by capital costs per job.

We reviewed the actions taken by CABEI on the implementation actions recommended by the evaluation. We found that CABEI did not rely much on the feasibility analyses made by the ICIs and continued to duplicate this analytical effort. It was not until mid-1981 that CABEI assigned a full-time staff to assist the ICIs in developing subprojects, and thus help to expedite loan implementation.

We believe that for the scheduled evaluation to be of any use, ROCAP must find some means of ensuring that CABEI implement, in a timely manner, the recommendations made. If CABEI does not or will not implement the recommended changes, then the evaluation will be of little or no value.

The Impact of the Project on The Targeted Population Had Not Been Determined

CABEI had not made the necessary study to determine the social and economic impact of the project. CABEI had financed more subprojects than planned; however, there may be a shortfall in number of new jobs created. This may result in significantly less achievement under this project than what was planned. A thorough study needs to be made by CABEI.

The project goal was to improve the well-being of the rural poor, and a subgoal was to increase their participation in the benefits to be derived from agribusiness activities. To measure this project's impact, and also appraise its cost effectiveness, evaluations were to be made an integral part of the project.

Disbursements of loan funds were slow until the final stages of the project. Also, determination of whether these disbursements contributed to improving small farmer income and providing jobs for the rural poor were not made. The social impact and the institutional development of CABEI and the ICIs as agribusiness financiers as a result of this project were also not determined.

We requested data from CABEI on the social impact achieved. The information provided was the estimated impact that was determined prior to the approval of proposals. When we asked for the actual impact realized to date on subprojects fully and partially completed, we were advised by CABEI's Coordinating Unit that compilation of this information was their "next job". This means that, although the loan was signed more than five years ago and close to $9 million had been disbursed as of July 1982, the impact on the incomes of small farmers and the generation of rural employment was unknown.

A September 1982 summary obtained from CABEI of subprojects approved or in process of approval, and projected benefits showed:

	No of Subprojects	Estimated AID/CABEI	Costs (000) Total	Benefited Small Prod.	Rural Jobs	Estimated Cost Per Job
Costa Rica	43	$6,682.9	$16,717.4	3,622	1,574	$10,621
Guatemala	20	5,775.9	23,577.7	7,101	1,924	12,254
El Salvador	24	3,545.9	13,467.7	1,469	954	14,117
Nicaragua	15	2,770.5	3,002.0	1,066	496	6,052
Honduras	9	2,274.2	4,343.6	874	140	31,026
	111	$21,049.4	$61,108.4	14,132	5,088	$12,010

Some 50 subprojects were initially estimated to receive AID/CABEI financing of $20 million, with a total funding from all sources of $41.7 million. As summarized above, 111 subprojects costing an estimated $61.1 million were to be financed from all sources as of September 1982. If realized, this would be a substantial increase in the number of subprojects over original estimates. (ROCAP reported that 141 subprojects had been approved by March 1983. Data on the other figures in the above table were not submitted.)

However, the number of jobs expected to be generated, 5,088 was considerably less than the estimate included in the project paper of 18,500 jobs. This may be due to an unrealistic estimate and/or financing of subprojects which were not labor-intensive such as processing equipment. The evaluation should develop more complete information on employment generation achieved and small farmer participation realized.

We reviewed the projected costs-per-job generated by subprojects approved or under review by CABEI during the 1981-82 period. The sole social impact of 31 of these subprojects was estimated to be the generation of rural employment. The estimated total cost of these activities, including AID/CABEI financing of $5.4 million, was $13.6 million. This resulted in an average cost-per-job created of $12,670. If the $5,000 cost-per-job maximum limitation suggested by the 1980 evaluation had been applied by CABEI, only 5 of the 31 subprojects would have been acceptable for financing.

The project impact on the incomes of small farmers in the region was not determined by the 1980 evaluation. It was considered too early in the program to quantify these benefits because only 6 of the 20 subprojects reviewed by the evaluation showed significant potential small farmer impact.

The actual social impact of the project had not receive the attention needed during implementation of the project because emphasis was placed on expediting disbursement. We believe this matter must receive AID/CABEI priority attention to determine what this impact has been, and to take corrective action where possible to improve the benefits to small farmers and the rural poor. Any decision for further AID agribusiness financing through CABEI should be based upon the experience to date, and the economic impact realized.

ROCAP reported that as of March 25, 1983, all funds had been disbursed under the project; therefore, it is not necessary to modify the existing project and the results of any evaluation would be used in the design of any follow-on project. We disagree with this and believe that the results of an evaluation should be used in the continued implementation of the current project. Under the terms of the loan agreement, principal repayments under subloans (rollover funds) are to be used to finance additional agribusiness activities during the remaining life of the 30-year loan. Thus, rollover funds may be several times greater than the original $20 million disbursed on this project. Therefore, we believe that it is necessary for the planned comprehensive evaluation of the project to determine project accomplishments and what impact project activities have had on the target groups (small farmers, rural poor and institutional development). Where less than the planned objectives are shown to have been accomplished, the evaluation should recommend changes.

Recommendation No. 2

ROCAP should include in its scheduled evaluation of the Regional Rural Agribusiness Development project, a requirement that accomplishments and impact on target groups be determined and, if necessary, recommend changes for use of rollover funds.

Institutional Development

Institutional Development Of CABEI Was Limited. This project was designed to improve the institutional capability of CABEI and the ICIs in implementing agribusiness activities. CABEI's capacity to promote and finance agribusiness activities was strengthened somewhat by its participation in this project. However, CABEI still needed to improve its capabilities in such areas as agribusiness promotion, subloan processing, and review and disbursement procedures. A primary concern was the need for greater flexibility and responsiveness in meeting the demands of the agribusiness sector. We requested information on the growth of CABEI agribusiness financing in addition to that resulting from the AID program, but the data was not provided. This information should be determined in the evaluation to establish progress made by CABEI as an agribusiness financier. In our opinion, improvement in this area must be shown before CABEI is considered for participation in a follow-on loan for agribusiness financing.

Agribusiness Promotion. CABEI took little action early in the program to promote agribusiness financing. After satisfying the conditions precedent to initial disbursement, in July 1977, CABEI was involved in reviewing applications from regional ICIs interested in participating in the program. However, progress was limited since CABEI staff members were unable to devote sufficient time to loan activities.

In November-December 1978, ROCAP indicated that CABEI should assign an officer to spend most of his time on program follow-up. ROCAP also recommended that CABEI assign full-time staff to help the ICIs identify, select, and submit subprojects for possible financing. ROCAP estimated that disbursements in the following two years could be up to $10.2 of the planned $20 million. CABEI acknowledged that determining ICI eligibility and issuing subloans had been slow, and that the submission of subprojects by ICIs had to increase considerably.

However, while CABEI did act on the recommendation to improve follow-up, promotion efforts did not improve greatly until mid-1981, when two consultants were hired to work fulltime and assist ICIs in subproject promotion. This apparently helped to increase the level of approved subprojects, but too much time had been lost previously. The October 1980 level of approved subprojects, totaling $6.1 million, only rose to $13.8 million by July 1982.

CABEI Review Procedures. CABEI did not effectively modify its customary review procedures to meet the requirements of this program where intermediate financiers were performing feasibility reviews of proposed subprojects. CABEI continued to make subproject feasibility reviews as it did for direct commercial loans, without relying on the feasibility studies made by the ICIs. This duplication of effort delayed approval of subprojects and slowed the disbursement of AID/CABEI loan funds.

The ICI considered in detail the financial, economic, and technical viability of the subproject and its social impact. The results of these analyses were submitted to CABEI for review. CABEI should rely on ICIs to conduct thorough investigations and analyses of all subprojects, since the ICIs were responsible for implementation of the subproject. However, the various technical and financial offices of CABEI also performed comprehensive reviews prior to approval or rejection of the proposed subprojects.

Although this problem has been recognized for quite some time and was reportedly corrected (per CABEI letter in April 1981), it remained as a bottleneck in the loan implementation process. A CABEI February 1982 report said: "As of this date problems still persist in internal transmission that impinge on the progress of the project". Action is needed to correct this continuing problem. Two instances where CABEI deviated from established procedures for approval of subprojects are described in the Loan Administration and Management section of this report.

Subloan Issuance One of the primary causes for CABEI's slowness in making disbursements has been the lengthy period required to issue subloans. This was due to ICI's lack of familiarity with, and agreement on, CABEI subloan terminology. The lengthy CABEI review process also contributed to the time required. CABEI reorganized agribusiness program operations in June 1979. One of the objectives was to focus on the difficulty of subloan contractual clauses that ICIs had found to be too rigorous, thus delaying subloan execution.

We reviewed the period required from the time an ICI became eligible until a subloan agreement was completed. For eight subloans totaling $5 million, the period ranged from 8 to 34 months. As described in Annex A, we found subloans which had been under negotiation between ICIs in Guatemala and Costa Rica but had not been agreed upon. We have also reported in Annex A on a $3-million subloan whose implementation has been delayed due to lack of agreement between CABEI and the Government of Nicaragua on loan disbursement in dollars. Action has since resolved these matters.

Institutional Building of ICIs. While a number of ICIs initially contracted with CABEI for subloans, more recently some of these ICIs have not assumed subloans due to the problem of foreign exchange risks. These circumstances resulted in Central Banks assuming a significant portion of the subloans financed. The national ICIs, in these instances, were still involved in the identification and feasibility review of subprojects and were continuing to develop their capabilities in this regard.

Prior to project inception, 48 ICIs throughout the region were visited by ROCAP/CABEI to prequalify those interested and experienced in agribusiness financing with plans/projects for future financing of agribusiness activities When the project was planned, 13 ICIs in the region appeared capable of project participation.

In July 1982, some 17 ICIs in the five participating countries had received subloans for subproject implementation. In two of the countries, Costa Rica and Guatemala, ICI participation essentially had been only in the selection and implementation of subprojects since early 1982. The Central Banks in these two countries were asked to take responsibility for repaying subloans to CABEI because the ICIs are unwilling to assume the risks inherent in making foreign exchange repayments. Nonetheless, the ICIs are continuing to build up their experience in implementing subprojects. This is important because agribusiness financing generated by the AID loan will be a long-term activity due to the use of rollover funds. In view of the expanded level of ICIs now participating in the project, we make no recommendation.

Technical Assistance Needs. Original plans for providing required technical assistance to the participants of this project were not realized. In actual practice, technical assistance was being provided to the participants, and was being financed, by different sources. The project still needed some technical assistance; however, the exact needs have to be determined.

The project plan recognized that it would perhaps be difficult to identify the level of technical assistance required. The estimate from the ICIs, based on their limited experience, was that 10 percent of total subproject costs would be required for this support. This estimate amounted to $2 million of the $20 million programmed. Anticipated problem areas requiring technical assistance included production technology; use of fertilizers, insecticides, and pesticides; quality control; plant operating methods; and financial management.

The record showed that AID/CABEI-financed technical assistance was substantially below the amount anticipated in the project design. We specifically identified $136,000 used to finance technical assistance financing. Part of these funds were used to finance the technical assistance obtained by an ICI, FIGSA, in Guatemala for four of its subprojects. Late in the program (in mid-1981), CABEI financed the first-year salaries of two full-time promotion advisors. They have consulted regularly with ICIs and subborrowers, particularly in preparation of subproject feasibility studies and loan documentation. However, the level of technical assistance actually provided is greater than this and the record did not tell the complete story.

The facts are that some technical assistance was provided to agribusinesses from ICIs and equipment suppliers and the cost of this support could not be identified. In some instances, managers of agribusinesses and their production supervisors provided the required technical assistance. In other instances, suppliers of loan-financed machinery and equipment provided the required expertise in installation, operation and maintenance, and included the cost in the purchase price. Public technical institutes also provided supporting services. Some ICIs even used part-time assistance to review loan applications but these costs were not charged to the loan.

There were some project activities still in need of technical assistance. In our visits to subprojects, we noted instances where technical assistance to effectively implement subproject activities had not been provided. The ICI FECOMERQ, in Guatemala, was unable to obtain or provide any technical assistance in the use of fertilizers purchased with loan funds. The Government of Guatemala did not provide agricultural extension service to farmers located in the area where FECOMERQ cooperatives supplied this fertilizer due to the security problems. With proper use of fertilizer, rural farmers could realize a significant increase in income. Reportedly, conditions in the area improved recently and the provision of technical assistance should be reconsidered.

Our visit to the URCO PAPA subproject in Costa Rica disclosed that technical assistance was needed for this agribusiness to properly store and process perishable products. This would enable production to be greatly increased with better use of workers and equipment. Since inception of operations earlier this year, the subproject had problems with inadequate drying equipment financed by the loan. Management officials attributed their difficulties to inexperience and the lack of technical guidance which led to the purchase of a dryer which was unsuitable for the climate in Costa Rica. The firm needed financing for technical assistance to help establish a storage area in its plant to increase processing capacity and regularize production. The staff also needed training in the handling of perishable products.

The technical assistance plans for this project were not realistic. They did not contemplate the possibility that other sources would be providing and financing such technical assistance. This appears to have resulted in overestimating the amount of financing needed for this part of the project and its subsequent non-use delayed the utilization of loan funds. The adequacy of technical assistance provided and its impact on subproject activities and contribution to target social benefits, as well as the amount of any additional technical assistance still needed should be determined in a project evaluation.

Loan Administration And Management By CABEI

CABEI did not administer or manage the project and funds in the most effective manner. Steps were needed to improve effectiveness in several areas; such as, the organization, the procedures to approve subloans, the channels used to processing subloan applications, and the expected benefits of the subloans. In response to a draft of this report, ROCAP reported that changes were made within the CABEI organization, subloan approvals and assistance to ICIs. The changes resulted in the rapid disbursement of funds over the last eight months of the project. We have included the following sections in this report for consideration during the planned evaluation.

The Organization. Initially, CABEI had difficulty in staffing its organization and developing plans for administration of the loan. Submission of such plans was required as a condition precedent to initial disbursement, and according to ROCAP, the condition was satisfied in June 1977. However, CABEI did not complete these plans until December 1979, when its operations dealing with the agribusiness program were reorganized to help expedite the program. A unit was established to: (a) coordinate CABEI actions on operating problems; (b) assist ICIs in presentation of projects and disbursement documents; and, (c) improve program coverage. CABEI's regional offices in the five countries were also brought into the coordination process to serve as contact points between ICIs and CABEI's home office in Honduras. Despite this reorganization, CABEI was unable to meet the disbursement schedule and the TDD had to be extended to March 31, 1983.

In November 1978, ROCAP discussed with CABEI the need to obtain outside technical assistance to help ICIs in subproject preparation and development, and to speed up implementation. But 2-1/2 years passed before CABEI provided full-time staff specifically for technical assistance. This delay further contributed to the lag in disbursements.

Procedures to Approve Subprojects. CABEI has not always followed established procedures to approve subprojects. For instance, established procedures were not followed for the approval of subprojects financed under loans in Costa Rica and Guatemala. This resulted from a CABEI attempt to speed up the approval process. The concerned Central Banks were not consulted, nor given the opportunity to approve the subprojects in accordance with agreed upon procedures. The banks however did approve the subprojects before funds were disbursed.

Procedures for the review of subprojects were based on the ICIs relending to agribusiness activities determined eligible for financing. Thus, the participating ICI's were the focal point for identifying and promoting subprojects and their design. The ICIs were to apply acceptance criteria for subproject eligibility and make a target beneficiary group analysis, along with financial viability and technical feasibility analyses. Subproject eligibility was determined by the ICIs on a case-by-case basis. They considered the nature of the agribusiness, the impact on production versus rural employment, farmer net income in the subproject region, and prior experience with the crops to be grown.

The ICI should reach its own conclusion on a subproject. Then if approved, the loan application should be presented to CABEI for financing under the program. CABEI's technical analysis staff would then receive and review the loan applications and make final determination on subproject eligibility.

Benefits of Some Subloans. A significant portion of loan funds were allocated, with the approval of ROCAP, to a subproject in Guatemala which had no benefit to small producers. The financing was questioned on the basis of two points. First, the subproject was solely for extraordinary employment generation, and secondly, an alternative source of financing was apparently available.

A subloan of $3.1 million to ICI Financier of Guatemala (FIGSA) was approved by ROCAP in October 1979. AID funds of $2,560,000 was allocated for this subloan and CABEI provided the remainder. FIGSA agreed to finance $465,000 with the subproject contributing $7,365,000 to the total subproject costs of $10.9 million.

The subproject scope called for planting and cultivating 1,800 hectares of rubber trees in the southwestern part of Guatemala. The subborrower's contribution was to finance land acquisition, some plantation costs, building construction, a hydroelectric plant and financing costs. The AID/CABEI contribution was to provide the remaining plantation development costs, other building and infrastructure costs, plus most of the machinery and equipment.

A total of $643,900 was disbursed from AID/CABEI funds for plantation development, machinery and equipment, infrastructure construction, and technical assistance. FIGSA did not disburse the remainder of the funds authorized because of implementation difficulties. The subborrowers were reportedly using the funds allocated for the rubber plantation in support of their coffee program which was in difficulty because of declining prices.

Other financing was obtained by the rubber subproject to replace the undisbursed AID/CABEI funds which were released to finance other approved subprojects. We believe that more consideration should have been given to the possibility of the subborrowers obtaining alternative financing before AID/CABEI funding was authorized. Subsequently, in a similar situation on another rubber subproject in Guatemala, proposed by ICI FIASA, ROCAP advised CABEI that it should not approve a project for financing if the subborrower had other sources of funds available.

Seventeen percent of the total AID funds available were allocated for the one rubber subproject in Guatemala. Our review disclosed that the only social benefit basis for approving this subproject was the estimated number of jobs that would be generated. No small producers were to benefit. We believe that this shows a need for closer examination before allocating a relatively large portion of available funds to a single subproject without any planned benefits for small farmers.

CABEI Bypassed Established Channels. Established channels were bypassed for processing some subloans. We found such deviations for subloans to ICIs in both Costa Rica and Guatemala.

In our discussion with CABEI in late August 1982 on the status of program disbursements in Costa Rica, we were informed that $4.3 million of reimbursement documents had been prepared by the implementing ICIs - the Bank of Costa Rica (BCR) and the National Bank of Costa Rica (BNCR). However, when we visited the ICI borrower, the Central Bank of Costa Rica (BCCR), we found that it had not yet signed the $6 million subloan, nor had it been provided with subproject applications for reimbursement request documentation. We were also informed that CABEI had approved eight subprojects amounting to $1.3 million prior to any approval decision by the BCCR. The Central Bank however, did approve the subprojects prior to the disbursement of funds.

We inquired at CABEI about why this deviation had been made from normal procedure, proper internal control, and good business practice. We were advised that CABEI wanted to hasten the approval process by reducing the bureaucratic procedures. However, two of the subprojects approved by CABEI in early July were reportedly still under analysis in mid-August. Thus, CABEI approval was given before a complete review had been made.

In Guatemala, a subloan agreement was completed between CABEI and the Central Bank of Guatemala for $2.825 million. However, CABEI approved subprojects amounting to $3.736 million for three implementing ICIs. Therefore, the subloan with the Central Bank will have to be amended to cover the additional amount approved by CABEI. Again, CABEI acted outside of established procedures in the approval process. Also, in this instance, the ICIs have to get Central Bank approval of subprojects before disbursement. One of the ICIs informed us that, although it had not completed an evaluation of two subprojects, CABEI had nevertheless approved them.

Correct procedures should be followed in the approval of subprojects for A.I.D. loan financing. CABEI should be required to obtain subproject applications properly approved by ICIs and then make its decision as to whether the subproject meets the criteria set forth for financing.

Actions of ROCAP. In our discussions with ROCAP management, the fact was stressed that they frequently met with or wrote to CABEI management to press for faster implementation. In response, CABEI periodically made new disbursement projections, but these proved to be unrealistic. An example of this was noted by ROCAP in August 1982, CABEI projected disbursements of $4.0 million during the period of January to June, but only $450,000 was disbursed during that period.

The Long-Range Needs. As we have discussed elsewhere in this report, in view of the long range nature of this program and the rollover funds from subloan principal repayments to finance more agribusiness activities, action should be taken to resolve the problems constraining implementation of activities. Also, the serious economic situation in Central America should be studied.

The Regional Rural Agricubusiness Development Project
Project No. 596-0059
Loan No. 596-T-016
Regional Subloan Activities of ICIs By Countries

As of July 1982, CABEI reported that 22 subloans had been issued. These loans amounted to $13,842,000 of the $20 million provided by AID ($15 million) and CABEI ($5 million). The subloans issued by country were as follows:

Country	Participating ICIs	Number of Subloans	Subprojects 1/	Value of Subloans ($000)
Honduras	Honduran Financier Bank (BANFINAN)	1	3	$196
	Cooperative Savings & Credit (FACACH)	2	4	915
	National Ag. Dev. Bank (BANADESA)	1	1	869
	Total	4	8	$1,980
Guatemala	Financier of Guatemala (FIGSA)	3	7	$1,648
	Industry and Farming Financier (FIASA)	1	2	500
	Coffee Bank (BANCAFE)	1	1	150
	Federation of Cooperatives for Marketing and Various Services (FECOMERQ)	1	1	500
	Banco de los Trabajadores (Workers' Bank)	1	-	500
	Total	7	11	$3,298

1/ Subprojects disbursed or partially disbursed as of July, 1982.

Costa Rica	Costa Rican Cooperative for Industrial Financing (COFISA)	2	3	$1,114
	National Institute for Cooperative Support (INFOCOOP)	1	1	500
	Banco Central (Central Bank)	1	3	1,000
	Total	4	7	$2,614
El Salvador	Industrial Bank (BANDEINSA)	1	1	$500
	Financier for Agriculture (FISAL)	1	4	500
	Credit Federation (FEDECREDITO)	2	5	950
	Federation of Cooperatives for Savings and Credit (FEDECACES)	1	4	500
	Agricultural Dev. Bank (B.F.A.)	1	2	500
	Total	6	16	$2,950
Nicaragua	Central Bank (BCN/FED)	1	-	3,000
	Total	22	42	$13,842

Subloan Activities in Honduras

The Honduran Financier Bank (BANIFAN). When the project was planned, Honduran ICIs were expected to participate significantly in implementing subloans. However, one of the institutions (BANIFAN) which had contracted for subloans, went bankrupt. BANIFAN's $195,800 subloan was assumed by another ICI, BANADESA.

The Honduras National Agriculture Development Bank (BANADESA). BANADESA has also experienced financial difficulties. BANADESA has a partially disbursed subloan of $869,300 and is currently trying to overcome its problems with the help of the Honduran Government.

BANADESA has taken various measures in order to continue to serve as an agricultural bank providing credit to small farmers, as well as an ICI under the AID ROCAP loan. In our 1982 audit of the Honduran Agricultural Sector II Program, we found that BANADESA had not staffed regional offices nor increased the credit specialist staffing level as intended by that program. Substantial losses had raised the bank's deficit to the equivalent of $25 million and over half of the loans were delinquent.

Some steps have been taken to greatly improve BANADESA's financial condition. Operating costs were reduced in the first quarter of 1982, and over $20 million of payments for delinquent and other loans were recovered.

In July, the Government of Honduras authorized $57.5 million of additional capitalization, as well as refinancing of the BANADESA debt due the Central Bank. USAID/Honduras believes that these measures by BANADESA's management will help it to continue as an agribusiness financier.

The Cooperative for Savings and Credit (FACACH). The third ICI, FACACH, has received $915,000 for two subloans which have been completely disbursed. An additional subloan for $500,000 was in the process of being approved by CABEI in August 1982.

Other Honduran ICIs declined to participate in the program because they considered the credit conditions and procedures for disbursement of funds to be unduly restrictive. The risk of exchange losses in repayment of dollars was an additional deterrent to their participation, particularly since the Central Bank of Honduras has not assumed a role as guarantor of dollar repayments.

Subloan Activities in Guatemala

The Industry and Farming Financier (FIASA). A CABEI subloan to ICI FIASA for $500,000 has been completely disbursed. This subloan took two

years to work out with CABEI, and FIASA contends that the subloan application was too restrictive, detailed, and time consuming. Of the six subprojects it submitted to CABEI, four did not meet project criteria for financing. FIASA has proposed additional subprojects totaling $2.5 million to CABEI for inclusion in a subloan by the Central Bank of Guatemala.

The Central Bank of Guatemala. The Central Bank became involved when the participating ICIs were reluctant to continue obtaining subloans because of the prospect of devaluation and exchange losses resulting from repayments in dollars. The Central Bank has assumed part of the role of the ICIs by accepting the risk of devaluation. Thus the ICIs are concerned only with implementation and monitoring of the subprojects.

The Industrial Financier of Guatemala (FIGSA). FIGSA's three subloans have been completely disbursed for $1,648,200. FIGSA had an additional subloan in process for $127,000 but was unwilling to continue contracting for subloans because of the risk of currency devaluation and the exchange losses resulting from subloan repayment in dollars. FIGSA will participate in further subloan implementation only if repayment to CABEI is assumed by the Central Bank of Guatemala.

Other ICIs. Two other Guatemalan ICIs, BANCAFE and FECOMERO, had subloan financing of $650,000 which has been completely disbursed. Another ICI, the Banco de los Trabajadores, has had its initial subloan approved by CABEI for $500,000.

A potential ICI participant in the program, the cooperative FENACOAC, has been negotiating a subloan for $500,000 with CABEI for over a year. This cooperative has considerable demand for local currency financing but will not agree to repay the loan in dollars. The loan would finance inputs for small farmers, crop diversification, and crop marketing.

Subloan Activities in Costa Rica

The Central Bank of Costa Rica. The Central Bank has received a subloan of $1 million which has been partially disbursed and has assumed a major role in implementing Costa Rica's agribusiness financing under the AID loan because of the impact of currency devaluation and foreign exchange losses sustained by financial institutions. Concerned ICIs will no longer assume the risks of such losses. This was a very serious problem created for private financial institutions by the deteriorating economic situation in the country, and by restrictive Government monetary and foreign exchange policies.

At the time of our audit, the Central Bank had a $6.0 million subloan in process of agreement with CABEI. Some 31 subprojects in Costa Rica amounting to $4.2 million had been proposed under this subloan. At the conclusion of our field work this subloan had not yet been agreed upon by the Central Bank but it was approved shortly after. As indicated, greater priority is needed by CABEI to expedite the issuance of subloans.

The Costa Rican Cooperation for Industrial Financing (COFISA). COFISA had received $1,113,900 for two subloans which had been completely disbursed. However, this ICI has had serious financial difficulties and is no longer involved in the financing of agribusiness activities under the AID loan. COFISA has been a major private financing institution and an important factor in the development of Costa Rica's industrial, construction, and agricultural sectors. During the years 1975-80, COFISA made about 1,500 new loans totaling nearly $100 million. COFISA is no longer active in the AID agribusiness program due to a marked financial decline. COFISA's importance to the Costa Rican economy is evident because their borrowers employ thousands of workers. USAID/Costa Rica analysis indicates that the continued viability of COFISA debtors depends on rescheduling of their debts and continued access to credit only COFISA can provide. However, without additional capital and further rescheduling of its own debts to foreign lenders, COFISA will not survive.

In mid-1981, USAID/Costa Rica analysis of COFISA showed a considerable increase in borrower delinquency and default. This has been compounded by the impact of the currency devaluation which enabled COFISA borrowers to repay dollar-denominated debts at an overvalued official exchange rate of 8.61/$1.00, while COFISA had to obtain a moratorium on its debt payments to foreign banks.

A USAID/Costa Rica loan to COFISA of $15 million, including 5 million in local currency (colones), is the result of various analyses, financial projections and credit-demand surveys. Emphasis is to be on quick and flexible disbursement of the proposed loan with particular attention to the current portfolio and to producers of export products. With the approved loan and other sources of funds, and if various project assumptions are realized, COFISA will again be a major entity in Costa Rica financing.

The National Institute for Cooperative Support (INFOCOOP). INFOCOOP has partially disbursed its subloan of $500,000 which covers two subprojects. While INFOCOOP has not received any additional subloans, it has submitted proposals for additional agribusiness financing to CABEI now that the Central Bank is to assume responsibility for dollar repayments.

Subloan Activities in Nicaragua

CABEI and the Government of Nicaragua (GON) had not reached an agreement on the payment in dollars of a $3.0 million subloan at the completion of our field work . The GON contends that signing of the subloan was delayed for nearly 2 years because of this lack of understanding. The Nicaraguan Central Bank contended that CABEI has not complied with an agreement to fully disburse the subloan in dollars. Despite the impasse, CABEI has authorized issuance of a Letter of Credit for $835,000 for equipment and accessories for a $1.2-million poultry farm subproject.

Funds amounting to $585,000 for six other subprojects for milk production in various areas of Nicaragua had not been released. ROCAP has advised us that the subloan was agreed upon and all funds fully disbursed.

Subloan Activities in El Salvador

When the project paper was prepared in 1976 only one ICI was considered able to participate in the program. However, four ICIs have actually participated and obtained six subloans amounting to $2.95 million with $2.5 million disbursed despite the civil unrest which has beset the country. While we did not visit El Salvador, CABEI reports indicated subprojects have been implemented to improve dairy and poultry production, and to expand the fishing industry.

REGIONAL RURAL AGRIBUSINESS DEVELOPMENT PROJECT
PROJECT NO. 596-0069
LOAN NO. 596-T-016

FINANCIAL STATUS AS OF JULY 31, 1982

		Amount Approved	(000) Amount Disbursed	Undisbursed Balance
37	Subprojects totally disbursed	$7,850.3	$7,850.3	$ -
5	Subprojects partially disbursed	1,407.9	988.9	419.0
52	Subprojects approved or in process of approval with no disbursements	10,373.1		10,373.1
94	Total	$19,631.3	$8,839.2	$10,792.1

By Country

	Guatemala	Honduras	Costa Rica	EL Salvador	Nicaragua	Total
Subprojects ( ) totally disbursed	(11) $2,806.8	(7)$1,110.9	(5) $1,497.8	(14) $2,434.8	$ - 0 -	(37) $7,850.3
Disbursements on subprojects in process	- 0 -	(1) 553.2	(2) 372.7	(2) 63.0	- 0 -	(5) 988.9
Total Disbursements 7/31/82	(11) $2,806.8	(8)$1,664.1	(7) $1,870.5	(16) $2,497.8	$ - 0 -	(42) $8,839.2
Subprojects approved or in process of approval with no disbursements as yet	(14) 4,132.0	(2) 550.0	(19) 2,798.3	(7) 812.2	(10) 2,080.6	(52) 10,373.1
Total	(25) $6,938.8	(10)$2,214.1	(26) $4,666.8	(23) $3,310.0	(10)$2,080.6	(94)$19,212.3

(a) Funds remaining to be disbursed amount to $419,000.

EXHIBIT B

Regional Rural Agribusiness Development Project
Project No. 596-0069
Loan No. 596-T-016

Profile of Subprojects Approved or in Process of Approval - July, 1982

No. of Subprojects	Category	Amount (000)
13	Poultry Processing	$3,483.2
26	Dairy and Milk Production	3,086.1
1	Foodstuffs	1,275.1
3	Basic Grain Commercialization	1,209.0
5	Rubber Production	983.9
8	Agroindustrial	942.1
1	Incubator	701.3
2	Rice Production	699.4
1	Seed Production	666.3
3	Concentrates	586.4
9	Fish	491.5
22	Other Categories	5,507.0
Total 94		$19,631.3

APPENDIX A

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