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UNITED STATES INTERNATIONAL DEVELOPMENT COOPERATION AGENCY
AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

PROJECT PAPER

INDONESIA

FINANCIAL INSTITUTIONS DEVELOPMENT

(497-0341)

JUNE 1984

USAID/JAKARTA

PROJECT AUTHORIZATION

INDONESIA

FINANCIAL INSTITUTION
DEVELOPMENT PROJECT
PROJECT NO. 497-0341

1. Pursuant to Section 103 of the Foreign Assistance Act of 1961, as amended, I hereby authorize the Financial Institution Development Project for Indonesia, the "Cooperating Country", involving planned obligations of not to exceed $15,500,000 in loan funds and $3,000,000 in grant funds over a two year period from date of authorization subject to the availability of funds in accordance with the A.I.D. OYB/allotment process, to help in financing foreign exchange and local currency costs for the project. The planned life of the project is seven years from the date of initial obligation.

2. The project consists of assisting the Government of Indonesia to increase rural off-farm employment through (1) support of the development of local rural credit systems that provide financial intermediation for village residents at reasonable cost, (2) production of loan portfolios of employment generating activities, primarily off-farm and (3) promotion of savings mobilization programs. Project funds may be used for technical assistance, training, commodities, capitalization costs, and other project operations costs.

3. The Project Agreements which may be negotiated and executed by the officers 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.

4. a. Interest Rate and Terms of Repayment

The Cooperating Country shall repay the Loan to A.I.D. in U.S. Dollars within forty (40) 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 (a) two percent (2%) per annum during the first ten (10) years, and (b) 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 Commodities, Nationality of Services.

Commodities financed by A.I.D. under the project shall have their source and origin in the Cooperating Country or, if loan-funded, in countries included in A.I.D. Geographic Code 941, or if grant-funded, in the United States except as A.I.D. may otherwise agree in writing. Except for ocean shipping, suppliers of commodities or services shall have their nationality in the countries included in Code 941 or Indonesia if loan-funded, and if grant funded, shall have their nationality in the United States and Indonesia, except as A.I.D. may otherwise agree in writing. Ocean shipping financed by A.I.D. under the project shall, except as A.I.D. may otherwise agree in writing, be financed only on flag vessels of the United States, if grant-funded, or Indonesia and Code 941 countries if loan-funded.

c. Conditions Precedent to Disbursement for Project Activities Other Than Technical Assistance and Pre-Implementation Activities.

The GOI will provide the following:
(a) evidence that the GOI has assigned at least five full-time professionals to the BPD Tingkat I team in each of the provinces assisted by this Project, and (b) evidence that the GOI has established and staffed a team for rural credit in Bangda, Ministry of Home Affairs, with at least two full-time professionals.

d. Condition Precedent to Disbursement of Funds for System Capitalization.

The GOI will provide the following:
(a) evidence of the procedures established for the transfer of funds between the Ministry of Finance and the respective BPD's and for the transfer of those funds to participating units, and (b) evidence that the GOI has taken the necessary steps to allow village-based credit systems assisted by this Project to accept voluntary savings from borrowers and non-borrowers and to safeguard such savings through procedures reflecting unit performance.

e. Condition Precedent to Disbursement of Funds for Computer-Related Equipment.

The GOI will provide an assessment of BPD computer needs in West Java, Central Java, and West Sumatra.

f. Additional Special Covenants.

The GOI shall agree to the following additional Special Covenants: (a) to structure accounting practices and interest rates of village credit systems under this project to insure their financial viability, including procedures to reserve funds for loan losses and to write-off uncollectable loans, and (b) to ensure that the Badan Pembinaan Pembangunan Kredit Pedesaan will meet at least once a year to review performance of each of the village credit systems and to consider adjustments based on performance, with the paramount criterion being financial viability.

Signature: William P. Fuller
William P. Fuller
Mission Director

Date : 23/5/84

Clearances: PRO:DZvinakis:
EED:TMYers:
FIN:RMcClure:
DD:RKClark:

Drafted:LA:LChiles:05/09/84, mai

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AGENCY FOR INTERNATIONAL DEVELOPMENT

PROJECT DATA SHEET

1. TRANSACTION CODE: A (A = Add, C = Change, D = Delete) — Amendment Number: ______ — DOCUMENT CODE: 3

2. COUNTRY/ENTITY: Indonesia

3. PROJECT NUMBER: 497-0341

4. BUREAU/OFFICE: ASIA — 04

5. PROJECT TITLE (maximum 40 characters): Financial Institutions Development

6. PROJECT ASSISTANCE COMPLETION DATE (PACD): MM 05 DD 31 YY 91

7. ESTIMATED DATE OF OBLIGATION (Under 'B:' below, enter 1, 2, 3, or 4)
A. Initial FY 84 — B. Quarter 3 — C. Final FY 85

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

A. FUNDING SOURCE	FIRST FY 84 B. FX	C. L/C	D. Total	LIFE OF PROJECT E. FX	F. L/C	G. Total
AID Appropriated Total	10,970	5,530	16,500	12,970	5,530	18,500
(Grant)	(1,000)	(–)	(1,000)	(3,000)	(–)	(3,000)
(Loan)	(9,970)	(5,530)	(15,500)	(9,970)	(5,530)	(15,500)
Other U.S. 1.						
Other U.S. 2.						
Host Country	–	1,500	1,500	–	9,250	9,250
Other Donor(s)						
TOTALS	10,970	7,030	18,000	12,970	14,780	27,750

9. SCHEDULE OF AID FUNDING ($000)

A. APPRO-PRIATION	B. PRIMARY PURPOSE CODE	C. PRIMARY TECH. CODE 1. Grant	2. Loan	D. OBLIGATIONS TO DATE 1. Grant	2. Loan	E. AMOUNT APPROVED THIS ACTION 1. Grant	2. Loan	F. LIFE OF PROJECT 1. Grant	2. Loan
(1) FN	240B	240	240			3,000	15,500	3,000	15,500
(2)									
(3)									
(4)									
TOTALS						3,000	15,500	3,000	15,500

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

11. SECONDARY PURPOSE CODE

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

A. Code	BR	BL	PART	–		
B. Amount						

13. PROJECT PURPOSE (maximum 480 characters)

(1) To support the development of existing local rural credit systems that provide financial intermediation for village residents at reasonable cost, (2) to produce loan portfolios of employment generating activities, primarily off-farm and (3) to promote savings mobilization programs.

14. SCHEDULED EVALUATIONS
Interim MM 06 YY 86 — MM 06 YY 88 — Final MM 01 YY 91

15. SOURCE/ORIGIN OF GOODS AND SERVICES
[X] 000 [X] 941 [ ] Local [ ] Other (Specify) ______

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

17. APPROVED BY
Signature: William P. Fuller
Title: Director USAID/Indonesia
Date Signed: MM 05 DD 22 YY 84

18. DATE DOCUMENT RECEIVED IN AID/W, OR FOR AID/W DOCUMENTS, DATE OF DISTRIBUTION: MM DD YY

AID 1330-4 (8-79)

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Financial Institutions Development Project

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Annexes

I. National Jakarta Based Agencies:

BI	Bank Indonesia
DEPARTEMEN DALAM NEGERI	Ministry of Home Affairs
DEPARTEMEN KEUANGAN	Ministry of Finance
BAPPENAS	National Level Planning and Coordinating Agency
BANGDA	Director General of Regional Development located in Ministry of Home Affairs

II. Provincial Agencies:

BAPPEDA	Provincial Level Planning and Coordinating Agency
BANK PEMBANGUNAN DAERAH (BPD)	Provincial Development Bank
BADAN KREDIT KECAMATAN (BKK)	A project-supported, rural credit system located in Central Java
BANK KARYA PRODUKSI DESA (BKPD)	A project-supported, rural credit system located in West Java
LEMBAGA PERKREDITAN KECAMATAN (LPK)	A project-supported, rural credit system in West Java
LUMBUNG PITIH NAGARI (LPN)	A project-supported, rural credit system located in West Sumatera
KABUPATEN	A district-level administrative and geographic unit
BUPATI	Head Government official in a kabupaten
KECAMATAN	A sub-district-level administrative and geographic unit, located just below the kabupaten.
CAMAT	Head Government official in a kecamatan
DESA	A village
LURAH	A village administrator
PENGAWAS	A supervisor and/or auditor
PETUGAS	Line personnel, such as assistant managers, bookkeepers, cashiers, loan officers
KEPALA UNIT	Manager of a bank unit such as a BKK, LPK, BKPD, LPN
INSPECTOR MUDA	A district auditor/supervisor based in a kabupaten and reporting to the Bupati
TINGKAT I (TK I)	Provincial level
TINGKAT II (TK II)	District level
CABANG	A branch of the BPD located usually at the kabupaten
UNIT	An autonomous financial institution such as the BKK, LPK, BKPD, or LPN located at or below the Kecamatan level

III. Other

GOI	Government of Indonesia
DUP	A GOI Project Proposal
DIP	A GOI Implementation Order (an approved DUP)

I. SUMMARY/INTRODUCTION OF THE PROBLEM

The Financial Institutions Development Project is a US$27.8 million project to strengthen the ability of four existing, village-based credit systems in West Java, West Sumatera, and Central Java to extend credit to borrowers, to expand loan portfolios beyond trader credits to include small entrepreneurs and to mobilize voluntary savings. The project provides training, technical assistance and equipment to develop the staff and operational procedures of the local credit institutions and to forge a closer link between them and provincial banks responsible for their supervision,training and inspection. The project also provides funds to capitalize individual units to help expand loan portfolios.

The project will work through two ministries, the Ministry of Finance and the Ministry of Home Affairs, and the provincial development banks (Bank Pembangunan Daerah--BPD) to strengthen credit systems that have already demonstrated a potential for expansion--the Bank Karya Produksi Desa (BKPD) and Lembaga Perkreditan Kecamatan (LPK) in West Java, the Badan Kredit Kecamatan (BKK) in Central Java and the Lumbung Pitih Negara (LPN) in West Sumatera. Each are owned by the local government and are referred to in this paper as village credit systems.

The project responds to a serious challenge faced by Indonesia--the efficient mobilization and use of domestic resources to finance employment opportunities for an expanding, largely rural, workforce. The need for new jobs, and for the credit required to support the enterprise development necessary to create them, is acute in Indonesia's heavily populated rural areas. The absence of institutions providing reliable credit at a reasonable price remains a major constraint on enterprise development in rural areas. Credit that has reached rural areas has been subsidized, and although encouraging agricultural production, it has distorted the real cost of capital and reduced institutional responsibility to preserve and increase capital.

The credit systems included in this project attempt to provide financial services to village borrowers on a self-sustaining basis. The Financial Institutions Development Project will help them expand by strengthening links to provincial development banks which in turn will provide supervisory guidance, technical expertise, training and access to capital. In doing so, the project will demonstrate elements of viable, self-financing local credit systems which may be applicable elsewhere and provide the GOI with detailed procedures and appropriate training strategies for further development of rural credit institutions throughout the country.

The provincial systems selected reflect different histories and different degrees of organizational maturity. They are similar, however, in their ability to deliver credit to the village and their potential for self-financing operations. To realize that potential they will need to resolve issues basic to improved financial performance which have been set as sub-objectives of the project: establishment of strong accounting and management information systems; a strong link with the provincial development bank to provide training, supervision and access to credit; an overall pricing structure reflecting true costs; expanded programs to mobilize rural savings; and a more efficient system to deliver rural credit. Recognizing their differences, the project will build on their strengths and respond to the various needs of each of the provinces involved. Because of system variations, the project will be phased by province to allow each system to consolidate organizational and procedural changes with BPD and unit managment development before expanding to undertake new services.

The end of the project will attempt to have the units from all four systems operating as a self-sustaining basis. To do this the BPDs will establish performance criteria and allow qualified units to conduct: a) further expansion to cover more villages by setting up more village posts, b) savings mobilization programs, and c) a small industries loan program.

Project outputs will include four village credit systems operating in three provinces. Each will have more standard loan, administrative and accounting procedures; a simplified, internally consistent, and usable management information system; formal administrative and financial linkages with the provincial development banks; and trained banking personnel both in the units and in supervisory and inspection positions within three BPDs.

II. PROJECT RATIONALE

As outlined in the Mission's CDSS, during the next decade Indonesia faces a major challenge -- the efficient mobilization and allocation of domestic resources to create jobs. Through the 1980's Indonesia will add two million people to its labor force annually. Even during the high growth years of the late 1970's, the Indonesian economy was unable to absorb the growing number of workers coming onto the labor market. From the latter half of the 1970's through 1981, Indonesia's gross domestic product (GDP) growth rate averaged more than seven percent per annum while per capita income increased five percent annually. Despite this growth, unemployment and underemployment remained high, and per capita income--approximately $520 per year--remained below other ASEAN countries.

The employment situation is unlikely to improve. Highly dependent on oil revenues--about 70 percent of GDP--GDP declined to about two percent in 1982. It has risen sharply in 1983 to between 3 and 5 percent because of increased food production and oil sales, but nevertheless, remains below the boom years of the 70's and is likely to remain so for the foreseeable future.

The brunt of this slower growth is borne in rural areas which have 83 per cent of all Indonesian households. Increasingly these households are forced to live on progressively smaller farms or to leave agriculture altogether, but the alternatives to agriculture are constrained by inadequate financial services. USAID and World Bank funded research shows that nearly 60 per cent of rural household income comes from various forms of off-farm employment, yet off-farm activities have scant access to institutional credit. The current recession and the resulting decline in public expenditures may have reduced discretionary income and lowered demand for goods and credit, but it has also resulted in an increasing number of un- or underemployed rural workers forced to turn to self-employment for their livelihood thus increasing demand for credit.

The Rural Setting: AID's experience in PDP (Provincial Development Project), evaluations such as DAI's study of the BKK system in Central Java, and other donor studies show a majority of rural people earn most of their income from non-agriculture activities such as trading, handicrafts, food preparation and retailing. An analysis of these activities shows:

1. The activities can be done with a little capital and a relatively large amount of labor.
2. The addition of credit (less than Rp. 50,000) spurs entrepreneurship and increases returns per work-day.
3. The activities produce a profit and a cash flow from which credit can be repaid.
4. Since the borrowers are known in the village, borrowers can be identified at minimum expense.
5. Borrowers repay loans on time since the chief incentive for repayment is confidence that credit will be available again, possibly in larger amounts.

In rural areas the family engages in changing income generating activities over time as different opportunities become available. A wife engages in rice planting and harvesting for a few weeks each year, but during the rest of the year she may manufacture simple handicrafts or sell small food items. The husband may farm a small plot of land part time in the wet season, work as a tukang kayu (carpenter) part time in the dry season, and work with his wife manufacturing bamboo products when no other work is available. This ability to engage in different activities as the micro-economic situation changes gives basic economic security as the family constantly shifts labor and capital to the activity with the highest return. Such shifts will be enhanced by access to rural credit through intermediary financial institutions supported under this project. Without such institutions taking and relending surplus funds only limited means are available of reliably moving funds from one family enterprise to another or for guarding savings until needed. Instead, savings will remain in gold or crops or some other non-productive form of investment.

The Need for Financial Intermediation

The need for improved financial intermediation in Indonesia is indicated by the low ratio of money (M-1) to Gross Domestic Product (GDP) -- 19 per cent in Indonesia compared to 40 and 53 per cent for India and Malaysia respectively. Savings as a percentage of GDP is also low -- 2% in Indonesia compared with 5% and 6% in the Philippines and Thailand. World Bank surveys show a savings growth rate between 1974 and 1980 of only one-half of GNP growth. The lack of formal savings is particularly apparent in the household and informal business sector. The World Bank estimates household income accounts for 70 percent of GDP, but formal household financial assets are less than 3% despite a strong propensity to save. Recent studies show households in Indonesia saving 20 percent of their income on average with households in the upper quartile saving as much as 40%, a level similar to other rural areas in Asia. According to a recent USAID-sponsored evaluation, most of this savings is held in the form of property, gold, rice and other commodities.

The lack of formalized savings has many causes. Until recently negative interest rates on savings deposits hindered deposit mobilization. Perhaps most importantly, formal banking institutions in Indonesia are highly centralized and have a limited rural presence. The central bank, Bank Indonesia, the five state banks and the Government development banks control more than 90 per cent of all financial assets. Foreign banks and private commercial banks account for a little over 5 per cent. All of these banking institutions are essentially urban. State banks operate approximately 140 branches each, but most are in provincial capitals or in major populations centers at the district level. Foreign commercial banks are legally restricted to Jakarta, and few of the 70 private national commercial banks extend branches beyond major cities. Most private national banks consider lending to villagers as risky and the development of a large branch network as beyond their institutional capabilities.

Until recently government credit programs reaching the sub-district or the village have been heavily subsidized with a retail cost of about 12% annually compared with 22% from private institutions. The subsidies inhibited development of self-sustaining financial institutions by distorting the institution's real cost of funds and allowing those institutions to ignore the genuine potential of generating savings through offering competitive rates. The Government's development goals of aiding economically weak borrowers, stimulating the adoption of agricultural inputs, and redistributing funds often have taken precedence over establishing institutions that require strict repayment, mobilize savings or generate profit. The GOI, aware of the implications of its past policies, has instituted changes in monetary policy. In June 1983 they lifted the credit ceilings imposed on state banks and freed restrictions on interest rates allowing banks to establish rates reflective of market demand.

Improved operations of credit institutions in rural areas also have been hampered by lack of appropriate procedures and institutional support, trained personnel, transportation and equipment. Standard commercial practices such as aging overdue loans and maintaining reasonable reserve requirements for overdue loans are overlooked because of other policy objectives, lack of trained staff, or lack of adequate management information systems.

Besides limited formal credit, fragmented informal credit systems operate throughout Indonesia as reflected by the high level of rural savings compared to savings of formal institutions. Moneylenders' credit is usually tied to the distribution of products with its comparative advantage resting on providing not just finance but also complementary marketing channels. Traditional informal community credit groups include the arisan and simpan pinjams. The arisan is a group of people, usually women, who pool savings and then receive use of the money through a simple rotation by lottery. Simpan-pinjams are usually arisans that have taken on a lending function and require much more sophistication, discipline, and organization than an arisan. Land/labor-linked credit is another important part of the informal credit system and includes forward sale of crops, land rentals in advance, and land use contracts equivalent to a mortgage with a variable maturity. Although meeting some needs, the inability of these systems to be integrated into an efficient network limits the transferability of resources to opportunities with the highest return.

Formal Rural Credit in Indonesia

Three formal channels exist for credit to reach the village in Indonesia:

1) Bank Rakyat Indonesia: The vast majority of credit to villages comes through the BRI, administered through 3500 Bank Unit Desas (village unit banks) operating at the sub-district level. The BRI program operates about 279 different credit programs (KIK/KMKP, KIB, KUBEDES, etc.), each with their own terms, procedures, reporting and bookkeeping requirements. Until recently the BRI system depended on government subsidies through low interest (3-4%) liquidity credits from the central bank. The low rate allowed BRI to extend low interest credit -- around one per cent per month - to priority areas while insuring a high spread (the difference between the rate charged to BRI by the central bank and the rate charged the borrower by BRI). This low rate, however, discouraged BRI from developing programs to mobilize savings. Recently the GOI announced a series of major reforms for the BRI system in part based on the changes instituted on the credit systems supported under this project. Despite these changes, the BRI system remains limited by a branch system which reaches only about 14 percent of the rural population and the need to retrain and revitalize many dormant branches.

2) <u>Cooperatives</u>: Until recently the major credit program administered by the Koperasi Unit Desa (village unit cooperative) has been the Kredit Candak Kulak (KCK) that provides short-term, three-month loans at interest rates of about 1.5 percent per month. In 1980 about 6.3 million borrowers had outstanding loans totalling 50 billion rupiahs (US$50 million). Default rates were high, and the system, dependent on budgetary transfers through the Ministry of Cooperatives, did not mobilize savings or charge interest rates sufficient to cover operating costs. Most KUD units are located at the sub-district level. They have recently been assigned the responsibility of administering the large agriculture production input program BIMAS which also has low interest rates and serious repayment problems.

3) <u>Local Banking Institutions</u>: The formal credit channels judged potentially most effective in reaching the village level and supported by this project are local financial institutions operating as indpendent units at the sub-district level. They are the Badan Kredit Kecamatan (BKK) in Central Java, the Bank Karya Produksi Desa (BKPD) and Lembaga Perkreditan Kecamatan (LPK) in West Java and the Lumbung Pitih Nagari (LPN) in West Sumatera. The BKK, LPK and LPN are linked formally or informally to the Provincial Development Banks (BPD's), which are under the Home Affairs Ministry. The BKPD is technically attached and supervised now by the BRI.

Traditionally, the three BPDs have played a relatively small role in rural credit, serving instead as a fiscal management body for provincial authorities. In the 1960's a number of BPDs began providing supervision, technical assistance, training and funding to provincial credit programs. These local programs--BKK, LPN, and BKPD--promoted short-term higher cost credit. A recent evaluation shows the typical borrower is female using the working capital loan to buy raw materials for production, or goods for resale. High repayment rates of the areas surveyed indicated most borrowers use their loans productively to generate a cash flow to cover interest charges. The higher interest rates, conservative lending practices and relatively good repayment rates enabled several units to operate profitably.

Operating systems are simple. In the BKK system, loan officers take satchels of money on a regular round on village market days making loans and collecting payments. In the LPN system the unit is open at set times every other week. By operating at the local level the institution reduces overall transaction costs for small loans to the individual borrower, and this explains why borrowers have been willing to pay higher nominal interest rates.

The BKK system in Central Java now operates 491 units with 1,800 weekly posts. Also, 103 LPN has 561 units. The systems are at various stages West Sumatera the LPN has 561 units. The systems are at various stages of development and operational efficiency, but share a number of characteristics to be supported and strengthened under this project:

1. In varying degrees they lend without subsidy and borrowers can rely on them as a source of funds when they need additional capital.
2. They respond to all kinds of credit requests and recognize that lending is done against the aggregate cash flow of a family.
3. Loans depend not on collateral but on character references from local officials.
4. Since small increments to a family's capital bring relatively high returns, the first loan to a new borrower is small. If the borrower repays the loan, a credit rating is established permitting loan of larger amounts in the future.
5. The bookkeeping system is designed for the education level of the staff and contains a limited number of different standard loan terms.
6. Loans are booked as close to the village as possible to reduce borrower transaction costs.
7. There is personal contact with local government officials responsible for identifying new borrowers. The local official can inquire about any overdue loans and hold down the bad debt rate. The lending officer can also process more loans in a shorter time.
8. Poor individuals have access to these credit facilities.

Expanded support under this project will allow the deepening and improvement of these four systems. Support is warranted by indicators of past financial viability and the potential for future growth. Existing systems presently are unable to meet an increasing demand for credit and credit units frequently stop lending because of a lack of loanable funds. Potential borrowers must wait until others repay old debt before the institution can extend new loans. Furthermore, despite government supported credit programs, most people do not have access to reliable financial services.

Central Java with its population of 25 million people, for example, is probably the most heavily serviced rural financial market in Indonesia. Three formal local-level credit institutions dominate cash credit in Central Java: the Bank Unit Desa (BUD) with 707 units; the Koperasi Unit Desa (KUD) with 590 units; and the Badan Kredit Kecamatan (BKK) with 491 units and 1,800 weekly village posts. Cumulatively, these partially serve only 2881 of the 7998 rural villages in Central Java. For even those relatively few villages served, limited capital prevents the institutions from meeting demand. Experience in West Java with its population of 27 million is similar. 40 percent of the 3727 rural villages (nearly 10 million people) are not served by any formal rural financial institution. The main village credit vehicles in West Java are the Bank Unit Desa (BUD), Kooperasi Unit Desa (KUD), Lembaga Perkreditan Kecamatan (LPK) and Bank Karya Produksi Desa (BKPD). To date these institutions have only been able to touch a small fraction of potential customers. In West Sumatera as well the prime factors holding back lending have been a lack credit outlets and insufficient capital to meet demand.

This summary of sources of rural credit in Indonesia confirmed by Mission experience through other projects points to strengthening local established credit institutions as the approach most likely to build a self-sustaining village credit system to encourage small enterprise development. Centrally funded credit programs depend on subsidies that discourage savings mobilization and loan recovery and even where they operate effectively, they stop at the district level. Informal credit programs, while flexible, are expensive and often beyond the reach of the rural borrower. After working with a variety of credit programs and extensive experience with the BKK program in Central Java, the Mission has concluded strengthening the existing units of these local credit institutions has the potential to significantly improve the present low level of financial intermediation in the Indonesian rural sector.

III. TECHNICAL AND ORGANIZATIONAL ANALYSIS

The end of project status and the project's expected outputs will be affected by the resolution of major organizational issues facing the village systems and the provincial development banks: the relationship of the village credit system to the provincial government and development bank, the relationship of the village system and provincial development bank to the major financial agencies—the Ministry of Home Affairs, Bank Indonesia and the Ministry of Finance, and the internal organization of the each local credit system. At each of these organizational levels, questions of supervision, credit allocation authority and control must be resolved.

Resolution of these organizational issues and operational questions will grow out of the project's ability to build on existing control and supervision procedures and the current relationships between village, provincial and national institutions. The pace of the project in each province will respond to the level of development of the respective village institutions. A description of the institutions follows:

Badan Kredit Kecamatan: The provincial development bank, the BPD, was established in Central Java in 1963 and now has 602 employees and 16 units operating in 29 kabupaten (See Annex D for a summary of the banks current financial position and organzational structure). In 1972 the provincial government of Central Java began developing a rural credit system partially following the general model established in the BKPD system of West Java to provide productive credit for off-farm income generating activities. BKKs were established throughout the province with initial capital provided by the provincial government. Management of the BKK system is currently vested in the Bureau Pengawasan (the Control Bureau) of the BPD. A special sub-bureau staffed by eight people has prime responsibility for BKK supervison(see organizational structure in Annex D).

Currently 491 BKK units operate with approximately 1800 weekly posts. Further posts and reactiviation of dormant units are necessary. Although operating under the provincial government and the BPD, each BKK is locally administered and financially autonomous. The BPD provides financial, technical, inspection and training services which the proposed project will expand.

The financial viability of the BKK, while fragile, is real. Assets are used productively with most in outstanding loans and interest rates have generated sufficent profits to allow a system expansion. From 1972 to 1982 borrowed capital in BKK operating units grew 19 percent annually. Outstanding loans, minus payments overdue, and savings have both grown at more than twice the average yearly inflation rate of 16.8 percent since 1972. High profits have enabled equity to grow at a 55 percent compounded annual rate since the program began. The BKK program has also increased its reliance on internal profits as a source of equity, and there is now a need to refine and rationalize the accounting system which tracks those profits. Client savings account for almost twenty percent of BKK funds. New programs will have to be designed if that percentage is to be increased.

Based on available accounting data the quality of the loan portfolio of reporting BKK's is generally good. Program capital has been used well in the BKK program with more than 90 percent of assets held in outstanding loans and an average loan turnover rate of 2.6 times annually. Excluding loans more than six months overdue, six percent of outstanding loans were delinquent in June 1982. This compares favorably with the agricultural production-oriented BIMAS program where more than 60 percent of loans are overdue and probably unrecoverable. Only 14 percent of current outstanding loans in the BKK program are more than six months overdue and could be considered unrecoverable. This includes more than ten years of loans, most in the early years of operation. Overall, clients missed approximately 32 percent of payments due, but many delinquent borrowers frequently made a balloon payment at the end of the loan. The BKK's consolidated balance sheet and income statement is presented in Annex D.

The current BKK classification system, described in Annex C shows 57 units (12% of total units) as Class One, 91 units(19%) as Class Two, 128 units (26%) as Class Three, 68 units (14% as Class Four, and 143 units(295) as Class Five. Many of the Class Five units have not operated for some time or only at modest levels. Recent evalutions show that the program has a positive impact on clients both for family income and alleviating underemployment.

The BKK nominal interest rate structure of 2 to 4.8 percent per month is effectively much higher since interest is charged on the original loan amount rather than on a declining balance. Annex D compares the monthly nominal and effective interest rates for the six different types of loans under this project. The BKK rates are greater than the inflation rate and, given high repayment rates, promote growth of the loan portfolio in real terms. The most popular loans, those with a weekly and monthly repayment period, have effective monthly interest rates of 6.9 percent and 5.3 percent respectively. These rates, while high, are required to cover costs, and evaluations indicate the returns are sufficient to cover borrower costs and produce profit margins. Despite the effectiveness of BKK, its growth has been hindered by a lack of capital, technical and administrative capacity, and transportation.

Lembaga Perkreditan Kecamatan and Bank Karya Produksi Desa-West Java: Established in 1961 the BPD in West Java now has 19 branches and 602 employees. The bank's financial statements are outlined in Annex D. The LPK developed in the western part of West Java where there were no village banking services. The system has an estimated $700,000 worth of loans outstanding but this figure is unaudited. The LPK structure gives limited authority to the BPD and a great amount to the kabupaten government. For example, under current regulations the kabupaten government owns individual units; the BPD gets inspection reports indirectly through the provincial Government and remains divorced from policy initiatives and any major training efforts. Most importantly the inspection function is performed by the Inspector Muda, an official appointed and supervised by the kabupaten government. In addition, parallel BPD inspection authority is understaffed while Inspector Muda authority is broad but undertrained and linked to the kabupaten whose interests, understandably, are political as well as financial.

The BKPD system was one of the first rural banking institutions in the country. Of the total 225 BKPDs on paper, approximately 200 are in operation. In 1972 the GOI, fearful of a too-rapid expansion of rural banks stopped the establishement of new BKPDs, and in 1972 supervison was transferred to the BRI where it remains. Despite an unaudited lending portfolio of approximately $2.6 million, the BKPD's have not grown and lending viability remains more a function of individual units.

This project will shift supervisory and inspection responsibility over the LPKs to the BPD and away from the kabupaten government. In the BKPD system operational authority will shift away from the BRI to the BPD. Provincial and BPD officials have stated their intent to designate full time pengawas located at BPD kebupaten offices to supervise LPK and BKPD credit activities. The BPD in Bandung will recruit and train new staff to perform inspections as described in this section in project outputs. It will also mean that the Badan Pembina, an essentially independent coordinating body in the provincial organizational structure concerned with general questions of credit will not be involved in daily operational or management responsibility of the project. It will also mean that the BPD will strengthen its staff. In comparison to the eight people (five full time and three inspectors) in West Java, for example, the BPD in Central Java now only has three people. The number will be increased and a special LPK/BKPD section be created within the BPD.

Lumbung Pitih Negari-West Sumatra: The BPD-West Sumatera was established in 1962. The bank has 12 branches covering the province's eight kabupatens. An organization chart and basic financial statements are presented in Annex D. In 1982 the BPD had 343 employees and a credit volume of Rp. 26,110,569,000, assets of Rp. 36,141,021,000 and earnings of Rp. 1,646,941,000.

The Lumbung Pitih Negari (LPN), monitored by the BPD, is a community based, non-government controlled, credit system based on the Negari organization indigenous to West Sumatera. It has been in existence since the early part of the century as a special, clan-based, administrative organization covering approximately eight villages each. There are 562 LPNs throughout West Sumatera with 257 having a functioning lending operation; 89 receiving additional capital from the BPD. Forty-one LPNs are classed as viable under the BPD's generous classification standards, 180 are considered as poor performing and data is unavailable from 87 others. A consolidated balance sheet in Annex D shows a loan portfolio of 1.2m Rp.(or US$ 1.2 million) funded largely by involuntary savings and retained earnings. The lending program has simple administrative procedures though figures of loan portfolio turnover are difficult to obtain. Each LPN has a board of directors, usually of five members, elected every four years. Daily operations are run by three staff working part time, usually but not always consisting of a head, a treasurer and secretary. Units are open for business on average once every two weeks, and because there is no village post system, full market coverage in the LPN is limited. There is a small fee to join the LPN, and membership varies between 180-400 persons per Negari.

Loan ceilings are set by the respective boards with the amount depending on past loan performance and length of Negari membership. Money is usually lent for a six months at 10 % p.a. This, together with mandatory savings of 10% of the loan, gives an effective lending rate of approximately 40% on an annual basis. Loans either require collateral or are small uncollateralized trading credits and are processed by the manager who obtains lurah (village chief) approval. If the borrower is 10 days past due, he is fined at a rate of .02 percent for each late day after that 10 days period. Bad debt is minimal.

Administrative costs are low; office space is shared with the Nagari office, and staff are paid 20 % of the LPN's annual net income. No interest is paid on savings; instead, depositors divide 45% of yearly profits. Basic figures representing a compilation of individual LPNs prepared by the BPD are available but lack important informational requirements such as aging of overdues, unit profitability, and complete cost estimates.

IV. PROJECT GOAL, PURPOSE AND END OF PROJECT STATUS

The goal of the Financial Institutions Development Project is to encourage enterprise development, increase productivity and generate employment opportunities in rural areas. The purpose is to 1) support the development of existing rural credit institutions that provide financial intermediation for village residents at reasonable cost, 2) produce loan portfolios of employment generating activities, primarily off-farm and 3) promote savings mobilization. The end of project status is the development of four self-sustaining, locally-oriented, financial systems that mobilize savings and extend credit. The specific institutions targeted for assistance are:

Institution	No. of Units	Province
Badan Kredit Kecamatan	491	Central Java
Bank Karya Produksi Desa	217	West Java
Lembaga Perkreditan Kecamatan	103	West Java
Lumbung Pitih Negari	561	West Sumatera

The project is a first step toward an improved rural banking system and provides an expanded model for the GOI and ultimately for the private sector. Each system has reached a certain level of managment efficiency and has different needs, but each has a tradition of serving customers in the village to reduce transaction costs, an established customer base, an interest rate structure offering the possibility of financial viability, and a record of policy flexibility. These institutions will be more deeply integrated into the existing provincial banking network of the Bank Pembangunan Daerah (BPD) and increasingly fund their loan portfolio by using surplus, market-priced, BPD funds and locally-generated savings. Their portfolios also should mature to include small-industry credits as well as trader credits.

Achieving the goal and purpose will require the development of an internally consistent system of accounting and operations, appropriate training programs, and professional staff development at the BPD for supervisory control for each province. Inputs and implementation schedules will be set to the appropriate level for each system to fit their individual stage of development. Units will receive additional training capital and be monitored by financial criteria and higher level auditors.

While the end of project status will be to create a self-sustaining and expandable system for mobilizing and delivering credit in three specific provinces, the lessons learned from this project should be applicable to the government's efforts in extending the village credit to other provinces as well. To achieve the end of project status first requires a description of the inputs AID and the GOI will finance.

The consolidated project budget is as follows:

Local Currency/Foreign Exchange Budget ($000's)

	A I D		G O I		TOTAL
	LC	FX	LC	FX	
Technical Assistance	1,210	4,290	-	-	5,500
Training	7,360	90	3,000	-	10,450
Commodities and Equipment	500	250	2,750	-	3,500
Capital	3,000	-	3,500	-	6,500
Contingency	900	900	-	-	1,800
Total	12,970	5,530	9,250	-	27,730

V. PROJECT INPUTS:

A) Training Support: Approximately 5,300 employees will be trained or retrained during the life of the project in order to create and maintain a system of efficient but widely dispersed financial units. Each BPD will develop its in-house training capability to provide a continuing training program that provides all operating personnel in the project with periodic training up-dated regularly. AID funds will be used to support this significant and long-term training effort. The GOI will make funding contributions for the development of training centers at the BPDs and toward personnel training costs. Specific training programs for new petugas, experienced petugas, pengawas, camats, kepala units, and lurahs will be developed and will include formal classroom study, informal study, comparative study, and apprentice programs. The AID portion of the training budget will also sponsor one trip to the Philippines, Taiwan and Korea to observe comparable rural credit programs with applicability to the Indonesian program. Approximately 30 people will go over the life of project, the majority coming from the participating BPDs. The team will spend approximately three weeks visiting programs in these countries observing programs and evaluating which elements might have applicability to Indonesia. The project will also fund yearly workshops covering various operational issues of interest to managers of small scale rural financial systems. Such a workshop would include presentations of papers, group discussions, and field visits related to a predetermined subject or theme. Participants would include Ministries of Home Affairs and Finance, BAPPENAS, Bank Indonesia, BPDs, and operational personnel from BKKs, LPDs, BKPDs and LPNs. These workshops will be held at the BPDs in Central Java, West Java, and West Sumatra on a revolving schedule

An estimated budget for training follows:

Province	Number of Trainees	Estimated Cost
West Java	9190	$2,470,213
Central Java	9365	3,407,600
West Sumatera	5134	2,585,012

B) Technical Assistance:

1. Technical assistance (TA) under this project will work closely with the respective provincial development banks to help develop their management, supervisory and inspection capability. TA will provide resident and short-term specialists to work with the provincial banks to create and improve management information systems (MIS), savings programs, accounting systems, and curriculum design to support a large training effort.

The initial tasks of the BPDs working with technical assistance will be to review accounting procedures in use, consolidate the financial position of the sub-systems assisted, classify participating units and conduct an initial assessment of computer requirements to support MIS development. Later, the BPDs with TA will develop the capacity of individual units and the BPD to monitor larger types of loans. The bulk of technical assistance will be provided through a competitively-bid AID direct institutional contract with a firm experienced in rural credit and accounting. The contract will finance resident technical advisors in each province for four years and have forty-person months of special short-term assistance with an option to extend. Technical assistance will have the following elements:

a) Resident advisors will reside in West Sumatera, Central Java and West Java for four years. Knowledge of the Indonesian language and the Indonesian financial system will be an important criteria in contractor selection. The senior team member will spend approximately a third to a half of his time in Jakarta and in provinces other than the three main project areas.

b) 40 person-months of short-term specialized assistance. It is anticipated this component will be used initially for curriculum development and training program design. Specialized assistance likely will also be required to assist the BPDs in:

i) management information system development.
ii) designing savings mobilization programs.
iii) accounting system redesign and modification where warranted.
iv) designing financial instruments to strengthening BPD linkages to Jakarta-based financial institutions.
v) a computer needs assessment of the BPDs and the BPD offices
vi) working on short-term specialized financial issues requested by the GOI.

2. An Indonesian firm will conduct the borrower viability portion of evaluations under a subcontract with the main firm and for a cost currently estimated at approximately US$100,000. Design assistance for the methodology and questionnaires used will be provided by the institutional firm, the government, and the USAID Mission's evaluation officer.

3. Approximately $250,000 or two-person years, assuming an institutional contract with overhead costs, will be set aside for specialized technical assistance needed by the GOI and not available from either the institutional or the local evaluation subcontractor but identified as necessary by the BPDs and Jakarta-based counterparts during project implementation. Some areas where assistance may be required are:

a) policy, legal and regulatory questions related to project implementation.

b) pre-feasibility and feasibility studies for project expansion into other provinces or assistance to other credit systems.

c) managerial questions related to overall BPD operations.

<u>Scheduling</u>: The scheduling of technical assistance during the project is estimated as follows:

<u>Time Period</u>	<u>Activity</u>
0 - 9th Month	Selection of technical assistance.
9th - 57th Month	Three long-term advisors resident in each BPD for four years supported by short term technical advisors.
57th - 84th Month	One long-term advisor supported by short-term advisors.
0 - 84th Month	Local firm conducts survey of borrower impact.
0 - 84th Month	Other technical assistance for specific research as identified. Approximately 24 person months or $250,000 based on similar cost experience.

C. <u>Commodities</u>: Approximately $3,500,000 worth of project commodities ($750,000 AID and $2,750,000 GOI) are estimated to be needed during the life of the project. USAID's contribution will include vehicles, limited office equipment, and computer equipment. The GOI's contribution will consist of office equipment required to reestablish units and conduct larger training programs.

1. <u>Vehicles</u>: Approximately 46 four-wheel drive vehicles are required for regional supervisors/auditors based at district-level BPD branches. Five 12 passenger vans are required for resident technical advisors and for training. The four-wheel drive vehicles

will be used to transport supervisors/auditors from kabupaten branch offices to kecamatan units and village posts and thus allow a greater number of visits. BPD's will fund purchases of motorcycles for unit loan officers to establish village posts. This will be based on procedures to be established in each province. (In Central Java, for example, the BPD has established a fund for this out of the fee structure to be established for services provided by the BPD to the village systems). The 12-passenger vans at the BPD main office will be for monitoring and training. One jeep and one van will be based in Jakarta for use by visiting advisors, the BANGDA Credit Team, and for trainees that may come to Jakarta. Vehicles will be locally assembled, four-wheel drive American Motors CJ-7 jeeps; the five 12-passenger vans will be Code 935 diesel vans. Procurement will be direct, competitive and phased as required over 24 months. The estimated distribution of vehicles is as follows:

VEHICLE PROCUREMENT PLAN

Vehicle	Province	Procurement Phasing Year 1	Procurement Phasing Year 2
Jeep	Central Java	12	-
	West Java	5	15
	West Sumatera	2	11
	Jakarta	1	-
	Total	20	26
Estimated Cost		US$170,000	US$260,000

Vehicle	Province	Procurement Phasing Year 1	Procurement Phasing Year 2
Van	Central Java	2	-
	West Java	2	-
	West Sumatera	-	-
	Jakarta	1	-
	Total	5	
Estimated Cost		US$45,000	

Total Estimated Vehicle Cost US$475,000

2. Equipment: Limited equipment for local units including typewriters, calculators and fireproof safes required by each unit will be purchased by the GOI and phased per the implementation schedule and expansion plan of each individual province. Items purchased annually will depend on the number of units that the GOI reactivates and phases into the project.

3. Computer Equipment: Equipment purchased to support a management information system will consider overall BPD needs and be phased. For example, BPD/Central Java has already acquired a microcomputer and modest peripherals. FID would increase Central Java's capabilities by adding additional storage capacity, more terminals, and extra printers. Technical assistance will help the BPD in West Java and West Sumatera to design a system compatable with their needs and where possible compatible with those used in other provinces. An assessment of information needs and computer capabilities will be done at the beginning of the project.

4. Miscellaneous: Limited AID-financed miscellaneous equipment including training equipment (overhead projectors, graphic displays, and printed materials) will be determined by each BPD as they begin a training program and identify equipment needs.

D. Funds for System Capitalization: System expansion will depend on financial performance and developing management capacity at the BPD and unit level. Capitalization flows will be based on current Ministry of Finance procedures which now support the expansion of good but savings deficient units and the reactiviation of marginally preforming ones. Funds for capitalization and expansion will be conditional on units' meeting performance criteria established by the GOI. Once criteria are established, disbursement procedures will be largely automatic and depend on a particular unit's past level of performance. Beyond a certain level, additional loan expansion is expected to come from savings, the individual unit's equity accounts less a reserve for potential losses, and normal interbank facilities at competitive rates. Unit capitalization requests will be funded from Ministry of Finance's established lines to the provinces which are now as follows:

A) Central Java Rp. 3,000,000,000 line established; 1,500,000 used.
B) West Sumatera Rp. 1,500,000,000 line established; Rp.500,000,000 used.
C) West Java: Rp.1,000,000,000(line to be established).

Drawdown of funds will be matched by AID from the capital line item of the project budget. The funds loaned by the Ministry of Finance to provinces will be per existing GOI terms—interest free, a four-year grace period and a twenty-year payback period. The fund is a special item under the aegis of the Ministry of Finance and is not under DUP/DIP funding. AID will make capital available to each province after CPs are met, a preliminary accounting and unit review is completed and a unit classification system is established in West Java and West Sumatera.

E. Contingency: The project budgets approximately $1,800,000 contingency. This will likely be used for additional capitalization requirements if the expected rate of unit growth is exceeded and for a limited number of additional vehicles and training equipment. The annual financial review will identify requirements from the contingency account.

VI. PROJECT OUTPUTS:

The following project outputs will receive attention, primarily through technical assistance and training, to achieve the end of project status:

A) Self-Sustaining BPD Training Capability: A self-sustaining training capability in the three BPDs of West Java, West Sumatera and Central Java is perhaps the most essential element to institutionalize procedures and policies supported under this project. Specific levels of job performance will be required from the approximately 5,300 rural credit employees to be either retrained or recruited if the project is to expand lending while at the same time improving loan quality. Many unit personnel require further skills development in loan appraisal, loan processing and bookkeeping and need access to relevent instructioual material or regularly scheduled training courses. This will become especially important as the more sophisticated units begin developing small industry loans and dealing with larger borrowers. FID will help the BPDs develop a training capacity in West Java, Central Java, and West Sumatera to develop annual training plans and courses based on established job descriptions, performance requirements, assessment of current needs and requirements for new services such as specialized lending for small industry. The courses will include such things as simulation, case studies and, where appropriate, apprenticeship opportunities.

Training will be based on material, methodology and experience that the respective BPDs have found effective to date but will be refined to account for variations of each particular province. Both the content of training curriculum and scheduling of unit and BPD personnel will be developed jointly by the BPD and technical advisors early in the project.

B) Improved Auditing, Inspection and Supervision: The project will strengthen supervision and auditing by assisting the BPDs to address the personnel and reorganization requirements related to major expansion of lending and savings. Assistance will include increased training for area supervisors and auditors, increased mobility with additional vehicles, and improved access to relevant financial information. The supervisor, working out of the BPD kabupaten office, will act as a motivator of sub-district unit personnel and will develop monitoring and inspection skills in order that timely managment decisions may be taken. The area auditor, at a BPD office covering several districts, will be trained to audit and analyze the financial condition of individual units. The province will designate a group of supervisors and auditors as full-time BPD employees.

Each of the BPDs will undergo limited or moderate expansion of inspection staff to enable inspectors to visit each unit of the participating systems at least monthly and to be knowledgeable in new project initiatives such as small industry lending and savings promotion. Based on MIS and accounting changes adapted during the first phase of implementation, inspection reporting formats will be revised where necessary to capture essential data on performance and profitability. Over the life of the project, an auditing reporting system will also be combined with the overall MIS requirements and may include unannounced audits. A first task in project implementation will be to assess current inspection procedures and formats and staffing levels.

C) Formal Efficient System of Savings: Despite recent reforms in the banking sector, savings mobilization in Indonesia lags behind most other Asian countries. Low interest rates, vis-a-vis the inflation, and the safety of customer's deposits prevent the mobilization of sufficent savings to finance loan demand. In these village systems, only 21% of the loans in Central Java and 50% of the loans in West Sumatera, for example, are sourced by savings. The BKPD, a bank under banking law, can and does accept voluntary savings. West Sumatera pays no set rate on savings while Central Java requires borrowers to open a savings account and will soon be testing a voluntary savings program on a pilot basis. Required savings for loans are taken and provide collateral, but the potential for voluntary savings as a source of funds for lending remains to be tested. Each of the systems plans to expand the emphasis on savings mobilization significantly by relying on the village post system. Expansion of savings will require a number of steps:

1. A Stronger Emphasis On Voluntary Savings: During the life of project, mandatory savings requirements may be phased out as systems become capable of mobilizing voluntary savings. Approaches to phasing out forced savings, i.e. by borrower, by unit or by system, will be examined during project implementation. The long-term goal will be that savings in each system should be returned on request to any saver who does not have an outstanding overdue loan but implementation will be phased to the development of a particular unit. Within funding and loan security requirements, mandatory savings should play less of a role as voluntary savings increase.

2. Interest Rates Sufficient to Attract Savings: Current interest rates where offered by village lending institutions are unattractive when set against the inflation rate or savings rates at competing institutions. But potential impact of increased interest rates to mobilized savings is best illustrated in the commercial banking sector where a recent increase in interest offered resulted in a significant increase in formal savings. The project will focus early on determining a rate in each system which encourages individuals to save. Currently, for example, Central Java is considering establishing a rate of 15% p.a. As part of the financial review, the rate will be reviewed annually for its impact on financial viability, its effect in attracting voluntary savings, and the ability of savings to finance planned village-post expansion. The evaluation will also review the effectiveness of savings programs initiated to date.

3. Allow Posts to Accept Savings from both Borrowers and Non-Borrowers: In the four systems to receive assistance under this project only borrowers are now permitted to save. This restricts the ability of each system to self-finance its lending portfolio since all potential savers are not necessarily borrowers. Furthermore, current Ministry of Finance and Bank Indonesia instructions prevent non-bank financial institutions from taking savings deposits. The Government is well aware of the importance of this, and a request now is in process from the Ministry of Home Affairs via the Ministry of Finance to the Bank Indonesia which would allow the Central Java system (BKK) to accept savings. Similar authorization would be given eventually to the two other non-bank financial systems in West Java and West Sumatera. The pace of implementing a voluntary savings program will depend on the institutional development of each of the systems, both in terms of individual unit performance and overall system monitoring and supervision. It is envisioned that voluntary savings will only be allowed by the provincial government for units operating as Class I and perhaps Class II with class ratings based on established performance criteria. This should help ensure the safety of voluntary savings.

4. Mechanisms to Safeguard Savings Deposits: During the life of project, each province plans to institute mechanisms to safeguard savings deposits. As an initial step, the provincial government of Central Java is considering establishing procedures whereby the collapse of any individual unit could be offset by funds provided by provincial and Ministry of Finance project funds. Such procedures will be established early in the project and be linked closely with the financial performance of the system as a whole.

5. Specialized Programs and Campaigns to Promote Savings Generation: The above steps should ensure an environment conducive to savings generation. Subsequently, the BPDs plan to initiate a series of programs and savings instruments to promote savings which can be phased into stronger performing units. The programs may well include a series of savings promotion efforts using a combination of small gifts, non-negotiable certificates, and public meetings. Initiation of these efforts will be done in conjunction with phasing in of the training program described earlier. Technical assistance will help the BPDs design specific programs and savings instruments.

D) A Self-Sustaining Pricing Structure: A self-sustaining interest rate structure is a most critical element for project viability. Interest rates must consider contrary factors: they must encourage savings mobilization, offer the borrower a profit from his investment, and return enough interest to cover institutional costs, loan losses, inflation, and expansion. This project will support the existing pricing structure now used by the BPDs and supported by the findings of a recent evaluation of village credit systems in Central Java that: the difference between the formal rates for institutional credit and the real returns to borrowers from available investment opportunities allows formal credit rates to be high without reducing either borrower profitability or loan demand. The interest rate structure now in place is as follows:

Type of Funds	BKK	LPK	BKPD	LPN
Interest Paid by BPD for funds from MOF	0%	0%(1)	0%(1)	0%
Interest Paid by Units Initial BPD Funds	12%	12%(1)	12%(1)	7%
Interest Charged by Units for Loans to Borrowers	45%	36-48%	36-48%	20%

(1) to be established when Ministry of Finance line established

While the interest rate structure now used by the BPDs offers the prospect of financial viability, revisions may be warranted during the life of the project. The project includes a yearly financial evaluation beginning in the project's second year. The evaluation will assess the performance of each province, incorporating real expenses, such as administration and loan losses and will present its findings to the Ministry of Finance and other members of the national rural credit committee with specific recommendations for adjustment of project elements.

Borrowing rates while high are less then the rates of informal money lenders, the only real alternative for the majority of borrowers. During the first phase of the project, each of the provinces will need to consider establishing procedures and rates for borrowings from regular BPD facilities when and if their financial performance so warrants. Central Java is currently considering establishing a rate of around 21%. After individual units reach class II status per performance criteria, they should have sufficient equity for lending expansion and pay a more competitive price for funds.

E) <u>Strengthened Operational and Accounting Procedures for Each System:</u> Each of the systems participating in this project faces unique problems in its accounting procedures and in their application to a greater number of village posts. Some, such as Central Java, have a relatively strong system; others, such as West Sumatera, face the problem of reaching and accounting for relatively remote villages. Accounting and operational procedures in each system will be reviewed at the beginning of the project to make them more applicable.

During the project each province plans to revise selected accounting procedures and supporting operational manuals to allow for a significant expansion in lending and savings. Central Java, for example, has a relatively comprehensive system, but further adherence by units in its system is needed. Specific training programs and technical assistance will address this shortfall. Systems in West Java and West Sumatera, on the other hand, have not had a systematic review of accounting procedures, and an analysis of the consequences of applying the current system to a significantly greater volume of lending will be done early in the project. In addition, none of the systems have defined sub-capital accounts, specifically reserve accounts for loan losses to better measure profitability and the degree of system expansion. As each of the systems grow, these elements will be important.

Over the seven year life of the project, the BPD and consultant will build on existing procedures to design, implement and refine a more effective accounting system in each province together with supporting operations manuals. Loan processing procedures will build on established practices—such as maintaining loan authority in the unit at the kecamatan level and quick loan approval times—which have helped the systems to grow.

As BPDs make procedural and documentation revisions, they will address the issue of managing surplus funds either from the accumulation of savings or from increased equity. This money is now often kept in the district office safe or placed in central office account of the BPD earning minimal interest. Additionally, some units in Central Java and West Sumatera have built up a relatively large equity position but have not been able to apply that to lending opportunities in their areas. To maximize the use of these monies BPD and technical assistance will design procedures that allow surplus units to place money with the provincial BPD office for set periods and at competitive rates. The BPD, for example, could establish market-priced credit lines to units with insufficient funds but where performance to date warrants lending expansion. The project may also establish special secondary lines to tide over units during periods of heavy withdrawal when savers will want access to voluntary savings. Both functions will be the core of the financial intermediation under this project.

Additionally, the BPDs will address operational questions such as setting limits for cash on hand. All of these issues are related to development of a properly priced interest rate structure which can insure the maximum utilization of existing resources without stifling savings accumulation and of an asset/cash management capability in the BPD which allows the most effective use of resources.

During the course of project implementation, the BPDs will design and phase in a) procedures to estimate more accurately the recovery of outstanding loans; b) incorporate those estimates into the earnings statement; and c) reserve for potential loan losses in the capital accounts. Technical assistance will assist the BPDs to establish simplified procedures to measure loan recovery where none exist. The proposed project also will help minimize loan overdues by helping to:

1) establish reserve accounts in the capital account of individual units.

2) establish reserve and write-off policies based on actual performance.

3) consider methods to track overdue loans such as special overdue subsidiary loan ledgers at each unit outlet.

4) set up audit and inspections triggered by the overdue position of an outlet.

5) set up credit policies based on the unit classification system to prevent lending expansion when outstanding overdues are above acceptable norms.

F) Management Information System (MIS): Each system requires a management information system tailored to the abilities and needs of the units and the BPD management staff. Current management information within the participating systems varies by province but, in general, does not now provide sufficient data to assist the BPDs in supervision of a major expansion of lending. Under this project the existing management information systems will be refined and upgraded as managment capacity develops and specific information needs are identified. The level of analysis will need to be compatible with the ability of the operational level. Thus, flexibility in overall development and the rate of geographical expansion in each province is essential. Concurrently, though, there should be an integration of reliable information in the operational and accounting procedures of each system. Under this project the BPDs will work to further develop a simple management information system that will:

1. Track operational performance of each unit in terms of loan performance, loan delinquencies, equity growth, loans outstanding, number of borrowers, number of village posts, monthly loan circulation, total savings, expenses and income;
2. Consolidate the above to help the BPD set realistic credit and growth ceilings for each unit;
3. Identify and prevent malfeasance;
4. Produce reports on a monthly, quarterly, and semi-annual basis;
5. Maintain centralized, consolidated, financial statements regarding overall sources and applications of project funds;

Development of the above in each province will be the responsibility of the BPDs' supervision units with the assistance of the consultant team. The first task will be to review frequency of reports, their organizational distribution and management actions taken as a result. Each province will be approached based on its development needs. Central Java, for example, began upgrading its management information system by conducting an in-depth needs assessment in 1983 which documented the current BKK management information system, analyzed its anticipated uses and evaluated the system's present and projected capacity to meet those needs. The assessment found lending outpaced the development of the information system. As a result, incoming data was increasingly inaccurate and often as much as six months late. A 1983 redesign created a monthly financial progress report, a quarterly combination budget status report and profit and loss statement, a quarterly balance sheet and a semi-annual classification survey. The new system eliminated independent compilation of reports and merged them into a single, interrelated, data base accessible either manually or by computer. BPD supervisory staff now enter information into the system once but use the information in a variety of formats; all reports be generated at BPD headquarters but be derived from the four field reports submitted by each unit via kabupaten-based BPD supervisors. In addition the information generated provides the basis for a unit-performance classification done semi-annually.

Despite these changes, most of the bookkeeping for the village system has remained unchanged because the Supervision Bureau, the BPD bureau responsible for MIS reporting in Central Java, is the only user in the BPD to have computerized their MIS reports. The other bureaus of BPD have not yet computerized the other multiple manual registers and receipts. Evaluations and field visits indicate the BKK reports are adequate in Central Java, but there is now a need to continue integrating findings with management decision making, to refine cash management reporting, to consider coding loans by type and to monitor the current unit classification system.

The situation in the other provinces is similar. MIS development in this project, therefore will integrate accounting systems with the MIS system. Technical assistance for MIS and accounting to the BPD will go beyond strictly village credit system needs to consider overall BPD requirements as well. The BPD in each province will develop procedures to catalogue information now available, to identifying basic requirements and to integrating them on the basis of yearly performance evaluations and personnel development.

In introducing a MIS system into West Sumatera and West Java, the BPDs will first review the existing reporting format and its application to limited computerization. As in the case of Central Java, technical assistance will need to go beyond assistance to village credit systems to provide assistance for overall BPD needs. Introduction of the MIS will first require a review of the accounting procedures in place and a confirmation of the accuracy of consolidated financial data of all units. Implementation will be phased with training and BPD staffing.

VII. IMPLEMENTATION AND MONITORING PLAN:

The project implementation plan includes a description of the responsibilities of project participants, initial implementation steps, schedule of project inputs and detailed procurement plans.

A. Project Participants:

Ministry of Home Affairs: Since the provincial development banks, the BPDs, are under the authority of the provincial government, the Ministry of Home Affairs will play an extremely important role. Home Affairs will assign a Project Manager and one assistant to a full-time team in BANGDA covering only rural credit. BANGDA will be the main project signer, help coordinate the contributions of the various project participants and maintain a constant dialogue with the other provincial agencies interested in implementation of the project. They will also review the consolidated budget of the project containing contributions from the Ministries of Finance and Home Affairs, provincial contributions and operational expenses incurred by the BPDs. Furthermore, because of the expectation that the project may have application to other provinces, it will be important that BANGDA evaluate all phases of project implementation. Thus, the role of BANGDA will be to

1) provide GOI contributions to the training and equipment budgets;
2) monitor overall project implementation and system expansion;
3) review requests forwarded to the Ministry of Finance;
4) coordinate the host country contribution from other GOI participants; and
5) relate FID experience to other provinces for possible replication.

Ministry of Finance: The Directorate of State Wealth Management, Ministry of Finance, will finance unit recapitalization and expansion per procedures already established. The Directorate's rupiah line of credit equivalent to US$3 million to Central Java and $1.5 million to West Sumatera for rural credit expansion will be increased(see project inputs). In addition, the Ministry will chair the review committee on rural credit's annual meetings. Finally, together with the Ministry of Home Affairs, the Ministry will continue its present role of coordinating mid-project adjustments that require assistance from agencies, such as the Central Bank, not directly participating in the project.

Badan Pembinaan Pembangunan Kredit Pedesaan (Village Credit Development Board) is a working group already formed under the leadership of the Ministry of Finance to monitor overall rural credit policy in Indonesia. It will monitor the overall policy content of this project and consist of senior officals of the Ministry of Home Affairs, the Central Bank, Ministry of Finance, and BAPPENAS. The Board will meet at least yearly immediately after the regular evaluation to review yearly financial results and concur and facilitate project changes identified.

Bank Indonesia: The Bank Indonesia will participate in the project by participation on the Badan Pembinaan Pembangunan Kredit Pedesaan and also via their Bank Inspection Division which has oversight responsibility for overall BPD operations.

Provincial Counterparts

Bank Pembangunan Daerah(Provinical Development Bank): The three BPDs of West Java, Central Java, and West Sumatera will be the daily operational counterpart of this project. The specific management office in each respective BPDs is as follows:

West Java: Bureau for Research and Planning
Central Java: Bureau for Supervision
West Sumatera: Bureau for Supervision

Each BPD will strengthen their staff to inspect and train the local credit systems under their authority. While a separate bureau remains an individual organizational question, what will be needed from the beginning of the project is the additional staff for implementation, monitoring and supervision. These bureaus, all of which fall under the direction of the BPD, will be the prime counterpart for formulating unit expansion requests, additional capitalization requests, and the size, content and phasing of the training program. The BPDs in turn will be monitored by the provincial Badan Pembinaan consisting of various TK I administrative bodies such as BAPPEDA, governor's office, Kooperasi, and the BPD itself. Exact Badan membership varies in each province.

B. Initial Steps for Project Implementation: The Ministry of Home Affairs, Ministry of Finance and provincial BPDs will coordinate the first implementation steps. Subsequent coordination will take place via normal arrangements plus, through the coordinating committee meeting of the Village Credit Development Board in July of each year to prepare overall yearly budgetary levels, apportion a contribution from the respective agencies, review system expansion to date and assist in any required policy changes. The immediate implementation task will be to meet the conditions precedent discussed in the negotiation section. That will be followed by:

1) Core Staffing Assignments: The appointment of a two member, full-time rural credit team in BANGDA should be made as soon as possible while BPD offices in West Java, West Sumatera should be strengthened. Currently, the BPKD and LPK systems in West Java are monitored by a two-man team in the Bureau of Research and Planning while the BPD in West Sumatera has stated their intention to create a separate bureau for rural credit activity. Both provinces have said they would augment these bureaus with additional staff. The BPD offices will be staffed up to at least five people to provide the credit, unit accounting, MIS and supervisory personnel critical for an expanded lending and savings program.

2) Initial Operational Assessment: After meeting initial conditions precedent and while the additional conditions precedent to disbursement are being met, AID and the GOI will work closely to contract for technical assistance. The first task of the BPD will be to work with the technical advisors to:

a) review accounting and operational procedures and determine any adjustments needed,
b) formulate a workplan for identified accounting and procedural changes,
c) recompile and reconfirm the aggregate financial position of participating systems with appropriate adjustments to consolidated records,
d) establish unit performance criteria for West Java and West Sumatera,
e) conduct a computer needs analysis of the participating BPDs to determine system requirements for MIS and accounting formats and for compatibility with overall BPD computer procurement,
f) help design a comprehensive training curriculum and a schedule for the first year of implementation.

System Capitalization and Unit Classification: USAID capital flows will follow fulfillment of conditions precedent, redesign of a unit classification system for West Java and West Sumatera and the review of current accounting procedures and financial position of each system. The project will base performance standards for each participating unit on established classification systems but adjust them to the individual provincial characteristics. Criteria in the classification system include new loans booked, the ratio of village "posts" to banking units, the quality of the portfolio based on the percentage of overdue, loans, savings generated, and loan circulation. Those performance norms could be uniform in each province and applied to each unit of the village credit systems. Current estimates are that 12% of Central Java units, and none of the West Sumatera and West Java units are classified as I (highest). Conversely, 33% of Central Java, and perhaps one-half of the West Java and West Sumatera units are classified V (lowest).

The transfer of capital will be based on established procedures as follows:
1) When three months worth of funds or less remain in the BPD account, the BPD will prepare a request for additional capital for the signature of the governor to fund expansion of the village system in the coming year. The criteria will be established by the Badan Pembinaan Pembangunan Kredit Pedesaan and be related to the performance criteria of individual units. The criteria will likely include:
a) the current overall financial position of the system;
b) the number and quality of units to be given an equity contribution;
c) a summary of financial data confirming the unit's ability to use funds effectively: i)volume of lending and loan turnover rate, ii) overdue position, iii)savings position, and iv)trend analysis of leading indicators in the last year;

Precise criteria will be spelled out early in the project by the Badan Pembinaan in order that subsequent funding requests can be acted on quickly and in line with established criteria.

2) The loan application will be sent to the Director for State Wealth Management, Ministry of Finance, on behalf of the provinical government with copies to Home Affairs. Finance and Home Affairs, in turn, will provide the expansion plan to AID so they may promptly earmark a portion of the AID project budget for lending.

3) Finance will send a letter of agreement to the provincial government and a drawdown on the agreement will be effected by the Ministry of Finance who will restate the amount of loan, maturity date, interest rate, grace period, and disbursement schedule.

4) When funds are needed, the provincial government will send a withdrawal application to Finance who will pay that amount to the provincial account kept at the Bank Indonesia.

5)The provinces will send a brief status report when funds provided have been sent to individual units. Finance in turn will send that report to AID who will reimburse Finance.

6) Loan installments on the capitalization loan will be paid to the designated account of the Ministry of Finance in the Bank Indonesia.

7) Capitalization funds received by the BPD will be kept in a special account. Other funds available for previous provincial funding will be separated from other BPD activity. Authority over the accounts will rest within the province with the BPD acting as a fiscal agent per financial expansion criteria established by the Badan Pembinaan. Withdrawals for purposes other than unit capitalization may be made for training related needs and to pay back the Ministry of Finance loan. Interest received from the participating units for use of these loan funds will be deposited into the account after subtracting service fees set by the BPDs to cover supervisory expenses. The USAID Office of Finance, as part of its voucher verification program, will work with the Ministry of Finance to coordinate accounting procedures and documentation relating to capital contributions to insure the most prompt reimbursement from USAID as possible.

Project Implementation Schedule:

ACTION	ESTIMATED COMPLETION DATE	RESPONSIBILITY
Sign Project Agreement	June 1, 1984	GOI/AID
Send Implementation Letter No. 1	June 8, 1984	AID
Detail contracting/procurement procedures/CBD notice/selection criteria	June 15, 1984	AID
Review and agree to consultant terms of reference (see annex)	July 1, 1984	GOI/AID
Issue CBD notice	July 15, 1984	AID
Ministry of Home Affairs creates and staffs a team for rural credit	August 1984	GOI
Central Java, West Java, West Sumatera meet conditions precedent that allows them to mobilize and safeguard voluntary savings	October 1984	GOI
Contractors arrive and are in place	October 1984	AID and Contractor
Financial review complete	February 1985	GOI/Contractor
Contractor submits training plan and curriculum	May 1985	Contractor
First Annual Expansion Plan	July 1985	GOI
First Yearly Evaluation	January 1986	Contractor/AID/GOI
Second Annual Expansion Plan submitted	July 1986	GOI
Second Yearly Evaluation	January 1987	Contractor/AID/GOI
Third Annual Expansion Plan submitted	July 1987	GOI
Third Yearly Evaluation	January 1988	Contractor/AID/GOI

ACTION	ESTIMATED COMPLETION DATE	RESPONSIBILITY
Fourth Annual Expansion Plan submitted	July 1988	GOI
Fourth Yearly Evaluation	January 1989	Contractor/GOI/AID
Fifth Annual Expansion Plan submitted	July 1989	GOI
Fifth Yearly Evaluation	January 1990	Contractor/AID/GOI
Sixth Annual Expansion Plan submitted	July 1990	GOI
Final Evaluation	January 1991	Contractor/AID/GOI
PACD	May 31, 1991	

A Mission direct Letter of Commitment may be issued to the contractor if required. Training, essentially representing local cost expenses, will be implemented by the GOI via normal budgetary procedures with AID funds committed by PILs and financing via direct reimbursement. AID budgeted vehicles, commodities and equipment will be procured by AID with direct payment to suppliers. Capital contributions will be pre-financed by the GOI with AID direct payment reimbursement upon evidence that such contributions have been lent out to credit units.

The USAID Controller's Office as part of its voucher verification program will intially conduct a review of GOI accounting procedures and documentation relating to captial contributions. Thereafter, funds will be provided for an AID direct contract with an Indonesian CPA firm to conduct annual audits via direct payments.

VIII. BUDGET

Proposed Project Budget (000's; 1US$=1000Rp)

	A I D		GOI	Total
	Grant	Loan		
Technical Assistance	2,000	3,500		5,500
Training	500	6,950	3,000	10,450
Commodities and Equipment	-	750	2,750	3,500
Capital	-	3,000	3,500	6,500
Contingency	500	1,300		1,800
Total	3,000	15,500	9,250	27,750

Proposed GOI Contribution by Contributing Ministry

	MOF	MOHA	Province/BPD	Total
Technical Assistance	-	-	-	-
Training	-	2,000	1,000	3,000
Equipment	-	1,000	1,750	2,750
Capital	3,500	-	-	3,500
Contingency	-	-	-	-
Total	3,500	3,000	2,750	9,250

Local Currency/Foreign Exchange Budget

	A I D LC	A I D FX	GOI	FX	TOTAL
Technical Assistance	1,210	4,290	-	-	5,500
Training	7,360	90	3,000	-	10,450
Commodities and Equipment	500	250	2,750	-	3,500
Capital	3,000	-	3,500	-	6,500
Contingency	900	900	-	-	1,800
Total	12,970	5,530	9,250	-	27,750

Estimated Disbursements By Major Budget Categories
(in 000's of US)

CAPITAL

GOI	Yr 1	2	3	4	5	6	7	Total
West Java	–	200	300	300	200	–	–	1,000
Central Java	200	300	400	600	–	–	–	1,500
West Sumatera	–	200	200	200	200	200	–	1,000
Subtotal	200	700	900	1,100	400	200	–	3,500

AID	Yr 1	2	3	4	5	6	7	Total
West Java	–	200	300	300	200	–	–	1,000
Central Java	200	300	400	100	–	–	–	1,000
West Sumatera	–	200	200	200	200	200	–	1,000
Subtotal	200	700	900	600	400	200	–	3,000

TOTAL	Yr 1	2	3	4	5	6	7	Total
West Java	–	400	600	600	400	–	–	2,000
Central Java	400	600	800	700	–	–	–	2,500
West Sumatera	–	400	400	400	400	400	–	2,000
Subtotal	400	1,400	1,800	1,700	800	400	–	6,500

COMMODITIES:	Yr 1	2	3	4	5	6	7	Total
GOI								
West Java	–	250	375	375	125	–	–	1,125
Central Java	150	150	150	–	–	–	–	450
West Sumatera	–	160	285	285	285	160	–	1,175
Total	150	560	810	660	410	160	–	2,750

COMMODITIES:	Yr 1	2	3	4	5	6	7	Total
AID								
Vehicles	175	320	–	–	–	–	–	495
EDP Equipment	50	100	–	–	–	–	–	150
Other Misc.	15	30	30	30	–	–	–	105
Total	240	450	30	30	–	–	–	750

TRAINING	Yr	1	2	3	4	5	6	7	Total
GOI									
West Java		100	300	100	100	100	100	200	1,000
Central Java		100	300	100	100	100	100	200	1,000
West Sumatera		100	300	100	100	100	100	200	1,000
Total		300	900	300	300	300	300	600	3,000
AID									
West Java		150	300	500	500	500	300	-	2,250
Central Java		250	350	700	700	700	400	-	3,100
West Sumatera		150	100	500	500	500	350	-	2,100
Total		550	750	1,700	1,700	1,700	1,050	-	7,450

TOTAL	Yr	1	2	3	4	5	6	7	Total
West Java		250	600	600	600	600	400	200	3,250
Central Java		350	650	800	800	800	500	200	4,100
West Sumatera		250	400	600	600	600	450	200	3,100
Total		850	1,650	2,000	2,000	2,000	1,350	600	10,450

AID TECHNICAL ASSISTANCE	Yr	1	2	3	4	5	6	7	Total
Long Term		160	700	750	800	700	300	300	3,710
Short Term		40	300	350	150	250	400	300	1,790
Total		200	1,000	1,100	950	950	700	600	5,500

CONTINGENCIES:

	TOTAL
GOI	-
AID	1,800
TOTAL	1,800

TOTAL PROJECT COST:

GOI	9,250	(33%)
AID	18,500	(67%)
TOTAL	27,750	(100%)

IX. EVALUATION STRATEGY

As noted in the implementation schedule beginning in the second year of the project yearly evaluations will focus on four principal areas:

1. Borrower Impact: This will attempt to show the changes in income levels and economic activity that have occurred, the level of loan usage and profitability by type and by social group. Since the thrust of the project and supporting implementation documentation is geared to confirming and tracking financial viability of the units, this information will be the main source for reconfirming borrower viability. In addition, a limited program of applied research into related areas, such as demand analysis for credit and savings and the extent to which the project is affecting the informal money market in the project area, will be conducted throughout the course of the project.

2. Economic Assumptions: The evaluation will review underlying economic assumptions of the project:

a) expected loan demand;
b) pressure on interest rates to decline as lending portfolio matures and rates of return from investments decline;
c) potential returns *vis as vis* operational costs of providing credit; and
d) sensitivity of interest rates on savings mobilization.

3. Financial And Operational Viability: The evaluation will focus on the extent the project has achieved its goal of self-sustaining credit systems. The evaluation will highlight:
a. financial profitability reflected in information provided by the MIS in place;
b. success and appropriateness of training curriculum and programs;
c. adequacy of the management information system to meet identified needs; and
d. system adherence to accounting and operational procedures.

4. Efficiency in the Delivery of AID and GOI Inputs: The evaluation will look at the results from the previous year and make specific recommendations as to how the provision of inputs can be improved through adjustments in procurement procedures, contracting procedures, budgeting process, or training schedules.

Design and Methodology: The borrower viability component of the evaluation will be based on the survey designed and tested in Central Java for the BKK program to answer questions of loan usage and profitability from various types of ventures. Financial evaluation will be based on information developed by the MIS. Determining the efficiency and appropriateness of project inputs will be the joint responsibility of the GOI and AID with specific assistance from the AID Office of Finance against the criteria of the implementation schedule and budget contained in this project paper.

X. APAC PID ISSUES

The PID cable (see Annex I) raised the following issues: (1) community participation in project development; (2) linkages between credit and productivity/employment generation; (3) impact of AID capital contributions; (4) private sector credit roles; and (5) policy dialogue.

(1) Community Participation in Project Development: A major evaluation of the Badan Kredit Kecamatan (BKK) system was undertaken in November-December of 1982, Credit to Indonesian Entrepreneurs: An Assessment of the Badan Kredit Kecamatan Program, by Development Alternatives Inc., developed an information base on clients, their activities and opinions concerning BKK services and the BKK itself. The results have been used by the GOI in guiding the BKK and by AID in the design of this PP. National rural credit seminars have used the findings of this survey for discussion. The project's future evaluation program will continue client surveys to study the impact on policies and operations. In addition, GOI and AID officers have discussed participation issues with clients from each system in this project. The design reflects this and focuses on providing financial services at the village level and lowering total borrower transaction costs.

(2) Linkages between Credit and Productivity/Employment Generation Impact: The DAI survey showed that the BKK model system primarily gives trade-oriented loans but has both increased productivity and modestly increased employment opportunities. When the BKK and other systems gradually increase their small industry portfolio, a greater employment generation effect is anticipated. As stated, this will be monitored during evaluations.

(3) Impact of AID Capital Contributions: AID capital inputs will partially match a substantial input of GOI funds both planned and already committed to these systems. AID's funds will be used in the establishment and expansion of lending. Funds are necessary to establish units before operating profits and savings mobilization efforts produce sufficient revenues for operation and expansion. The proposed capitalization program is outlined in Annex E.

(4) Private Sector's role in rural Banking: As noted at the APAC review, the private sector'r sole in rural banking will remain limited in the near term. Most private banks are relatively small operations and are unable to quickly develop a large branch network needed to service rural areas. Development of hundreds of branches necessitates an extremely large, up-front investment in personnel, training, plant and equipment. The project will finance entrepreneurs, many of who will eventually need larger loans from private banks operating from their provincial capital location. The programs supported by this project will show that there is a large market for banking services and may attract private banks to seek aggressivlay smaller rural clients.

The project will also incorporate private sector banking procedures, policies and flexible interest rate structures in all four rural credit systems. Personnel incentive packages in all systems will include profit sharing and will be further refined during implementation to equate performance with pay. A new accounting system will generate reliable information needed to allocate costs to services and operations allowing for an efficient, effective and self-supporting system. Some funds set aside in the technical assistance component will be used in searching for ways to ensure a larger future involvement of the private sector in rural banking. Private sector banking will also be invited to participate in the annual workshops on rural credit funded by this project.

(5) Policy Dialogue: The project continues the policy dialogue with the GOI on rural credit begun with the Provincial Development Project (PDP). The BKK system, one of the most successful rural credit institutions, has influenced credit policies and institutional designs in several systems. AID's continued support to the BKK and other similar systems will present opportunities to continue productive policy dialogue on rural credit and savings mobilization issues. The project also incorporates an annual review of project progress with senior policy makers.

XI. COVENANTS AND CONDITIONS PRECEDENT

Conditions Precedent

A. Conditions Precedent for Initial Disbursement: Prior to the initiation of activity under this project, the government agrees to augment the staff of the Bank Pembangunan Daerah of West Java and West Sumatera so that at least five full-time professionals are assigned to the BPD Tingkat I implementation team full-time in each respective province.

The government agrees to establish and staff a team for rural credit in BANGDA, Ministry Home Affairs and staff it with at least two full-time professionals.

B. Condition Precedent for Disbursement of Funds for System Capitalization: Prior to the capital expansion of any of the participating systems with funds provided by AID, the government agrees to (1) describe the procedures for transfer of funds between the Ministry of Finance and the respective BPDs and to participating units; (2) take the necessary steps to allow village-based credit systems in this project to accept voluntary savings from borrowers and non-borrowers in the project area and safeguard such savings through procedures reflecting unit performance.

Conditions Precedent for Computer Related Equipment: Prior to the disbursement of any funds for computer-related equipment, the Government agrees to submit an assessment of BPD computer needs in West Java, Central Java, and West Sumatera as they relate to the implementation of this project and overall BPD computer requirements.

Covenants:

The Government agrees to structure accounting practices and interest rates under this project to ensure the financial viability of each of the particular village credit systems with accounting practices including procedures to reserve funds for loan losses and to write-off uncollectable loans.

The Badan Pembinaan Pembangunan Kredit Perdesaan will meet at least once a year to review performance and consider adjustments based on each respective systems' performance with the paramount criteria being financial viability as defined in the amplified project description.

XII. ECONOMIC ANALYSIS

The financial analysis of this project is contained in Annex I. It together with the techncial analysis earlier in this paper shows that the volume of lending projected is not unreasonable given past BPD and system activity. The Annex contains growth projections of lending and income in each of the three provinces. It shows a potential to increase significantly loans outstanding, income, and equity provided the project input schedule can be followed.

In the course of project implementation those growth assumptions will be adjusted yearly based on actual experience with a number of economic assumptions underlying this project:

1) The Underlying Demand for Credit: All the village credit systems in this project make the following assumptions:

a. interest rates above conventional rates are acceptable and in fact offer the borrower a reasonable rate of return.
b. demand for loan funds at these rates exists in other villages within current geographical operating areas (and outside present geographical areas as well, although not part of this project.)

Given these assumptions, the major constraint on the model, assuming revenues cover expenses, is the supply of loanable funds. The supply of loanable funds is derived from (i) loans from the central government to begin operations and from the provincial banking system, (ii) savings deposits, and (iii) net positive internal cash flow (i.e., equity plus retained earnings). New savings deposits are assumed in part to be a function of higher interest rates and initially are assumed to vary in proportion to outstanding loans of current year. This proportion varies from 10% to 60% given the particular unit being examined. It is an assumption and will be adjusted to actual performance in the second year of the project.

Since demand for loans is assumed to be unconstrained and the supply of loan funds fully available, the model presupposes the potential for a dramatic increase in the lending portfolio. Given a net positive interest rate in a purely economic sense, demand ultimately will constrain the growth of this model. There will be pressure on interest rates to fall as lending expands. Practically, this increase in loan demand and pressure to reduce interest rates is constrained by the many complex management issues the project addresses as well as the performance benchmarks built in to prevent expansion without a compatible growth in loan quality.

3. <u>The Cost for Credit:</u> In addition there are a number of factors that make the interest rate structure a central question in the implementation of this project. From the perspective of the borrower, the question is how much he is burdened under this system. In an extreme example, at a 100% interest rate, a five year loan of $100 requires $1600 to repay. The same loan repaid in 10 years would cost $51,200 to pay off. In addition the range of investments that can sustain such a cost of capital may be relatively low. This, of course, is a major question for the annual evaluations. However, borrowers are now paying 87% per year effective interest for short-term loans in the BKK system. A recent evaluation showed little concern for such high rates for funds by borrowers <u>if</u> funds were available at the village <u>and</u> the source of funds was reliable.

Experience indicates the borrower's only alternative source for funds is from higher, informal sources whose interest rate changes usually far exceed 100% per annum. In addition, the effect of that huge payout is mitigated by the fact that evaluations done to date indicate the bulk of lending done in each of the four systems has been largely for trader credits which have offered unusually high returns on small capital investments for limited periods of time. This project assumes that the same opportunity exists in villages not now served. It also assumes that when the small industry component begins, approximately in the third year of the project, more information will be known about the real returns on ventures outside of trader credits and that some adjustment to the interest rate structure may be necessary.

Two other key questions are whether labor will have a tendency to be overutilized and whether the project will encourage the excessive use of labor in the economic activities it finances.

These genuine economic concerns are weighed against institutional cost considerations and what is practical. The depletion of the capital of any credit system to keep interest rates down will not benefit the borrower if depletion reaches the point where no capital is available to lend the following year. Equal consideration must be given to preserving the capital of the lending institutions and the most optimal circumstance possible. Secondly, while it may be appropriate to adjust interest rates either because of the lower return from small industry credits or because of declining demand, such an adjustment must be done within the context of the institutional financial viability of the system. Practically, as is the case here, such an adjustment will be easier to achieve if it is downward rather than upward. By starting with a relatively higher interest rate, the project will have built-in, an essential flexibility.

Annex A, page 1

PROJECT LOGICAL FRAMEWORK

Project Title: Financial Institutions Development (497-0341)

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	IMPORTANT ASSUMPTIONS	MEANS OF VERIFICATION
Project/Sector Goal: To encourage enterprise development, increase productivity and generate Employment opportunities in rural areas	Measures of Goal Achievement: Increased productivity levels, New employment created in rural areas, increased individual Incomes from activities supported by lending	General economic conditions continue; moderate inflation continues	Project sponsored evaluations
Project Purpose: To support the development of existing local rural credit systems that provide financial intermediation for village residents at reasonable cost, produce loan portfolios of employment generating activities, mainly off-farm and promote savings mobilization programs in West Java, West Sumatera, and Central Java	Measures of Purpose Achievement: 1.3 M borrowers participating in programs by EOP; significant increased savings generated in system; a lending portfolio of Rp. 132.9 MM by EOP; improved quality of loan portfolio; adaption of a uniform documentation system; 4500 village posts operating, 550 currently dormant units reactivated.	GOI policy remains flexible on interest rates and decentralization continues; positive rates for savings adopted. GOI institutionalizes simplified MIS & reporting documentation.	Participant evaluation, financial analysis of report from MIS.
Outputs: 1. Self-supporting, credit system providing financial services at the village level. 2. Standardized loan, credit and administrative documentation.	Magnitude of Outputs: 1. Established village credit systems operating units in Central Java (Badan Kredit Kecamatan), West Java (Bank Karya Produksi Desa and Lembaga	Standardization agreed to by GOI and provinces; linkages created. Counterpart commitment of personnel and funding to staff banking units, interest rate structure is adjusted based on actual cost experience. Training conducted on schedule. Audit and supervision authority transferred to BPD. Savings regulations are reformed.	1. Financial reports from Provincial Development Banks 2. Site visits 3. Regularly scheduled evaluations 4. MIS reports 5. Consultant reports

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	IMPORTANT ASSUMPTIONS	MEANS OF VERIFICATION
3. Standardized and simplified management information system for proper administration, control, and responses. 4. Linkages between national, provincial and village level financial institutions for policy, direction, administrative support and funding. 5. Banking personnel at the provincial and district levels trained in procedures to be designed.	Perkreditan Kecamatan) and West Sumatra (Lumbung Pitih Negari) according to BKK procedures. 1372 total units. 2. MIS generating relevant and timely financial reports. 3. Standardized loan documentation and credit policies utilized throughout the project. 4. Funds and MIS reports circulating in national-provincial village linkage. 5. 5300 personnel trained. Establishment of an on-going training program including long and short-term activities, detailed curriculum and established training schedule.		
* Inputs: 1. Phased technical assistance at the national and provincial levels. 2. Standardized training programs in financial management and control for provincial and village level personnel. 3. EDP equipment for MIS. 4. Seed capital for start-up and/or expansion of financial system operations. 5. Limited office equipment.	Magnitude of Inputs: Technical Assistance - (AID) $5,500,000. LOP: 171 L/T P/MS, 73 S/T P/MS. Training - (AID) $7,450,000, (GOI) $3,000,000 Commodities and Equipment - (AID) $750,000, (GOI) $2,000,000 Capital - (AID) $5,000,000, (GOI) $3,500,000 Contingency - (AID) $1,800,000 (GOI) $750,000	1. Suitably qualified advisors contracted. a. Standardized curriculum accepted by GOI and provinces. 3. GOI capital inputs available and sufficient for joint funding. 4. Staff assignments made at provincial development banks.	1. USAID monitoring of TA activities. 2. Reports, observations on training activities. 3. Observations. 4. Financial reports from MIS, USAID documentation. 5. Regularly scheduled evaluations against a phased schedule of inputs.

Consultants Terms of Reference and Report Requirements

1. Assistance for Revising Accounting Policies and Procedures: The consultant will assist in the review, design or re-design of accounting sytems used under this project. The consultant will design systems to develop accounting uniformity across all four systems. Assistance will include:

A. A cataloging of each of the accounting systems now in use.
B. A listing of specific accounting instruments for incorporation.
C. Revised or fully redesigned accounting formats for each of the systems.
D. A phased implementation schedule considering design, training and implementation.
E. A review of the current system of interunit and between branch and BPD accounting procdures and specfic recommendations for the simplification of the existing system with the parallel goal that interunit accounting flows should be under a full cost pricing structure.
F. The consultant will help the respective BPDs format and put into place the revised interest rate structure agreed to under this project.
G. The consultant will monitor the overall interest rate structure to track the financial viability of each of the four systems. He will provide a yearly analysis of financial viability for presentation at the annual evaluation employing analytical techniques in conformance with commercial bank practices of tracking institutional profitability. The consultant will monitor the annual financial review and recommend adjustments to the current interest rate structure if analysis so warrants. Recommendations may include but are not neccessarily be limited to:

   a) an adjustment in interest rates in each major funding and lending element of the project.
   b) an adjustment of coverage of interest rate allowing some outlets to reduce charges and others to raise them when performance would so warrant.
   c. the incorporation and adjustment of loan reserve policies and loan write-off policies.
   d. an adjustment to demand projections based on past performance.

H. The consultant will assist in the design of appropriate loan loss and loan reserve policies and assist in the integration of those policies into the accounting system.

I. The consultant will assist in expanding the current accounting procedures for tracking the performance of overdue loans to allow an aging of overdue loan performance on a 3 month, 6 month one year and 3 year basis and make specific recommendations as to who those procedures will be integrated into existing systems.

J. The consultant will assist in the establishment of village, post, and unit subsidiary reserve accounts in the overall capital accounts of each sub-system.

K. The consultant will design an overdue loan ledger for use at village posts and unit outlet.

L. The consultant will design detailed audit and inspection programs with related formats, and training and implementation schedules.

2. Training Program Development: The consultant will for the three provincial development bank's (BPDs) four associated rural credit systems: (1) review current manpower capabilities and anticipated future needs; (2) develop a plan to effectively utilize project inputs in meeting organizational manpower development needs; (3) develop a program to establish in-house BPD training capabilities to handle future rural credit systems' manpower development; and (4)create standard curriculum and training courses to be used by the BPDs in their training programs for rural credit institutions.

1. Review of Current Manpower Capabilities and Anticipated Needs will include:

a) Review of all on-going rural credit training programs now underway in each of the participating BPD's;

b) Conduct job analyses and create job descriptions for current and future anticipated rural credit systems' job positions. Positions include but are not limited to unit managers, loan officers, unit supervisiors, area auditors, BPD branch managers, and BPD Tk.I management.

c) Review and suggest improvements to BPD plans for expansion of rural credit systems and to anticipate and prepare for manpower requirements.

2. Developing a Training Plan to Effectively Utilize Inputs is required to accomplish the strategic training objectives in each province and includes:

a) Drafting and begin the BPD to implement a multi-year training plan to provide for the training needs of each BPD supported rural credit system. The plan should be drafted in close colaboration with senior BPD management, specify clear objectives and include a detailed implementation schedule. The critical point is that expansion of BPD training services should proceed at a pace commensurate with development of the training staff itself.

b) Creation of a schedule for rapidly upgrading professional skills in the rural credit systems and associated BPD support offices. Emphasis here is on the use of a sequential series of intensive in-country short courses.

c) Establishing recruitment standards for entry-level full time positions and a schedule for recruiting candidates.

3. Assist in Developing of In-House Training Capabilities. The advisor will work with the BPD to:

a) conduct basic job analysis for rural credit system positions critical to the rural credit system, i.e. unit manager, loan officer, auditor, supervisor, BPD branch manager, etc. Identify major duties, responsibilities and outputs for each position and write standard job desciptions.

b) establish (through close coordination with line management) performance standards for key positions and assess patterns of knowledge/skill deficiencies which inhibit rural credit units from functioning smoothly.

c) design standard training program curricula with clear behavioral objectives specifically tailored to performance requirements of rural credit positions. Design programs in response to special problems. Design programs using the experiential learning methodology which require active involvement of participants through small group exercises, role plays that are closely linked with training activities and the actual job situation.

d) design materials such as trainer and participant manuals, suitable visuals, etc.

e) conduct courses using reasonably polished "stand-up" trainer skills.

f) evaluate, in close coordination with supervisors in the field, behavioral change several months following participants return to the job.

4. Curriculum Development for each province will be done for all jobs in each of the respective rural credit systems. Curriculum will be created for formal and informal training programs. All curriculum designed will be compatable with the other elements of the project. The training courses and curricula will explain operational responsibility of each position and include but will not be limited to the following:

a)The purpose of the Financial Institutions Development Project and the four credit systems under development.

b) Accounting procedures
c) Management information system
d) General BPD system operating procedures
e) Procedures for interest accrual
f) Dealing with overdue loans
g) Savings policy and procedures
h) Areas of new system initiatives or procedures as needed.

3. Managment Information System: The consultant will provide detailed assistance in the further design, implementation, and refinement of a management information system as detailed in the project paper. The

consultant will provide guidance on the current system now being implemented by the BKK in Central Java and assess its operational effectiveness and the extent the system should be changed. Concurrently the consultant will identify and develop other informational requirements to allow the BPD/participating systems to provide essential information for development of the credit systems. Information formats to be developed should include but not be limited to the following :

The consultant will assist the respective BPD's in the implementation of a revised management information system. Assistance will include:

a) a review of the existing BKK MIS system with suggestions as to how the system can be improved and transferred and implemented in the other participating systems;
b) a description of the additional information needs that should be included;
c) suggested revisions to information flows at each of the participating systems.
d) information and reporting formats to pass information to Jakarta interested agencies;
e) incorporation of yearly and overall project goals into the management information system.

Within 90 days after the management information specialist arrives in country, he will provide in writing a master plan for:

a)the specific revisions neccessary to the existing management information system now in use by the BKK;
b)a catalog of existing MIS type of information now being used in West Java and West Sumatra;
c)a timetable of major training, design and implementation to operationalize a new training system.

As part of the procurement of data processing machinery and computers to support the development of a MIS capability in West Java and West Sumatra, the consultant will present for each respective BPD a technical analysis of computer requirements based on the project accounting system and MIS needs the existing harwarde and software configuration if any, the the current procurment plans of the respective BPDs. The analysis will detail:

a) the information to be computerized;
b) the current availability of and compatibility with data processing machinery already in the respective BPDs;
c) system and format compatibility with the existing system in the Central Java BPD
d) the overall data processing procurement plans of the respective BPDs.

Per the above the consultant will make specific recommendations on:

a. the hardware configuration appropriate for West Java, West Sumatra and Central Java considering cost, training availability and service facilities.
b. the appropriate software configuration.

The consultant will detail the rationale underlying his recommendations. (Recommendations per a. and b. above will be formatted to the operational requirements of the BPD rather than to a specific brand name.) When operational requirements are prepared, he then will list the brand names of the data processing equipment that can meet the requirements. He will also note the availability of training and servicing facilities in the respective provinces for the brands presented.

4. Savings Promotion: The consultant will assist in the design and initiation of the savings element plus assistance and advice in the implementation of possible policy and regulatory changes supportive of savings generation.

The consultant will design specific programs to encourage savings generation. Such programs may include but not necessarily be limited to publicity campaigns, lotteries, entertainments, small gifts and other means to increase unit savings levels. The design for the first phase of the program will be completed within 60 days after the arrival of the savings specialist.

BKK Units: MIS and Accounting System

Management Information Systems for individual BKK units are composed primarily of traditional administrative and financial record keeping. All BKK use BPD-designed standardized formats, called "models," of which there are currently 18. Although these models are sometimes cumbersome and redundant, and are not differentiated by degree of importance, they are replete with cross-checks and internal controls, and are designed so that staff with a primary school education can use them after a one-month training course at provincial headquarters.

Table 7 presents a brief description of the BKK models. Theoretically, all 18 models are mandatory, but in practice, all but the largest BKK have neither the need nor the staff to maintain the entire set. Thus, in most cases, the most critical books, those necessary to complete the BPD-required financial reports, are updated daily, whereas the less important models are used at the discretion of each BKK.

For example, all BKK must use the models that perform the following essential functions:

* Compile a register of BKK clients by name (Model 6) and borrower number (Model 5);
* Provide these clients with a receipt of all loan transactions (Model 8) and savings transactions (Model 14);
* Keep track of loan repayment (Model 2A) and delinquent clients (Model 2B);
* Monitor the BKK's overall financial status (Model 3) and cash on hand (Model 12); and
* Inventory the BKK's fixed assets (Model 10).

If special problems arise, however, other models are available to address them. For example, if a BKK unit is having difficulty in managing its cash flow, it can use Model 11, or if a BKK would like to have written records of delinquent clients' renewed promises to pay, it can use Model 15. The problem with most of these models is that although they are conceptually sound, some are tangential to daily BKK operations, and therefore tend to detract from the quality of record keeping that is critical for effective BKK management.

Nonetheless, the BPD has been able to use its combination of overlapping, redundant, core, and peripheral models to build many cross-checks and internal controls into the BKK bookkeeping system. For example, the BKK cashier is responsible for keeping the cash book (Model 12), while the bookkeeper is responsible for maintaining a combination cash book and running balance (Model 3). Moverover, many critical documents, such as the client's loan repayment receipt (Model 8) and savings book (Model 14), require the signatures of both the BKK cashier and the bookkeeper. This in turn requires concurrent transaction entries into two different BKK accounts, one the responsibility of the cashier and the other of the bookkeeper.

Such financial controls are important BPD passive auditing tools for supervising hundreds of credit bodies whose very mandate is also the aspect of the BKK program most open to abuse: many BKK have only two employees, always dangerous in cash-oriented operations, and all BKK are locally run institutions, which both distances them from BPD observation and leaves them susceptible to pressure from local interests. This passive auditing system combined with active supervision has helped to identify instances in which local authorities have allowed BKK funds to be used for welfare rather than productive purposes, or misused funds in more nefarious ways.

BKK Bookkeeping Models

Model Number	Description	Frequency of Use
1	Client request/approval list	Daily
2A 2B	Loan repayment record Delinquent clients register	Daily, per village post and type of loans
3	Cash book/running balance	Daily
4	Savings book	Daily
5	Client register by number	Per new borrower
6	Client register by name	Per new borrower
7	Contract book/cash on hand	Daily
8	Customer's loan repayment record (receipt)	Per transaction
9	Composite register	Annually
10	Commission register (fixed assets inventory)	Per transaction
11	Cash estimation	Daily
12	Cash book	Daily
13	Bank deposit form	Per transaction
14	Customer's savings book	Per transaction
15	BKK village supervision report	Per trip to village
16	BPD supervisory report	Per BPD inspection of BKK

Model Number	Description	Frequency of Use
17	BKK budget	Annually
18	Supervision card	Per village post and type of loan

Classification Systems

Inputs transferred to units from a BPO depend on the lower level institutions performance ranking. At this time only the BKK in Central Java has a functioning ranking or "classification" system. Other systems supported by this project will incorporate a classification system into their operations during the project that have the same standard.

The BKK's classification system uses six weighted factors: total equity; ratio of villages to village posts; number of new borrowers; portfolio quality; total savings; and capital circulation. A semi-annual classification determines the capacity of each unit to absort new capital and its BPD credit ceiling.

BKK Classification Criteria

Class	I	II	III	IV	V
Criterion					
1. Equity (million of rupiah)	10,000	5,000 - 9,999	1,000 - 4,999	0 - 999	0
2. Ratio of village to village posts	2	2 - 3	3 - 4	4 - 8	8
3. Number of new borrowers (monthly average)	20	15 - 19	10 - 14	5 - 9	0 - 4
4. Portfolio quality (percentage)	90	89 - 80	79 - 70	69 - 50	50
5. Savings (million of rupiah)	2,000	1,000 - 1,999	500 - 999	200 - 499	0 - 199
6. Circulation (million of rupiah)	5,000	2,000 - 4,999	1,000 - 1,999	100 - 999	99
7. Overall classification	1.0 - 1.5	1.6 - 2.5	2.6 - 3.5	3.6 - 4.5	4.5

Source: Bank Pembangunan Daerah Jawa Tengah

For the most successful BKK, the BPD has established a top performing "sehat" class. The BPD will lend its own funds to units in this classification. The criteria for this group its outlined in Table 2.

Calculation of Healthy BKK Units

Criterion	Standard
Ratio of current assets (at 80% of the actual figure) to current liabilities	1.50
Ratio of debt to equity	0.75
Ratio of savings to equity	0.70
Ratio of debt plus savings to equity	1.25
Six months' profit	10%
Number of trained staff	4

Source: Bank Pembangunan Daerah Jawa Tengah

CONSOLIDATED BALANCE SHEET
Bank Karya Produksi Desa (BKPD)
Lembaga Perkreditan Kecamatan (LPK)
Estimated ar of 1/31/84
(Rp 000)

	BKPD	LPK
Assets:		
Cash in units	221,096	65,095
Cash on deposit	134,740	6,023
Loans outstanding	2,589,336	695,052
Plant and equipment	497,392	4,867
Total assets	3,440,564	771,037
Liabilities:		
Time deposits	545,425	4,000
Savings deposit	930,050	101,986
Loans payable	386,996	194,399
Other payables	230,406	294,707
MPBG (1)	292,450	87,034
Retained earnings	302,588	161,767
Original capital	548,404	53,036
	3,236,319	896,929
Unaccounted for resources (2)	204,245	(125,892)
	3,440,564	771,037

(1) Modal penjeujeuh bantuan Gubernur - Special investment fund from the Governor's office

(2) The BKPD and LPK accounting and management information systems produce poor quality reports. Not all units file reports and information is often missing and ill-defined. This balance sheet provides what information is available as of 1/31/84.

Estimated
CONSOLIDATED INCOME STATEMENT
Bank Karya Produksi Desa (BKPD)
Lembaga Perkreditan Kecamatan (LPK)
(Rp 000)

	BKPD	LPK
Revenue:		
Interest earned	640,196	236,943
Other income	113,368	36,065
Total	753,564	273,008
Earnings:		
Interest paid	118,354	47,625
Wages and salaries	271,425	79,903
Depreciation and other expenses	221,812	94,711
Total	612,089	222,239
Profit	141,475	50,768

CONSOLIDATED BALANCE STATEMENT
Bank Karya Produksi Desa (BKPD)
Lembaga Perkreditan Kecamatan (LPK)
Estimated as of 1/31/84
(Rp 000)

	BKPD	LPK
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STATEMENT OF EARNINGS
BADAN KREDIT KECAMATAN (BKK), CENTRAL JAVA
(FOR YEAR 1983 - AS OF SEPTEMBER 1983)

Revenues		
Interest:	Daily/Weekly Loans	Rp 724,269,911
	Monthly/Seasonally Loans	597,544,894
	Agricultural Loans	36,344,206
Other Cash Receipts		176,686
Other Income:		8,339,048
	Total Revenues	Rp 1,471,155,058
Expenses		
Interest paid to BPD		Rp 67,822,319
Salaries		213,699,147
Audit/Supervision		44,746,101
Operation Expenses		63,240,784
Other Expenses		106,231,356
Depreciation		1,088,693
	Total Expenses	Rp 496,828,400
	Net Income	974,326,658

STATEMENT OF FINANCIAL POSITION
BADAN KREDIT KECAMATAN (BKK), CENTRAL JAVA
FOR YEAR 1983 - AS OF SEPTEMBER 1983

Assets		Liabilities	
Cash	Rp 199,459,564	Loans from Government	Rp 1,250,655,137
Deposits in Banks	173,203,848	Village Cash Deposits	21,878,834
Loans Outstanding	6,071,905,486	Savings Deposits	1,188,074,221
Property & Equipment	232,470,106	Dinas and Other Deposits	71,043,334
Reserves	1,047,800	Earnings to September 1983	974,326,658
Other Items	53,276,865	Retained Earnings	3,225,385,487
	Rp 6,731,363,669		Rp 6,731,363,669

CAPITAL ACCUMULATION OF THE BKK SYSTEM

Year	Number of Units	Loans Out-standing	Overdue Payments	Borrowed Capital	Savings	Equity
			In million rupiah			
1972	200	213.4	31.5	152.5	38.4	(-8.7)
1973	350	498.3	89.8	306.0	110.7	(-8.2)
1974	432	857.9	181.3	446.1	220.1	10.5
1975	465	1,096.3	245.3	463.6	285.4	101.9
1976	486	1,305.8	326.5	462.2	338.4	178.7
1977	486	1,420.1	361.6	422.0	336.3	280.2
1978	486	1,581.2	475.0	394.3	385.5	426.4
1979	485	1,886.2	454.9	397.6	435.7	598.8
1980	485	2,507.7	561.0	500.3	565.9	880.5
1981	485	3,319.5	675.7	572.2	733.8	1,337.9
1982	485	4,817.8	808.2	1,001.2	1,002.4	2,006.1
1983 Oct.	486	6,241.1	968.7	1,303.7	1,264.0	2,704.6

Source: BPD Central Java

BKK Comparative Balance Sheets

Assets and Liabilities	December 31, 1975 (344 BKK)	December 31, 1978 (397 BKK)	June 30, 1983 (486 BKK)
	(million of rupiah)		
Assets			
Cash	33.3	65.9	199.5
Loan portfolio	894.4	1,463.6	6,071.9
Savings deposits with BPD	6.1	16.2	173.2
Materials building and equipment	22.6	78.0	232.5
Other	7.3	1,631.6	53.5
TOTAL	963.7	1,631.6	6,730.6
Liabilities			
Provincial government/BPD	349.8	311.0	1,250.1
Kas desa	18.1	24.9	21.8
Dinas deposits	22.8	11.6	71.0
Member savings	247.3	359.7	1,188.1
Retained earnings	199.3	669.4	3,225.3
Net profits from proceding year	126.4	254.9	974.3
TOTAL	963.7	1,631.6	6,730.6

Source: BPD Central Java

B K K

Nominal and Effective Monthly Interest Rates

Type of Loan	Payback Period	Nominal Monthly Interest Rate (excluding savings)	Effectively Monthly Interest Rate (1) (excluding savings)
Harian(2)	22 days	4.8	10.8
Pasaran	60 days	4.0	6.9
Mingguan	12 weeks	3.6	6.9
Bulanan	3 months	3.3	5.3
Lapanan	175 days	3.4	5.6
Musiman(3)	6 months	2.0	2.2

(0)

STATEMENT OF FINANCIAL POSITION LUMBUNG PITIH NAGARI (LPN)
WEST SUMATERA
DECEMBER 31, 1983

Assets	Total (Rp 000)	Liabilities and Equity	Total (Rp 000)
Cash	12,923	Loan from Provincial Govt.	130,978
Bank Deposits	11,083	Loan from BPD West Sumatera	131,214
Inventory	25,442	Savings Deposits	645,581
Loan Outstanding	1,252,650	- Non-Voluntary Rp. 622,081 (10% of loans must be in forced savings) - Voluntary Rp 23,800	
Other Items	39,616	Reserves	275,352
		- Capital Rp255,420 - Govt. Development Funds Rp 19,932	
		Other Items	40,321
		Retained Earnings	217,968
J U M L A H	1,441,714	Total Liabilities & Equities	1,441,714

STATEMENT OF FINANCIAL POSITION
LPN SUMATERA BARAT

NO.	YEAR	1974 (14 unit)	1975 (49 unit)	1976 (71 unit)	1977 (95 unit)	1978 (169 unit)	1979 (236 unit)	1980 (283 unit)	1981 (322 unit)	1982 (202 unit)	1983 (383 unit)	1983 (414 unit)
A.	ASSETS	12,558	54,586	94,156	143,308	249,400	396,582	572,594	764,108	700,909	1,132,046	1,152,670
1.	Cash	399	3,543	8,924	13,041	23,680	34,756	55,478	78,579	58,968	112,096	94,508
2.	Inventory	-	10	333	627	1,448	1,610	1,808	5,279	15,864	17,629	20,887
3.	Bank Deposits	-	-	-	-	-	32	857	1,605	3,195	4,606	5,469
4.	Loans Outstanding	11,954	49,131	80,499	121,506	212,144	339,017	481,460	633,951	604,244	964,937	1,001,216
5.	Pre-paid Expenses	192	1,730	3,695	6,175	10,139	17,014	28,460	36,661	-	-	-
6.	Other	13	172	705	1,959	1,989	4,153	4,531	8,033	17,916	32,778	30,590
B.	LIABILITIES	12,558	54,586	94,156	143,308	249,400	396,582	572,594	764,108	700,909	1,132,046	1,152,670
7.	Advance Payments	716	2,597	2,969	3,889	7,501	9,762	10,821	12,040	-	-	-
8.	Provincial Loans	7,000	24,380	29,335	32,359	60,161	82,324	92,568	100,530	56,473	116,067	124,312
9.	Bank Loans	-	-	-	-	-	-	400	16,936	35,962	39,488	40,741
10.	Voluntary Savings	464	467	374	597	1,292	3,345	6,103	6,753	12,066	13,054	12,773
11.	Forced Savings	2,280	13,545	32,063	56,038	93,574	156,399	243,736	331,230	319,892	502,227	539,315
12.	Reserve	61	920	5,147	11,738	22,095	41,092	68,121	110,259	123,936	212,718	223,791
13.	Government Develop. Funds	-	117	562	853	1,374	3,177	5,178	8,644	10,807	14,298	17,033
14.	Other	32	267	752	1,642	3,195	6,816	7,603	11,498	20,435	38,026	36,895
15.	Profit/Loss	2,005	12,295	22,954	36,192	60,208	94,667	138,044	166,218	121,336	196,198	155,810

Annex D, page 11

Statement of Financial Position
Per March 31, 1982

	BPD Central Java	BPD West Sumatera	BPD West Java
Assets			
Cash	10,062,442	3,192,652	11,237,000
Central Bank of Indonesia	8,485,848	1,088,372	9,122,000
Clearance guarantees	55,600	N/A	N/A
Asstes at other bank	454,086	106,578	989,000
Giro (notes receivables)	61,485	2,283,542	1,615,000
Shares		24,127	N/A
- Short term		14,419,334	N/A
- Medium/long term		11,691,234	N/A
Co Financing	12,000	413,828	N/A
Fixed assets and Inventory		2,097,836	1,598
At cost	2,335,192	N/A	N/A
Depreciation accumulation	(493,924)	N/A	N/A
Book Value	1,861,268	N/A	N/A
Bad debts		321,853	N/A
Miscellaneous (other) assets	1,608,356	1,145,371	681
	56,069,626	36,141,371	55,002
Liabilities			
Account Statement (cash at bank)	N/A	13,066,933	27,706,000,917,754
Giro notes (notes payable)	18,155,695	N/A	
Regional Cash	3,820,422	N/A	N/A
Other Pemda funds	4,911	N/A	N/A
Other liabilities payable	1,917,754	2,387,940	2,166,000
Savings	2,692,284	1,842,032	461,000
Time deposit	605,310	4,979,165	5,052,000
Central Bank of Indonesia	13,619,668	N/A	N/A
Loan received:			
-Medium/Long term:		N/A	N/A
-Obligation	N/A	N/A	N/A
-Other	N/A	6,500,110	13,561,000
-Short term	N/A	1,538,232	N/A
Co-financing	996,628	N/A	N/A
Liabilities at other bank	281,130	N/A	N/A
Miscellaneous liabilities	95,093	N/A	1,073,000
Reserved for capital	1,584,592	N/A	N/A
Deposite Capital	N/A	1,909,650	2,092,000
Guarantee deposit	N/A	22,707	313,000
Shares capital	3,055,800	N/A	10,000,000
Shares capital not yet deposit		N/A	7,908,000
Donation capital	20	N/A	N/A
Miscellaneous	N/A	117,361	N/A
Reserve	1,168,464	467,843	892
-General reserve	N/A	1,622,047	842
Previous year earning	N/A	N/A	113
Current year earning	3,165,179	1,646,941	721
	56,069,626	36,141,021	55,002

Statement of Earnings
March 31,1981-March 31,1982
(in thousands rupiah)

	BPD Central Java (in thousands rupiah)	BPD West Sumatra (in thousands rupiah	BPD West Java (in thousands rupiah)
A. Operational Income	1981/1982	1982	1982
Interest & giro notes service (income)	5,759,243	4,355,702	4,584,000
Provision (commissions income)	509,147	330,656	229,000
Other provision	131,569		N/A
Other operational income	N/A	221,341	104,000
	6,399,959	4,907,699	4,917,000
B. Operational expenses			
Employee/work force cost salary/wages	679,595	779,917	1,443
Office cost/rent	448,000	6,384	N/A
Special work support/Honor	172,950	6,456	N/A
Maintenance cost	339,953	91,359	N/A
Official travel cost	77,254	N/A	N/A
Branch Office cost	27,000	N/A	N/A
Educational cost	24,818	N/A	N/A
BKK cost	7,634	N/A	N/A
Interest cost	910,352	1,036,836	1,196
KIK cost	2,860	N/A	N/A
Depreciation cost	521,002	118,830	118,830
Other operational cost	32,366	233,982	233,982
Taxes	N/A	4,110	4,110
Debts depreciation	N/A	262,590	262,590
Material cost & 3rd party serv.	N/A	743,630	N/A
Total Operational Expenses	3,243,784	3,284,096	4,174,000
Operational profit	3,156,175	1,623,605	743,000
C. Non-operational expenses			
Non-operational income	170,184	108,935	23,000
Non-operational cost	(161,180)	(85,599)	(45,000)
	9,004		23,346
Profit	3,165,179	1,646,941	721,000
Previous year profit balance			

Major Rural Credit Programs

Credit Program	Interest Rate	Loan Size	Maximum Maturity	Collateral
Kredit Investasi Kecil (KIK)	12% Per Annum	To Rp. 10 million	10 years	Project Itself + 50% (maximum)
Kredit Modal Kerja Permanen (KMKP)	12% Per Annum	To Rp. 10 million	3 years	Project Itself + 50% of loan amount (maximum)
BIMAS/INMAS	1% per month	special package loan	crop cycle or 7 months	none, recommendation from village chief or worker
Kredit Candak Kulak (KCK)	1-2% per month depands on maturity	Rp. 2,000 Rp. 15,000	3 months	none, recommendation of village chief
Kredit Umum Pepesaan	12% per annum investment capital 21% per annum working capital	Rp. 10,000 Rp. 1,000,000	up to 2 years	required
* Badan Kredit Kecamatan (BKK)	2-4.8% per month depending on maturity	Rp. 10,000 Rp. 100,000	6 months	none, recommendation from village head
* Lembaga Perkreditan Kecamatan (LPK)	same terms and systems as BKK)			

Note

* a credit system that will be supported in the proposed new project.

Credit Program	Interest Rate	Loan Size	Maximum Maturity	Collateral
* Bank Karya Produksi Desa (BKPD)	1% per special; 4% monthly General loans on declining balance	Rp. 10,000- Rp. 100,000	6 months	none, recommendation from village
* Lumbung Pitih Nagari (LPN)	10% semi-annually	to Rp. 1.5mil.	6 months	required, some units required only recommendation for small loans

CHARACTERISTICS OF PDP INSTITUTIONAL CREDIT SYSTEMS

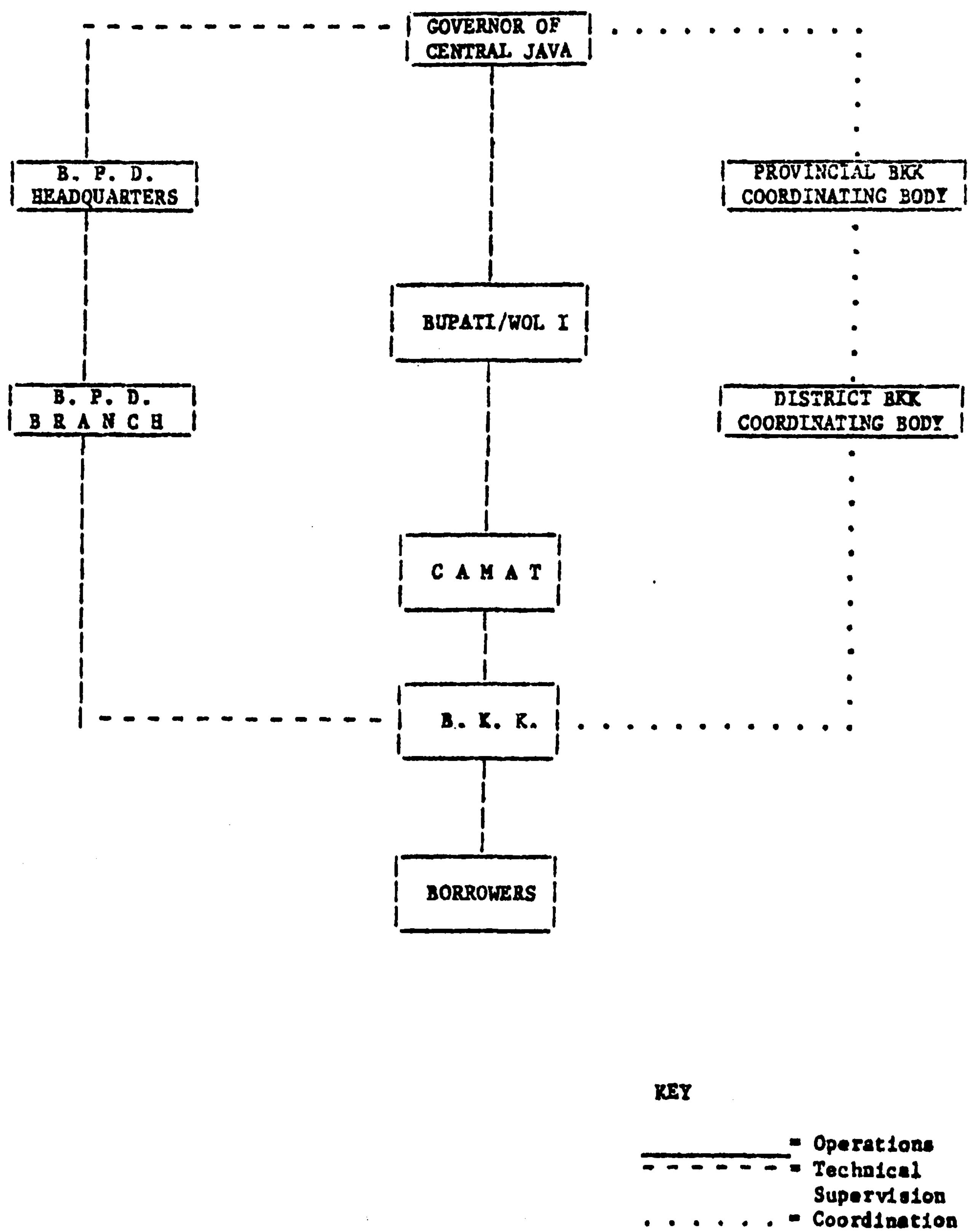
CHAR/NAME	C. JAVA BKK	W. JAVA LPK/BKPD*	BENGKULU BKK	ACEH LKK	KALSEL KURK	NTB/BPD (channel sys) BPD	NTB/ Koperasi KUD	E. JAVA KURK	NTT LUB
1. Age	14 yrs.	LPK: 8 yrs. BKPD: 18 yrs.	0	0	1 yr.	2 yrs.	2 yrs.	3 yrs.	2 yrs.
2. Administrative Body & Profit/ Loss Center	Kecamatan	Kecamatan	Kecamatan	Kecamatan	Kecamatan	Province	Kecamatan	Desa	Kecamatan
3. Supervising Body at Kabupaten	BPD Cabang	LPK: Kabupaten Inspector	BPD Cabang	BPD Cabang	BPD Cabang	BPD Cabang	KKOPD	BPD Cabang	Bappeda
4. Supervising Body at Prov.	BPD	BKPD: BRI UK: BPD BKPD: BRI	BPD	BPD	BPD	BPD	Kanwil Koperasi	BPD	Bappeda
5. Interest Rate (per month)	3.7 (average)	3.3 - 4.0	3.3	2 - 3	3.3	1.5	2	3.3	2
6. Savings (forced)	6.5-20% of Loan	1.0% of First Loan	3.3% of Loan					3.3% of Loan	
7. Savings (voluntary)	Beginning in pilot area m. 4-84	No	No	No	No	No	No	No	No
8. Interest paid on savings	15% yr	6% yr	No	No	No	No	No	No	No
9. Loans outstanding	1.5 Bil.				0.008 Bil.			0.3 Bil.	Unknown
10. Post/or other system for reaching desa	Yes	None			None	Limited mobil banking	None	Based in desa	None
11. Loan type	Trader	Trader	Trader		Trader	Small Industry	Trader	Trader	Anyone/ anything
12. Arrearage	1.6%	Unknown			Est. 15% of outstanding loans			6.5%	

CHAR/NAME	C. JAVA BKK	W. JAVA LPK/BKPD*	BENGKULU BKK	ACEH LKK	KALSEL KURK	NTB/BPD (channel sys) BPD	NTB/ Koperasi KUD	E. JAVA KURK	NTT LUB
13. Number of administering employees	3	3	3		3	1/cabang	3	2	5
14. Audit system	Yes	No	No	No	No	No	No	No	No
15. Loan Period	3 mo.	3 mo.	3 mo.	Not yet finalized likely 3-12 mos.	3 mo.	3 mo.	3 mo.	3-6 mo.	6-12 mo.
16. Staff Incentive System	Yes - 10% of profit	No	No	No	No	No	No	Yes 4% of total re-payments	No

* BKPD is not supported by PDP but has the same operating characteristics as the LPK

Source: PDP Credit Adviser

B K K O R G A N I Z A T I O N



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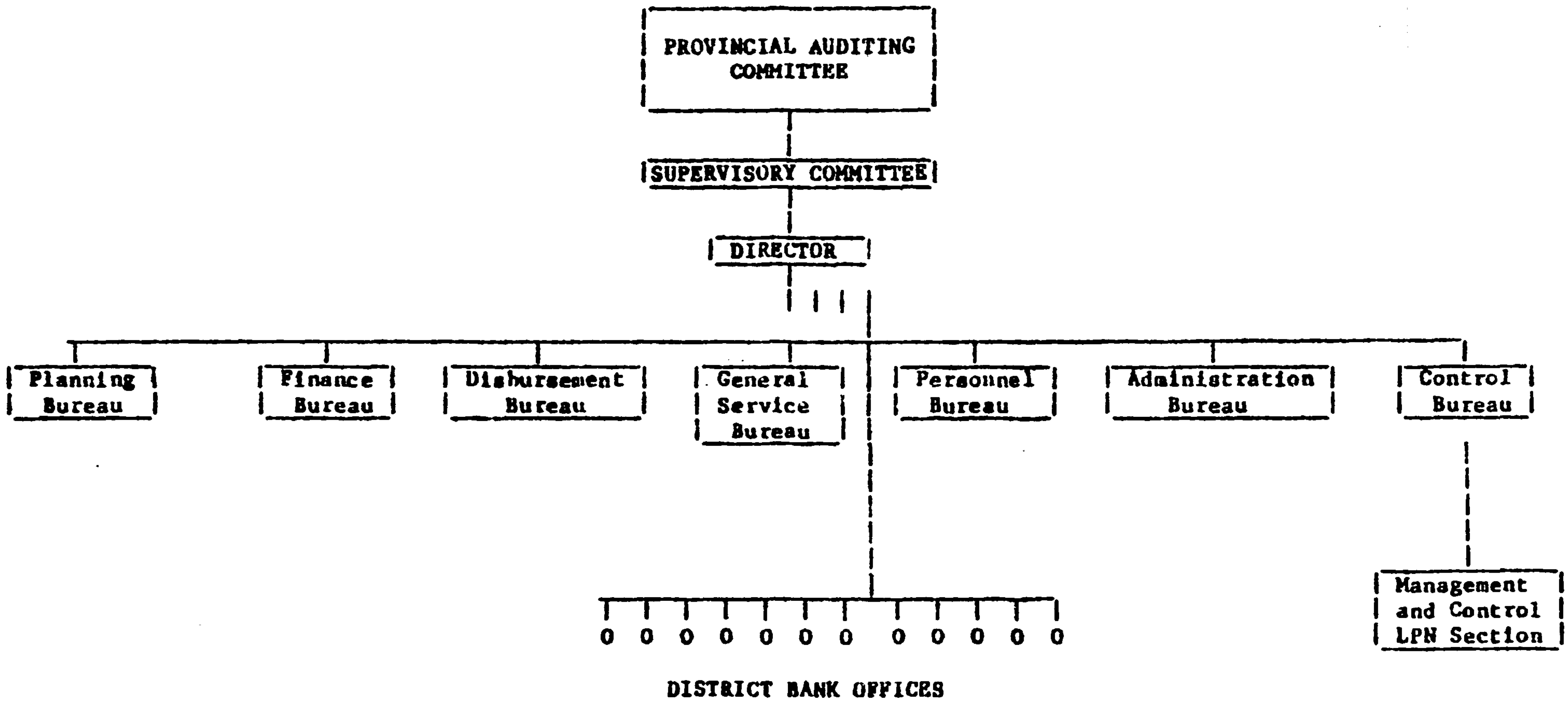
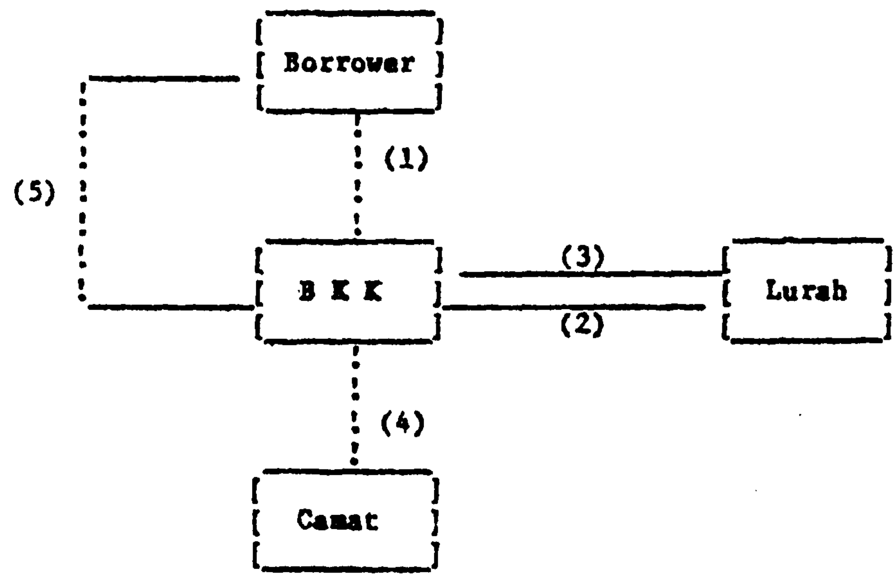
ORGANIZATIONAL STRUCTURE PROVINCIAL DEVELOPMENT BANK, WEST SUMATRA



LOAN PROCESSING PROCEDURES IN THE BKK SYSTEM



(1) - Borrower applies for loan to BKK office or post

(2) - BKK processes application

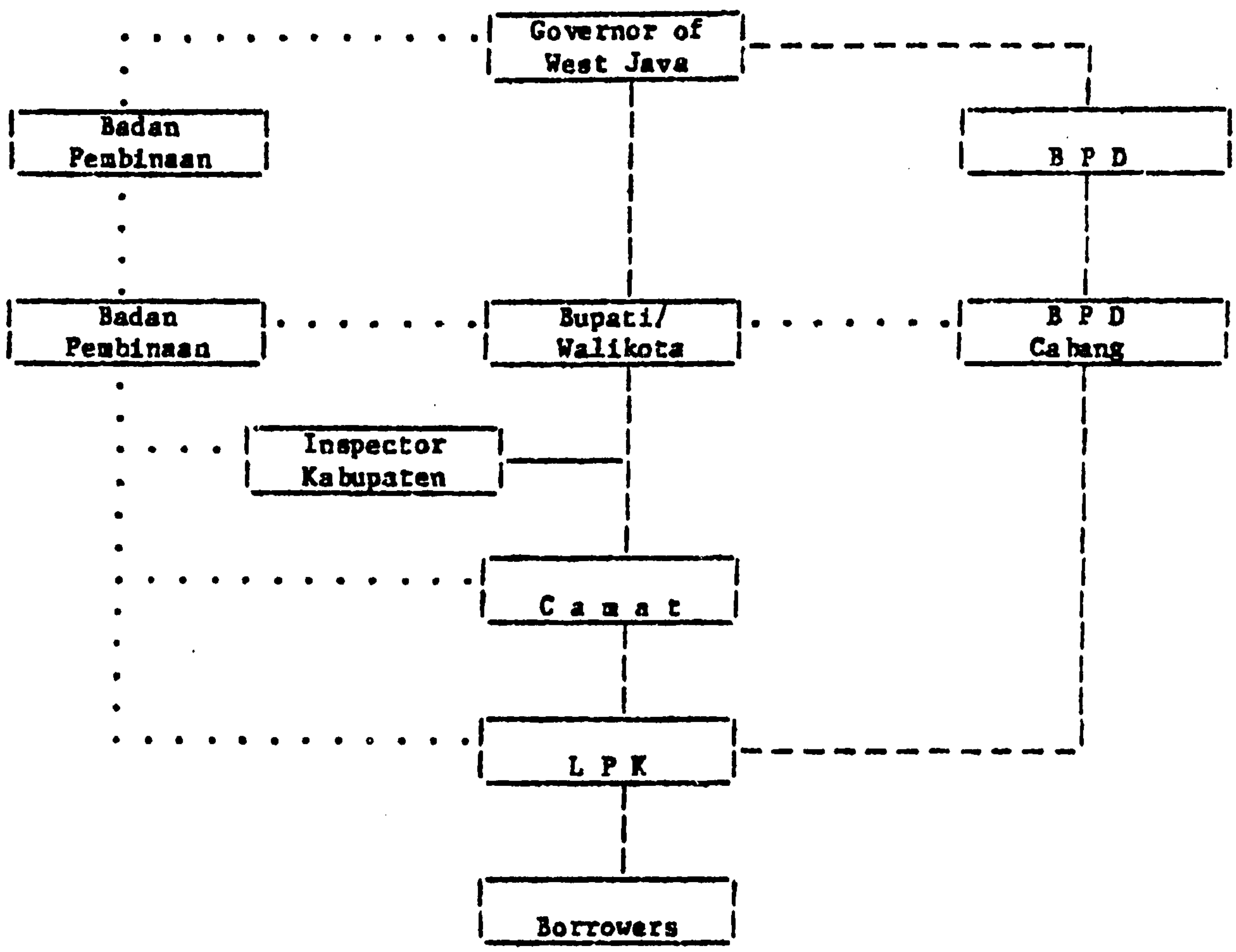
(3) - Application brought to Lurah for certification of "credit risk" and "community standing" of borrower

(4) - Information passed to Camat

(5) - Loan given to borrower

Note: Actions one through five are for first time borrowers. Action for follow-up loans between borrower and BKK if borrower has a good repayment record. Loan processing takes approximately two weeks for initial loan.

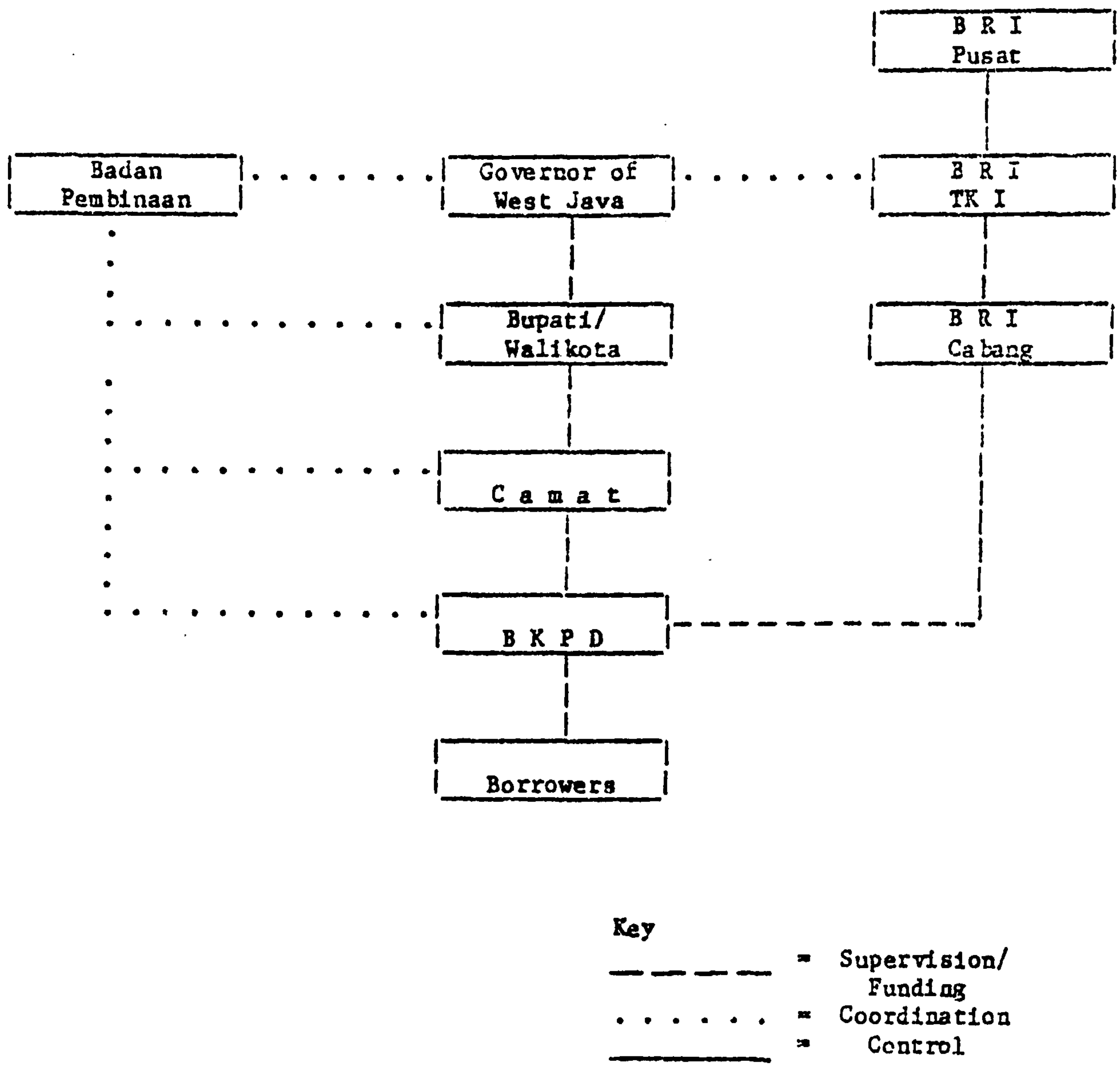
LPK ORGANIZATION



Key

- – – – = Supervision/ Funding
- . . . . . . = Coordination
- ——— = Control

BKPD ORGANIZATION



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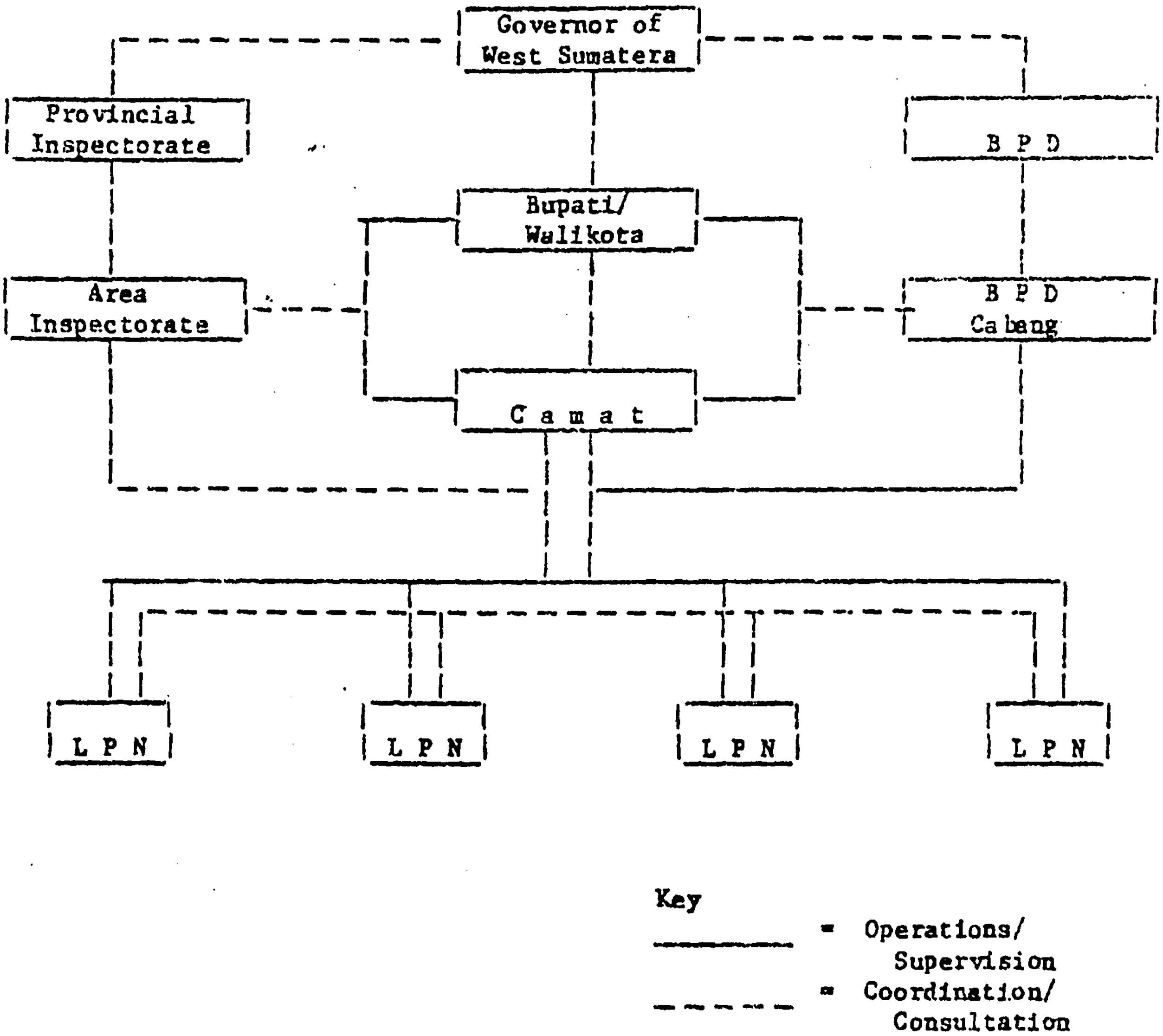
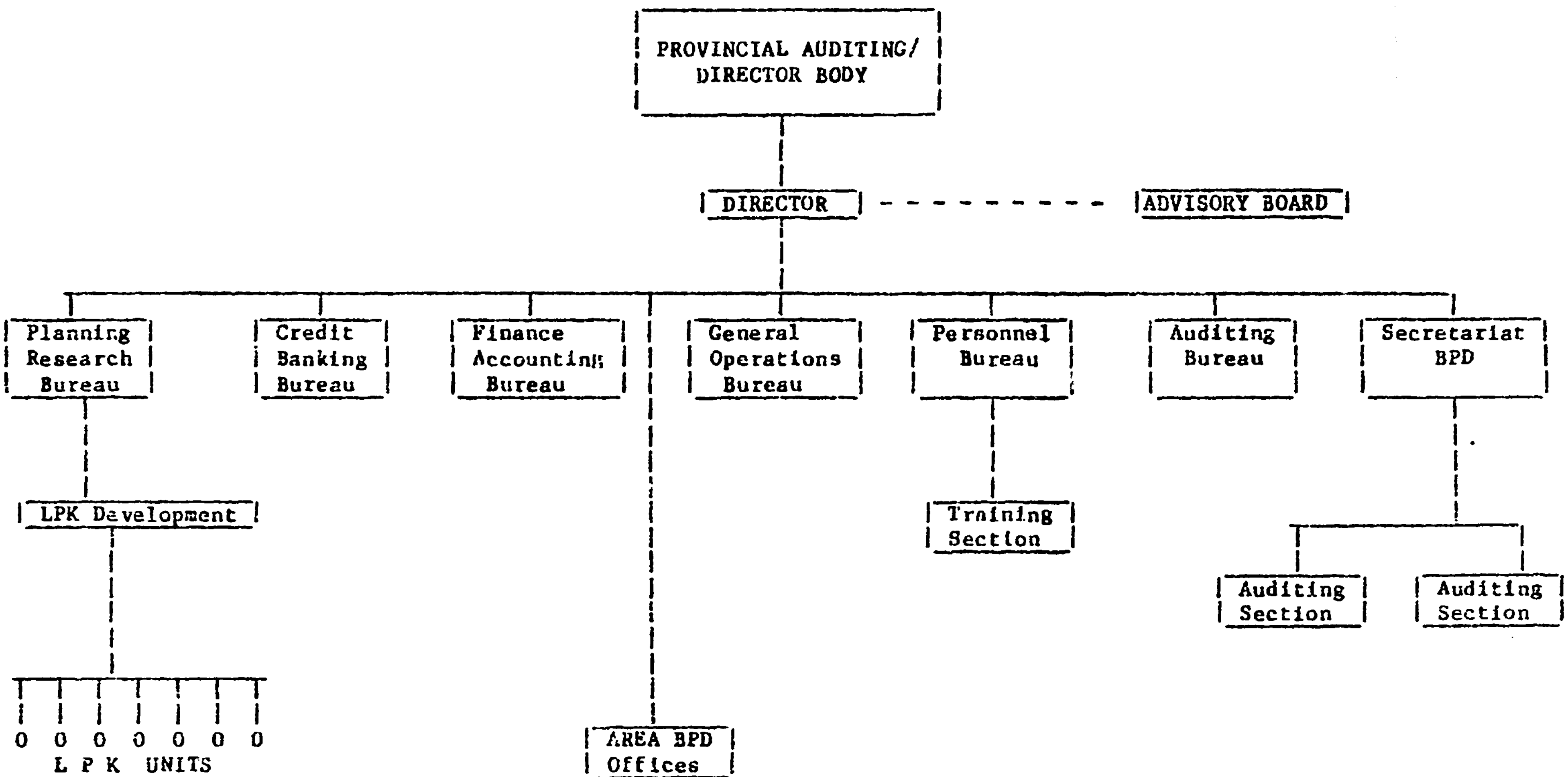
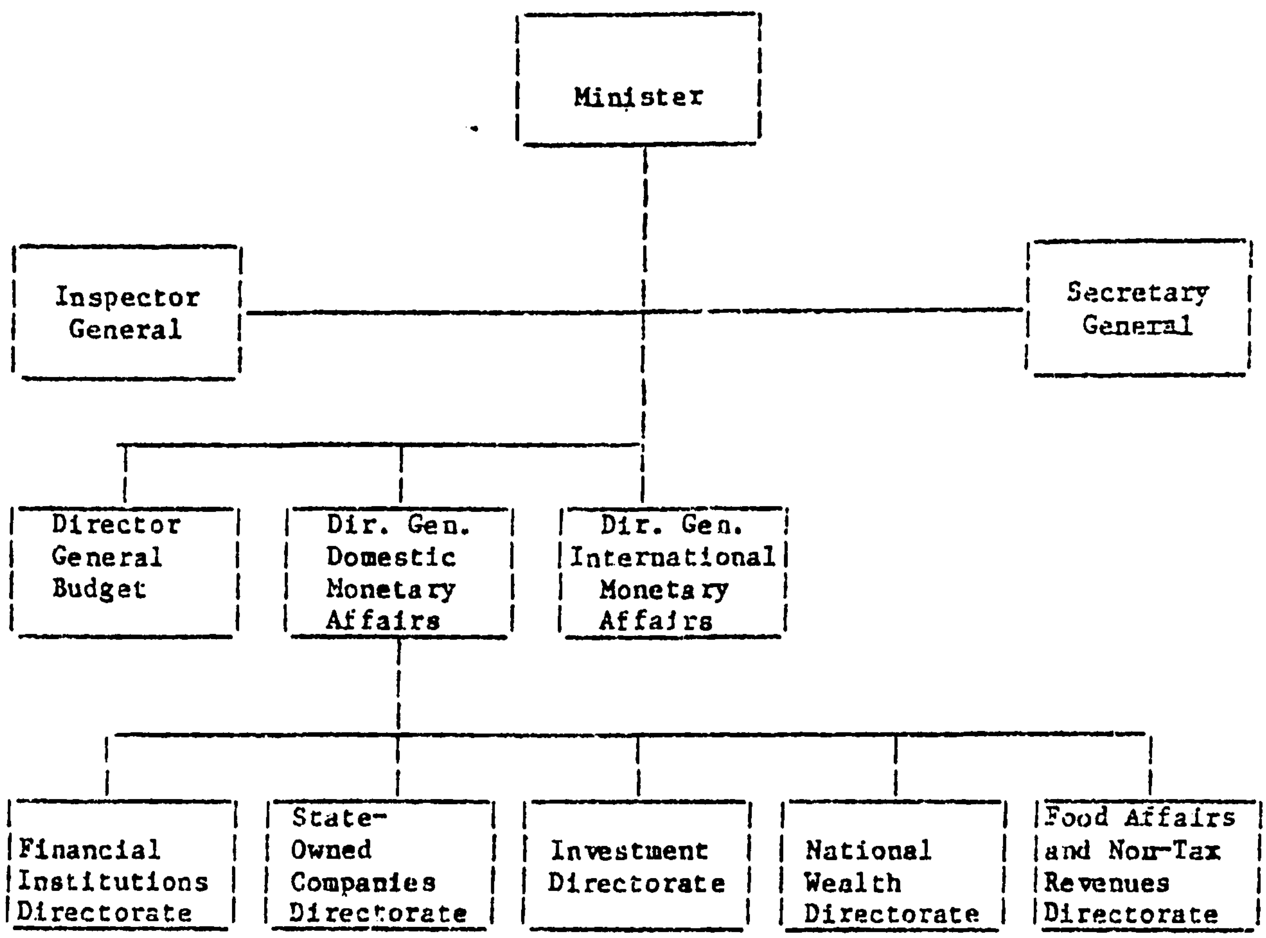
LPN WEST SUMATERA



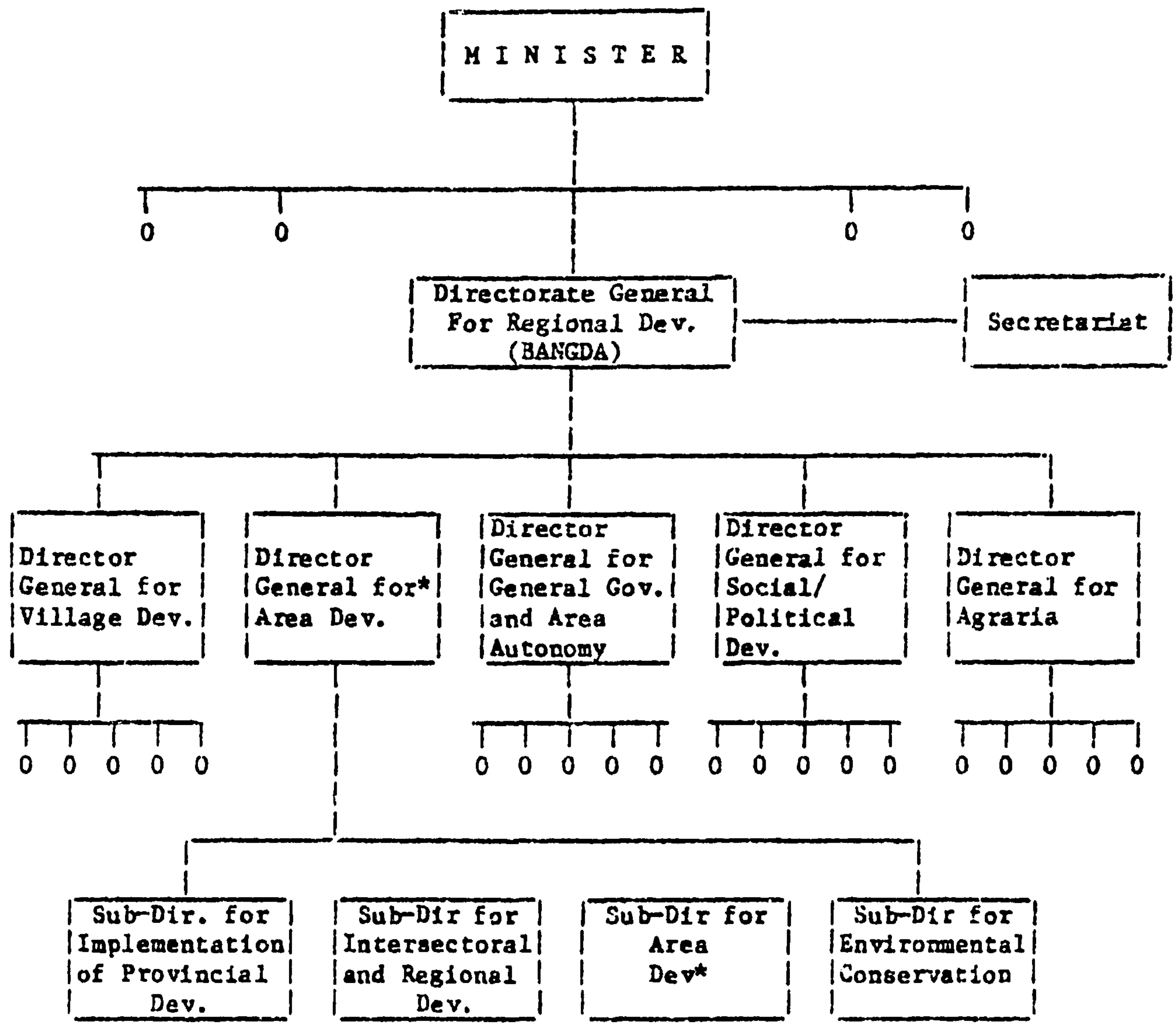
ORGANIZATIONAL STRUCTURE OF BPD WEST JAVA



ORGANIZATIONAL CHART
MINISTRY OF FINANCE



Ministry of Home Affairs



* FID Implementation Agency

Estimated Capitalization Schedule
(GOI and AID Funding)

Central Java

Foundation Capital:
(For units classified in ranks 3, 4 and 5)

Total Capital Inputs	$1,300,000
Estimated Number of units LOP	339

Expansion Capital
(For units classified in ranks 1 and 2)

Total Capital Inputs	$1,200,000
Estimated Number of units LOP	295

Total Capital:	$2,500,000
GOI Estimated Funds:	1,500,000
AID Proposed Funding:	1,000,000

Estimated Capitalization schedule
(GOI and AID Funding)

West Sumatera

Foundation Capital:
(For all units)

Total Capital Inputs	$2,000,000
Estimated number of units	561

Total Capital:	$2,000,000
GOI Committed Funding:	1,000,000
AID Proposed Funding:	1,000,000

Estimated Capitalization Schedule
(GOI and AID Funding)

West Java

Foundation Capital:
(For units classified in ranks 3, 4 and 5)

Total Capital Inputs	$1,300,000
Estimated number of units	288

Expansion Capital:
(For units classified in ranks 1 and 2)

Total capital inputs	$700,000
Estimated number of units	160

Total Capital:	$2,000,000
GOI Proposed Funding:	1,000,000
AID Proposed Funding:	1,000,000

CURRENT BPD CENTRAL JAVA/BKK EDP EQUIPMENT

Model	Specifications	Quantity
Televedio TS-816/40	Service processor, 128KB dynamic RAM, 16 terminal capacity, 42. 7MB 8" Winchester hard disk, 17. 4MB tape catridge drive	One
Televideo TS-800A	12" assynchronous desktop intelligent workstation, 64KB dynamic RAM	Three
Televideo	12" assynchronous desktop intelligent workstation, 64KB dynamic RAM, 2 floppy disk drives (each double sided, double density, 0.5MB)	One
ML-84P	OKI bidirectional dot matrix printer 200 CPS, 136 columns standard characters, 230 columns condensed type, serial interface	One
CI-Flo/55	C. ITOH Starwriter daisy wheel printer, 55 CPs, 163 columns, centronics parallel interface	One
Software	MmmOST version 2.11, CP/M 2.2 (operating systems; Optimum, dBase II, dUtil, dGraph, Quickcode (data base management); supercals, Multiplan, Microplan/Teleplan (electronic spread sheets); Wordstar, Spellstar, Mailmerge (wordprocessing); Statpack (statistics; Milestone (pl;anning); MBASIC (interpretre), CBASIC (compiler); Stats Graph, Super Chart (special business graphics); Tele Async (telecommunications); diagnostic diskette for TS-800 Series	One
TIS-36-500A	Uninterrupted power supply and stabilizer, 500 watts	One

Estimated Technical Costs

L/T Advisors:

171 person month @ $21,250 (average person month cost)
Estimated total L/T advisor cost = $3,633,750

Assumptions:
L/T Base monthly cost 16,500 (1)
L/T Average monthly cost 21,250 (2)

(1) Figure based on O/FIN
$128,000 year SPSC costs + $4,500/mo
(100% OH on salaries + 9% fixed fee

(2) Figure based on future value:
of 16,500, 3.5 yrs, 7.5% increase each
year.

S/T Advisors

61 person months @ $21,350 (average person month cost)
Estimated total S/T advisor cost = $1,302,350

Assumptions:
S/T base monthly cost 16,550 (1)
S/T average monthly cost 21,350 (2)

(1) Figure based on O/FIN
$13,000 PSC 60 day costs + 100%
OH on salaries + 9% fixed fee

(2) Figure based on future value
of 16,550, 3.5 yrs, 7.5% increase each year.

Total estimated L/T and S/T advisor cost =	$4,936,100
Indonesian sub-contractor services for evaluation	100,000
Other technical assistance contingency	130,000
Contingency	333,900
Total estimated technical assistance	$5,500,000

Estimated Equipment List for Typical Branch Unit

One (1) Fireproof safe approximate isze 70 cm x 50 cm)
Estimated cost US$ 500

One (1) Manual 18" typewriter
Estimated cost US$ 600

One (1) Calculator with printout, battery operated,
10 digit display
Estimated cost US$ 70

Total estimated cost per branch unit:
US$1,170 (year one prices)

Total estimated project cost:
US$2,000,000 (LOP cost)

TRAINING BUDGET ASSUMPTIONS

West Java:

1. New Petugas -

New petugas take a two week training program that includes BPD/BKPD/LPK activities, banking philosophy and operationals. Each new petugas. It is estimated that 1593 people will require this training over the LOP.

Base year per person training cost = $US396. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US517.

1593 (LOP number of trainees) x $US517 = $US823,581

2. New Petugas, start-up units -

New petugas in units reestablished will participate in an apprenticeship program and be placed in a work-study position at a good performming BKPD/LPK unit for one month. It is estimated that 500 new petugas will participate over LOP.

Base year per person training cost = $US75. Average LOP person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US100

500 (LOP number of trainees) x $US100 = $US50,000

3. Petugas -

Petugas already working at a functioning BKPD/LPK unit at the begining of the project will be given skills up grading training once every two years. This program will include training in basic operating skills, such as accounting and reporting, and in new products to be marketed by the BKPD/LPK, such as small industry loans and saving mobilization programs. Shown in subsequent tables, approximately 2426 trainees are expected over LOP.

Base year per person training cost = $US396. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US517

2426 (LOP number of trainees) x $US517 = $US1,254,242

4. Pengawas -

Because of their important supervision function, it is essential that pengawas are fully trained and that training is continually up-graded. For the first two years Pengawas will be given two week training at the BPD twice each year on operational, auditing and market development skills. For the years 3 to 5 training sessions will last one week and occur twice each year. 25 pengawas will be trained.

For years 1 - 2: Base year training cost = $US396. Average person training cost adjusted for cost increase of 10 percent/year, 2 year period = $US416.

100 (years 1 - 2 number of trainees) x $US416 = $US41,600

For years 3 - 5: Base year per person training cost = $US264. Average person training cost adjusted for cost increases of 10 percent/year, 3 year period = $US308

150 (years 3-5 number of trainees) x $US308 = $US46,200
Total training costs years 1 - 5 = $US87,800

In addition, the pengawas will be brought together in a three day conference to discuss special topics relating to operations, future planning, personnel matters, or other issues relevant to the system as a whole. The conference would include all pengawas and be held three times over LOP.

Base year per person training costs = $US100. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US130

75 (LOP number of trainees) x $US130 = $US9,750

5. Camats, Kepala Units, Lurahs -

Camats, petugas and lurahs will be given the opportunity to visit good performing BKPD/LPK units outside of their own district.

5a. Camats -

The camats will spend four days visiting other camats in successful areas, studying their role in promoting and guiding BKPD/LPK activities. Approximately 300 camats will participate two times in this comparative study over LOP.

Base year per person training cost = $US115. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US150

600 (LOP number of trainees) x $US150 = $US90,000

5B. Kepala Units -

The BPKD/LPK Kepala units will visit innovative BPKD/LPK units outside their own districts for a four day comparative study of the role of a kepala unit in a successful operation. Approximately 275 kepala unit will visit other BKPD/LPK units over LOP. Three visits over LOP are planned.

Base year per person training cost = $US92. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US120

825 (LOP number of trainees) x $US 120 = $US99,000

5C. Lurahs -

The lurahs from villages with poor performing units will travel to areas with good performing units for a one day comparison study. They will meet other lurahs with fully operational posts to learn the lurah's responsibilities and how to promote and administer the program at the village level. Approximately 960 lurahs from 150 BKPD/LPKs will take part in this program. The lurah would visit other units only once.

Base year per person training costs = $US20. Average LOP per person training cost adjusted for cost increase of 10 percent/year, 5 year period = $US27

960 (LOP number of trainees) x $US27 = $US25,920

6. Badan Pembinaan -

Members of the Badan Pembinaan (Governor's office, BPD, and BAPPEDA) will take part in a 2 week comparative study program to visit development banks, central banks and other financial institutions linked to village level credit institutions. Travel would be to other Taiwan, Philippines and Korea. Two groups of five participants would take part LOP.

Base year per person training costs = $US2,300. Average LOP per person training cost adjusted for cost increase of 10 percent/year, 5 year period = $US3000.

10 (LOP number of trainees) x $US3000 = $US30,000

WestJava estimated cost of training:

Total domestic	$US2,440,213
Total international	30,000
Total	$US2,470,293

WEST JAVA BPD/BKK ESTIMATED TRAINING COSTS

Trainee	Period	Location	Frequency	Type of Training	Number of Trainees	Cost/ Trainee	Total Estimated Cost
New Petugas	2 weeks	BPD Bandung	1 time each	Formal Basic	1593 LOP	$ 517	823,581
New Petugas	1 month	Good units	1 time each	Work-study	500	100	50,000
Petugas	2 weeks	BPD Bandung	1 time/ 2 years	In-service Update Training	2426 LOP	517	1,254,242
Pengawas	2 weeks	BPD Bandung	2 times/yr 5 yrs.	Formal	2501	351	87,800
Pengawas	3 days	BPD Bandung	3 times	Conference	75	130	9,750
Camats	4 days	Various BKPD/LPK Units	2 times/ each	Comparative Study	300 825	150 120	90,000 99,000
Petugas	4 days						
Lurahs	1 day				960	27	25,920
					Total Domestic Training		2,440,213
BPD Badan Pembinaan Members	2 weeks	International	2 times	Comparative Study	10 LOP		
					Total International Training		30,000
					Total Training		$2,470,213

WEST JAVA EMPLOYEE AND STAFFING LEVEL ESTIMATES

Current		977
New Positions		632
@217 + 103 units (320)(s)		1600

Year	1	2	3	4	5	Total	
Total Positions	977					1600	
Turnover/Yr.	195	195	170	193	217		
New Positions Added/Yr	0	156	156	156	155		623
Current Year Beginning Employees	977	977	1133	1289	1445		
Total Employees End of Year	977	1133	1289	1445	1600		
Total "New" Employees/Yr.	195	351	326	349	372		1593
Total "Old" Employees	782 (391)	782 (391)	1615 (808)	1096 (548)	1228 (614)		

TRAINING BUDGET ASSUMPTIONS

Central Java:
All calculations are based on actual BPD/BKK Training Activities

1. New Petugas -

New petugas will take a two week training program that includes BPD/BKK activities, banking philosophy and operationals. Each new petugas will attend. It is estimated that 1900 people will require this training over the LOP.

Base year per person training cost = $US396. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US517.

1900 (LOP number of trainees) x $US517 = $US982,300

2. New Petugas, start-up units -

New petugas in units reestablished will participate in an apprenticeship program and be placed in a work-study position at a good performming BKK unit for one month. It is estimated that 500 new petugas will participate over LOP. Base year per person training cost = $US75. Average LOP person training cost adjusted for cost incraases of 10 percent/year, 5 year period = $US100

500 (LOP number of trainees) x $US100 = $US50,000

3. Petugas -

Petugas already working at a functioning BKK unit at the begining of the project will be given skills up grading training once every two years. This program will include training in basic operating skills, such as accounting and reporting, and in new products to be marketed by the BKK, such as small industry loans and saving mobilization programs. Shown in subsequent tables, approximately 3800 trainees are expected over LOP. Base year per person training cost = \$US396. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = \$US517

3800 (LOP number of trainees) x \$US517 = \$US1,964,600

4. Pengawas -

Because of their important supervision function, it is essential that pengawas are fully trained and that training is continually up-graded. Pengawas will be given one week training at the BPD twice each year on operational, auditing and market development skills. 35 pengawas will be trained over LOP.

Base year per person training costs = \$US198. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = \$US258

350 (LOP number of trainees) x \$US258 = \$US90,300

In addition, the pengawas will be brought together in a three day conference to discuss special topics relating to operations, future planning, personnel matters, or other issues relevant to the system as a whole. The conference would include all pengawas and be held three times over LOP.

Base year per person training costs = $US100. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US130

105 (LOP number of trainees) x $US130 = $US13,650

5. Camats, Kepala Units, Lurahs -

Camats, petugas and lurahs will be given the opportunity to visit good performing BKK units outside of their own district.

5A. Camats -

The camats will spend four days visiting other camats in successful areas, studying their role in promoting and guiding BKK activities. Approximately 250 camats will participate two times in this comparative study over LOP.

Base year per person training cost = $US115. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US150

750 (LOP number of trainees) x $US150 = $US112,500

5B. Kepala Units -

The BKK Kepala units will visit innovative BKK units outside their districts for a four day comparative study of the role of a kepala unit in a successful operation. Approximately 400 kepala unit will visit other BKK units over LOP. Three visits over LOP are planned.

Base year per person training cost = $US92. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US120

1200 (LOP number of trainees) x $US 120 = $US144,000

5C. Lurahs -

The lurahs from villages with poor performing units will travel to good performing units for a one day comparison study. They will meet other lurahs with fully operational posts to learn the lurah's responsibilities and how to promote and administer the program at the village level. Approximately 750 lurahs from 150 BKKs will take part in this program. The lurah would visit other units only once.

Base year per person training costs = $US20. Average LOP per person training cost adjusted for cost increase of 10 percent/year, 5 year period = $US27

750 (LOP number of trainees) x $US27 = $US20,250

6. Badan Pembinaan -

Members of the Badan Pembinaan (Governor's office, BPD, BAPPEDA, Kooperasi) will take part in a 2 week comparative study program to visit development banks, central banks and other financial institutions linked to village level credit institutions. Travel would be to other Taiwan, Philippines and Korea. Two groups of five participants would take part LOP. Base year per person training costs = $US2,300. Average LOP per person training cost adjusted for cost increase of 10 percent/year, 5 year period = $US3000.

10 (LOP number of trainees) x \$US3000 = \$US30,000

Central Java estimated cost of training:

Total domestic	\$US3,377,600
Total international	30,000
Total	\$US3,407,600

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CENTRAL JAVA BPD/BKK ESTIMATED TRAINING COSTS

Trainee	Period	Location	Frequency	Type of Training	Number of Trainees	Cost/ Trainee	Total Estimated Cost
New Petugas	2 weeks	BPD Semarang	1 time each	Formal Basic	1900 LOP	$ 517	$ 982,300
New Petugas (start-up units)	1 month	Good Performing BKKs	1 month	Work Study	500	150	50,000
Petugas	10 days	BPD Semarang	1 time/ 2 yrs.	In-service Update Training	3800	517	1,964,600
Camats	4 days	Various BKK Units	3 times/ each	Comparative Study	750	150	112,500
Kepala Units	4 days				1200	120	144,000
Lurahs	1 day				750	27	20,250
Pengawas	1 week	BPD Semarang	2 times/ year	Formal	350	258	90,300
Pengawas	3 days	BPD Semarang	3 times	Conference	105	130	13,650
						Total Domestic Training	3,377,600
BPD Badan Pembinaan Members	2 weeks	International	2 times	Comparative Study	10		
						Total International Training	30,000
						Total Training	3,407,600

CENTRAL JAVA BKK EMPLOYEE AND STAFFING LEVEL ESTIMATES

Year	1	2	3	4	5	TOTAL
Total Positions	1237				2455	1218 new positions 600 turnover in current positions over 5 years
Turnover/Yr.	(160)	(120)	(120)	(100)	(100)	
New Positions Added/Yr	244	244	244	244	242	1218
Current Year Beginning Employees	1237	1481	1725	1969	2213	
Total Employees End of Year	1481	1725	1969	2213	2455	
Total "New" Employees/Yr.	404	364	364	344	342	1818
Total "Old" Employees	1077 (539)	1361 (681)	1605 (803)	1869 (935)	2113 (1057)	

TRAINING BUDGET ASSUMPTIONS

West Sumatera:

1. New Petugas -

New petugas will take a two week training program that includes BPD/LPN activities, banking philosophy and operationals. Each new petugas will attend. It is estimated that 562 people will require this training over the LOP.

Base year per person training cost = $US396. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US517.

562 (LOP number of trainees) x $US517 = $US290,554

2. Petugas -

Petugas already working at a functioning BKPD/LPN will be given skills up grading training once every two years. This program will include training in basic operating skills, such as accounting and reporting, and in new products to be marketed by the LPN, such as small industry loans and saving mobilization programs. Approximately 4242 trainees are estimated over LOP.

Base year per person training cost = $US396. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US517.

4242 (LOP number of trainees) x $US517 = $US2,193,114

3. Pengawas -

Because of their important supervision function, it is essential that pengawas are fully trained and that training is continually up- graded. For the first two years Pengawas will be given two week training at the BPD twice each year on operational, auditing and market development skills. For years 3 thru 5 of the project training sessions will last one week and occur twice each year. 12 pengawas will be trained.

For years 1 - 2: Base year training cost = $US396. Average person training cost adjusted for cost increase of 10 percent/year, 2 year period = $US416.

48 (years 1-2 number of trainees) x $US416 = $US19,968

For years 3 - 5: Base year per person training cost = $US264. Average person training cost adjusted for cost increases of 10 percent/year, 3 year period = $US308.

72 (years 3-5 number of trainees) x $US308 = $US22,176
Total training cost years 1 - 5 = $US42,144.

In addition, the pengawas will be brought together in a three day conference to discuss special topics relating to operations, future planning, personnel matters, or other issues relevant to the system as a whole. The conference would include all pengawas and be held three times over LOP.

Base year per person training costs = $US100. Average LOP per person training cost adjusted for cost increases of 10 percent/year, 5 year period = $US130.

40 (LOP number of trainees) x $US130 = $US5,200

4. Camats, Kepala Units, Lurahs -

Camats visit good performing LPN units outside of their own district.

4a. Camats -

The camats will spend four days visiting other camats in successful areas, studying their role in promoting and guiding LPN activities. Approximately 80 camats will participate two times in this comparative study over LOP.

Base year per person training cost = $US115. Average LOP per person training cost adjusted for cost inscreases of 10 percent/year, 5 year period = $US150.

160 (LOP number of trainees) x $US150 = $US24,000

5. Badan Pembinaan -

Members of the Badan Pembinaan (Governor's office, BPD, and BAPPEDA) will take part in a comparative study program to visit development banks, central banks and other financial institutions linked to village level credit institutions. Travel would be to other Taiwan, Philippines and Korea. Two groups of five participants would take part LOP.

Base year per person training costs = $US2.300. Average LOP per person training cost adjusted for cost increase of 10 percent/year, 5 year period = $US3,000.

10 (LOP number of trainees x $US3,000 = $US30,000

WEST SUMATERA LPN EMPLOYEE
AND STAFFING LEVEL ESTIMATES

	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Total Positions	561 x 3 = 1683					
Turnover/ Yr.	42	42	42	42	49	
New positions/ added/yr	-	-	-	281	281	562
Current year beginning employees	1683	1683	1683	1683	1964	
Total employees end of year	1683	1683	1683	1964	2245	
Total new employees/yr	42	42	42	323	330	779
Total "old" employees	1641 (821)	1641 (821)	1641 (821)	1641 (821)	1915 (958)	4242

WEST SUMATERA BPD/LPN ESTIMATED TRAINING COSTS

Trainee	Period	Location	Frequency	Type of Training	Number of Trainees	Cost/Trainee	Total Estimated Cost
New Petugas	2 weeks	BPD Padang	Once	Formal	562 LOP	$517	$ 290,554
Petugas	2 weeks	BPD Padang	One/two years	Formal	4242	517	2,193,114
Pengawas	1-2 weeks	BPD Padang	Twice year/ five year	Formal	120	351	42,144
Pengawas	3 days	BPD Padang	3 times	Conference	40	130	5,200
Camats	4 days	Various LPN Units	3 times/ each	Comparative study	160	150	24,000
						Total Domestic Training	$2,555,012
BPD Badan Pembinaan Members	2 weeks	International	2 times	Comparative Study	10	Total International Training	30,000
						Total	$2,585,012

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West Sumatera estimated cost of training:

Total domestic	$US2,555,012
Total international	$US 30,000
Total	$US2,585,012

Annex G, page 1

DRAFT

ACTION MEMORANDUM FOR AA/ASIA

Subject: Vehicle Waiver Request

Problem: Your approval is required to waive restrictions of Section 636 of the Foreign Assistance Act of 1961, as amended (the Act), and to authorize a source/origin componentry waiver allowing the purchase of 46 jeeps and 5 mini-buses. All of these vehicles are assembled in Indonesia using components from the United States or Code 935 countries. Under Delegation of Authority No. 40, you have the authority to waive source/origin requirements for the procurement of commodities up to $5,000,000 per transaction.

(A) Cooperating Country: Indonesia
(B) Project: Financial Institutions Development (497-0341)
(C) Authorizing Document:
(D) Description of Goods: 46 AMC C-J7 jeeps (gas)
5 Toyota 12 passenger mini-buses (diesel)
(E) Approximate Value: $US475,000
(F) Source: Indonesia (components from U.S. and Japan)
Origin US (approx. $9,300) and Japan (approx. $9,000).

Discussion: The subject of vehicle waivers in connection with procurement for AID-Financed projects in Indonesia has been thoroughly addressed in the past several years. The most comprehensive guidance was provided in a blanket waiver signed by the Administrator on August 17, 1981, for the purchase of 200 jeeps and sedans. This was more recently followed by a waiver signed by you on March 28, 1983 for the purchase of 117 jeeps, pick-ups, and vans.

In an effort to foster the domestic vehicle assembly industry, the Government of Indonesia (GOI) restricts the importation of completely built-up foreign vehicles when such vehicles are assembled locally using imported components. Source/origin waivers for the purchase of non-US vehicles under these circumstances have been approved in the past on the condition that (A) the vehicles are clearly needed to insure project success and (B) the potential for other donor or GOI financing has been explored with the conclusion that there is no alternate source of financing to USAID.

A. AMC CJ-7 Jeeps. The vehicles in question are necessary to transfer the exceptionally rough roads in project areas. As outlined in the Project Paper, area supervisors play a critical role in the efficient operations of rural financial institutions. Supervisors must have the mobility to visit up to twenty widely disbursed units on a regular basis. Without the vehicles supervisors would need to rely on public transport which is very erratic and could not cover the 20 miles or so between units. Supervisors are also frequently called upon to transfer physical funds, personnel, office equipment and materials between units. One jeep would be stationed in Jakarta for consultants and GOI use.

The 46 AMC Jeeps in this waiver request are assembled in Indonesia by Jakarta Motors, an Indonesian company operating under License from American Motors Company in the US. AMC officials in the US have reconfirmed their preference that AID purchase jeeps in Indonesia from Jakarta Motors rather than from AMC in the US. Thus, there is no objection from the only US manufacturer in the market for these vehicles, and approval of the waiver will have the added development affect of assisting an Indonesian US-Licensed enterprise.

It is AID policy, when vehicle waivers are proposed, to give preference to procurement of locally assembled vehicles using predominantly US-made components. AMC vehicles assembled by Jakarta Motors meet this criteria. Allowing their procurement will serve both US commercial and local interests. Nevertheless their price will be audited by the Mission to insure it is reasonable given post procurements.

B. Toyota Mini-Buses: Five, twelve passenger Toyota Mini-buses are requested. These vehicles will be based at provincial bank headquarters and in the capital city and used for: (1) transporting trainees; (2) inspection/auditing trips by headquarters based managers and advisors; and (3) inspection/auditing trips by supervisors based at the provincial bank headquarters but responsible for supervision of outlying units. The waiver justification is based on mini-buses in the US. Even if such right-hand drive vehicles were to be ordered from the US on a special basis, there would be a lack of servicing and spare parts facilities for those vehicles in Indonesia. The Toyota mini-buses are locally assembled using predominantly Japanese componentry. There are no locally-assembled mini-buses using US componentry. In both the AMC and Toyota cases the associated taxes will be borne by the GOI.

Recommendation: For the reasons presented above, pursuant to Handbook 1, Supplement B, Paragraph 4C2.d, it is recommended that you:

(1) Conclude that special circumstances exist meriting a waiver of the provisions of Section 636(i) of the Act;

(2) Approve a source/origin waiver for the project loan from AID Geographic Code 941 plus the Cooperating Country to Code 935 for procurement of the Toyota Mini-buses described above.

(3) Approve proprietary procurement of the AMC vehicles and Toyota Minibuses; and

(4) Certify that exclusion of procurement from other than the Cooperating Country and Countries included in Code 941 would seriously impede attainment of US Foreign Policy objectives and objectives of the foreign assistance program.

Approved __________________________

Disapproved __________________________

Date __________________________

Annex H

REPUBLIC OF INDONESIA
NATIONAL DEVELOPMENT PLANNING AGENCY
JAKARTA, INDONESIA

No. : 1211 /D.I/5/1984 Jakarta, 15 Mei , 1984

Mr. William P. Fuller
Director
USAID Mission
c/o American Embassy
Jakarta

Re : Financial Institutions Development Project

Dear Mr. Fuller,

On behalf of the Government of Indonesia, we hereby request a loan of up to fifteen million five hundred thousand United States Dollars ($ 15,500,000) and a grant of up to three million United States Dollars ($ 3,000,000) to implement the above project. The Government of Indonesia will provide the rupiah equivalent of $ 9,250,000 in cash and in kind to support this project over its planned seven (7) years life.

The purposes of the project are as follows :

1. To support the development of existing local rural credit systems that provide financial intermediation for village residents at reasonable and self sustaining cost;
2. To produce loan portfolios of employment generating activities and
3. To promote savings mobilization.

The project will be implemented by the Ministry of Home Affairs and the Ministry of Finance and their implementing units.

Looking forward to your favorable consideration.

Sincerely yours,

Muchtarudin Siregar
Deputy Chairman

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Annex I, page 1

BKPD

Income Statement	YR 0	YR 1	YR 2	YR 3	YR 4	YR 5	YR 6	YR 7	Annual Compounded Increase
Income –									
Interest Revenue		1,309,880	2,030,151	3,162,115	5,031,340	7,763,923	11,970,016	18,383,933	55.31%
Expenses –									
Interest Paid BPD Loans		–	–	57,120	142,800	228,480	285,600	285,600	
Interest Paid Other Deposits		209,309	251,171	301,405	367,798	434,023	520,827	624,993	
Interest Paid Savings Deposits		167,409	217,632	282,921	361,686	478,137	621,578	808,051	
Bad Debt		97,100	150,493	234,404	372,968	575,532	887,325	1,362,782	
Salaries		318,893	396,005	523,733	680,438	869,938	1,043,925	1,252,710	
Other Operational Costs		50,000	57,500	66,125	82,656	95,054	109,312	125,709	
Total Expenses		842,711	1,072,801	1,465,708	2,008,346	2,681,164	3,468,567	4,459,845	76.08%
Net Income		467,169	957,350	1,696,407	3,022,994	5,082,759	8,501,449	13,924,088	
Balance Sheet									
Assets –									
Cash	221,096	128,080	199,493	317,420	489,814	755,170	1,159,815	1,780,469	
Deposits	134,740	64,039	99,746	158,710	244,907	377,585	579,907	890,235	
Loans Outstanding	1,942,002	3,009,860	4,688,088	7,459,362	11,510,635	17,746,502	27,255,645	41,841,023	
Other	497,392	572,000	657,800	756,470	756,471	756,471	756,471	756,471	48.86%
Total	2,795,230	3,773,979	5,645,128	8,691,961	13,001,827	19,635,729	29,751,838	45,268,198	
Liabilities –									
BPD Loan	–	–	272,000	680,000	1,088,000	1,360,000	1,360,000	1,360,000	
Savings Deposits	930,050	1,209,065	1,571,785	2,043,320	2,656,316	3,453,211	4,489,174	5,337,009	
Other	1,162,827	1,395,392	1,674,471	2,009,365	2,411,238	2,893,486	3,472,183	4,166,620	
Total	2,092,877	2,604,451	3,518,256	4,868,685	6,155,554	7,706,697	9,321,357	10,913,629	26.61%
Equity –									
Equity	702,353	702,353	1,169,522	2,126,872	3,823,279	6,846,273	11,929,032	20,430,481	
Retained Earnings	–	467,169	957,350	1,696,407	3,022,994	5,082,759	8,501,449	13,924,088	
Total	702,353	1,169,522	2,126,872	3,823,279	6,846,273	11,929,032	20,430,481	34,354,569	74.32%
Total Liabilities & Equity	2,795,230	3,773,979	5,645,128	8,691,961	13,001,827	19,635,729	29,751,838	45,268,198	

L Y N

Income Statement	YR 0	YR 1	YR 2	YR 3	YR 4	YR 5	YR 6	YR 7	Annual Compounded Increase
Income –									
Interest Revenue		618,809	813,313	1,293,059	1,879,813	2,581,261	3,381,558	4,455,617	38.96%
Expenses –									
Interest Paid BPD/Provincial Loans		31,463	31,463	79,463	127,463	175,463	223,463	271,463	
Interest Paid Deposits		116,259	151,136	196,477	255,420	332,046	431,660	561,158	
Bad Debt		50,106	63,855	104,701	152,212	209,009	273,810	360,779	
Salaries		288,000	331,200	561,600	878,400	1,344,000	1,612,800	2,419,200	
Other Operational Costs		50,000	57,500	66,125	82,656	95,054	109,312	125,709	
Total Expenses		535,828	637,154	1,008,366	1,496,151	2,155,572	2,651,045	3,738,309	
Net Income		82,981	176,159	284,693	383,662	425,689	730,513	717,308	43.26%
Balance Sheet									
Assets –									
Cash	112,923	56,047	88,107	129,542	177,880	233,030	307,046	373,209	
Deposits	11,083	28,024	44,554	64,771	88,940	116,515	153,522	186,604	
Loan Outstanding	1,002,120	1,317,105	2,094,023	3,044,232	4,180,180	5,476,208	7,215,574	8,770,401	
Other	65,058	74,817	86,039	98,945	113,787	130,855	150,483	173,056	
Total	1,191,184	1,475,993	2,313,723	3,337,490	4,560,787	5,956,608	7,826,626	9,503,270	34.54%
Liabilities –									
Provincial Loans	130,978	130,978	130,978	130,978	130,978	130,978	130,978	130,978	
BPD Loans	131,214	131,214	531,214	931,214	1,331,214	1,731,214	2,131,214	2,131,214	
Savings Deposits	645,881	839,645	1,091,539	1,419,000	1,844,700	2,398,110	3,117,543	4,052,806	
Other	40,321	48,385	58,062	69,675	83,610	100,332	120,398	144,477	
Total	948,394	1,150,222	1,811,793	2,550,867	3,390,502	4,360,634	5,500,139	6,459,475	31.53%
Equity –									
Equity	242,790	242,790	325,771	501,930	786,623	1,170,285	1,595,974	2,326,487	
Retained Earnings	-	82,961	176,159	284,693	383,662	425,689	730,513	717,308	
Total	242,790	325,771	501,930	786,623	1,170,285	1,595,974	2,326,487	3,043,795	43.51%
Total Liabilities & Equity	1,191,184	1,475,993	2,313,723	3,337,490	4,560,787	5,956,608	7,826,626	9,503,270	

L P K

Income Statement	YR 0	YR 1	YR 2	YR 3	YR 4	YR 5	YR 6	YR 7	Annual Compounded Increase
Income –									
Interest Revenue		281,287	371,513	548,033	822,032	1,197,321	1,683,929	2,317,388	42.12%
Expenses –									
Interest Paid BPD		–	–	15,360	38,400	61,440	76,800	76,800	
Interest Paid Other Liabilities		57,875	84,463	101,355	121,626	145,951	175,141	210,170	
Interest Paid Deposits		18,357	23,865	31,024	40,331	52,431	68,160	88,608	
Bad Debt		20,852	27,540	40,625	60,936	88,756	124,828	171,786	
Salaries		150,067	186,355	246,463	320,206	409,362	491,260	589,511	
Other Operational Costs		25,000	28,750	33,063	38,022	43,725	50,284	57,827	
Total Expenses		272,151	350,973	467,890	619,521	801,685	986,473	1,194,702	
Net Income		9,136	20,540	80,143	202,511	395,636	697,456	1,122,686	122.97%
Balance Sheet									
Assets –									
Cash	65,095	23,438	34,575	51,861	75,537	106,237	146,200	205,054	
Deposits	6,023	11,719	25,930	25,930	37,769	53,118	68,160	103,027	
Loans Outstanding	417,031	550,797	812,503	1,218,728	1,775,124	2,496,559	3,439,712	4,842,277	
Other	4,867	25,000	28,750	33,063	38,022	43,725	50,284	57,827	
Total	493,016	610,954	893,115	1,329,582	1,926,452	2,699,639	3,705,297	5,209,185	40.05%
Liabilities –									
BPD Loans	–	–	128,000	320,000	512,000	640,000	640,000	640,000	
Savings Deposits	101,986	132,582	172,356	221,063	291,282	378,666	492,266	639,946	
Other	391,030	469,236	563,083	675,700	810,840	973,007	1,167,609	1,401,131	
Total	493,016	601,818	863,439	1,219,763	1,614,122	1,991,673	2,299,875	2,681,077	27.37%
Equity –									
Equity	–	–	9,136	29,676	109,819	312,330	707,966	1,405,422	
Retained Earnings	–	9,136	20,540	80,143	202,511	395,636	697,456	1,122,686	
Total	–	9,136	29,676	109,819	312,330	707,966	1,405,422	2,528,108	155.27%
Total Liabilities & Equity	493,016	610,954	893,115	1,329,582	1,926,452	2,699,639	3,705,297	5,209,185	

B K K

Income Statement	YR 0	YR 1	YR 2	YR 3	YR 4	YR 5	YR 6	YR 7	Annual Compounded Increase
Income -									
Interest Revenue		3,262,312	5,082,839	7,508,188	11,007,879	15,948,774	22,648,382	33,655,970	47.54%
Expenses -									
Interest Paid BPD		262,638	346,638	472,638	640,638	787,638	787,638	787,638	
Interest Paid Deposits		213,853	388,466	520,529	666,768	842,022	1,032,569	1,193,516	
Bad Debt		264,155	390,988	607,950	891,326	1,291,399	1,833,877	2,725,180	
Salaries		652,320	884,856	1,174,692	1,530,692	1,960,560	2,386,260	2,744,199	
Other Operational Costs		50,000	57,500	66,125	82,656	95,054	109,312	125,709	
Total Expenses		1,442,966	2,068,448	2,841,934	3,812,100	4,976,673	6,149,673	7,576,242	
Net Income		1,819,346	3,014,391	4,666,254	7,195,779	10,972,101	16,498,726	26,079,728	
Balance Sheet									
Assets -									
Cash	199,460	365,836	540,400	792,290	1,147,910	1,630,113	2,422,382	3,442,189	
Deposits	173,204	182,918	270,200	396,145	573,955	815,057	1,211,191	1,721,094	
Loan Outstanding	5,283,097	8,231,318	12,159,009	17,826,524	25,827,974	36,677,541	54,503,595	77,449,253	
Other	286,793	365,836	540,400	792,290	1,147,910	1,630,113	2,422,582	3,442,189	
Total	5,942,554	9,145,909	13,510,010	19,807,249	28,697,749	40,752,824	60,559,550	86,054,726	46.50%
Liabilities -									
BPD Loan	1,250,655	1,650,655	2,250,655	3,050,655	3,750,655	3,750,655	4,750,655	3,750,655	
Savings Deposits	1,188,074	2,158,145	2,891,826	3,704,378	4,677,901	5,736,497	6,630,642	8,399,670	32.23%
Other	92,922	106,860	122,889	141,322	162,520	186,898	214,933	247,173	
Total	2,531,651	3,915,660	5,265,370	6,896,355	8,591,076	9,674,050	12,982,050	12,397,498	
Equity -									
Equity	3,410,903	3,410,903	5,230,249	8,244,640	12,910,894	20,106,673	31,078,774	47,577,500	
Retained Earnings	-	1,819,346	3,014,391	4,666,254	7,195,779	10,972,101	16,498,726	26,079,728	
Total	3,410,903	5,230,249	8,244,640	12,910,894	20,106,673	31,078,774	47,577,500	73,657,228	55.10%
Total Liabilities & Equity	5,942,554	9,145,909	13,510,010	19,807,249	28,697,749	40,752,824	60,559,550	86,054,726	

Annex J, Page 1

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ACTION AID & INFO DCM ECON CHRON 11

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PP RUEHJA
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ZNR UUUUU ZZH
P 020101Z SEP 83
FM SECSTATE WASHDC
TO AMEMBASSY JAKARTA PRIORITY 7173
BT
UNCLAS STATE 250556

LOC: DISK 275
02 SEP 83
CN: 37352
CHRG: AID
DIST: AID

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E.O. 12356: N/A
TAGS

REF: STATE 234157

1. SUMMARY: SUBJECT PID WAS REVIEWED BY THE APAC ON AUGUST 15, 1983. USAID WAS REPRESENTED BY DENNIS ZVINAKIS AND DOUGLAS TINSLER. PID WAS APPROVED WITH THE FOLLOWING GUIDANCE PROVIDED FOR PP DEVELOPMENT:

A. PP SHOULD ANALYZE COMMUNITY PARTICIPATION IN PROJECT AND ENCOURAGE "BOTTOM UP" DEVELOPMENT MODES IN TOTAL PROJECT WHENEVER POSSIBLE.

B. TO THE EXTENT POSSIBLE, ECONOMIC ANALYSIS SHOULD ATTEMPT TO DEMONSTRATE LINKAGE BETWEEN CREDIT BEING OFFERED AND PRODUCTION AND EMPLOYMENT IMPACT. IT IS ALSO IMPORTANT TO DETERMINE THE POSSIBLE IMPACT OUR FUNDING MAY HAVE ON THE BENEFICIARY GROUP INCLUDING TERMS OF CREDIT, CRITERIA FOR LOANS, AND INTEREST RATES CHARGED.

C. AS A CONDITION OF ASSISTANCE, PP SHOULD PRESENT THE LINKAGE BETWEEN AID CONTRIBUTION TO CAPITAL INPUTS AND

INDONESIAN, AS OPPOSED TO STRICTLY GOI, AVAILABILITY OF FUNDING.

2. ISSUE AND DECISIONS:

A. ROLE OF THE PRIVATE SECTOR: THE APAC NOTED THAT THE FORMAL VILLAGE CREDIT SYSTEMS TO BE DIRECTLY AFFECTED BY THE PROJECT, BADAN KREDIT DESA, BADAN KREDIT KECAMATAN, BANK RAKYAT INDONESIA/UNIT DESA AND LEMBAGA PERKREDITAN ARE ALL PUBLIC SECTOR INSTITUTIONS. QUESTION RAISED WHETHER WE NOT ADVERSELY AFFECTING THE ENTRANCE OF PRIVATE NATIONAL CREDIT INSTITUTIONS IN THE RURAL CREDIT MARKET BY SUPPORTING THESE ESTABLISHED PUBLIC SECTOR CREDIT INSTITUTIONS OR, AT LEAST, BY NOT EXPLICITLY "BUILDING IN" A ROLE FOR PRIVATE BANKING CREDIT FACILITIES INTO THE PROJECT. USAID REPS RESPONDED THAT PRIVATE NATIONAL CREDIT INSTITUTIONS DO NOT HAVE A PRESENCE IN THE RURAL INDONESIAN ENVIRONMENT AT PRESENT AND IT WOULD TAKE AN

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ENORMOUS COMMITMENT OF RESOURCES, BOTH IN TERMS OF CAPITAL AND ALSO TRAINED MANPOWER, ON THE PART OF PRIVATE NATIONAL CREDIT INSTITUTIONS TO APPROACH SERVICES ALREADY PROVIDED BY THE PUBLIC SECTOR INSTITUTIONS NAMED ABOVE. WHILE ACCEPTING A ROLE FOR THE BKP ET AL., APAC FELT THAT THE INFORMAL CREDIT INSTITUTIONS WHICH EXIST IN THE RURAL AREAS AFFECTED BY THE PROJECT MIGHT BE A VEHICLE OF GREATER PRIVATE SECTOR INVOLVEMENT IN THE PROPOSED PROJECT, E.G. COLLECTIVE BORROWING, AND THAT THE PRIVATE, LARGELY URBAN, BANKS COULD HELP IN PORTIONS OF THE PROJECT LOAN PORTFOLIO.

B. APAC NOTED THAT THE PID DID NOT IDENTIFY THE SIZE AND RELEVANT SOCIO-ECONOMIC CHARACTERISTICS OF THE INTENDED BENEFICIARIES. TO ADEQUATELY DESIGN CREDIT PROGRAM AND PROJECT INTERVENTIONS AND TO EVALUATE THE IMPACT OF THESE INTERVENTIONS, IT WAS FELT THAT GREATER INFORMATION IS REQUIRED ON THE INTENDED BENEFICIARY GROUP. IT WAS AGREED THAT THIS ISSUE WOULD BE FULLY ADDRESSED IN THE PP.

C. POLICY DIALOGUE: THE APAC NOTED THAT THE LINKAGE BETWEEN OUR SUPPORTING INSTITUTIONAL CREDIT FACILITIES AND DIALOGUE ON POLICY CHANGES WITH GOI WAS NOT CLEAR IN THE PID. SPECIFICALLY, HOW SINCERE ARE GOI POLICY TRENDS IN THIS AREA? HOW FAR WILL THE GOI LET DEPOSIT RATES RISE? IT WAS RECOGNIZED THAT THE PROJECT IS NOT FEASIBLE UNLESS LOCAL SAVINGS ARE MOBILIZED, YET WITH AID'S DIRECT CAPITAL INPUT, WHICH WILL GENERATE GREATER LIQUIDITY CREDITS FROM THE INDONESIAN CENTRAL BANK, WON'T MOBILIZATION OF SAVINGS BECOME SECONDARY TO LENDING

OBJECTIVES? USAID REPS CONFIRMED THAT THE GOI IS INTERESTED IN ALLOWING MARKET FORCES TO DICTATE DEPOSIT RATES AND THAT RECENT GOI POLICY DIRECTIVES UNDERSCORE THIS POINT. THE USAID REPS ALSO STATED THAT RESOURCE MOBILIZATION WAS ESSENTIAL FOR A SELF-SUSTAINING FINANCE SYSTEM AND THE PROJECT WOULD EXPLORE WAYS OF ENCOURAGING GREATER DEPOSITS INCLUDING, AS SUGGESTED BY THE APAC, GOI GUARANTIES ON SAVINGS ACCOUNTS. FINALLY, THE APAC WAS CONCERNED THAT AS RESOURCE MOBILIZATION WAS A KEY ELEMENT TO THE SUCCESS OF THE PROJECT IT WAS IMPERATIVE THAT THIS PROJECT COMPONENT BE INITIATED IMMEDIATELY IN PROJECT IMPLEMENTATION. USAID REPS STATED THAT THE SAVINGS MOBILIZATION PROGRAM WOULD BEGIN IMMEDIATELY BUT SIGNIFICANT RESULTS WERE NOT ANTICIPATED UNTIL THE THIRD YEAR OF IMPLEMENTATION.

D. LOAN PORTFOLIOS: THE APAC NOTED THAT DURING THE LIFE OF THIS PROJECT THE LOAN PORTFOLIOS OF THE AFFECTED CREDIT SYSTEMS WILL BE EXPANDED FROM MAINLY TRADER CREDIT TO INCLUDE SMALL INDUSTRY LOANS, IN ORDER TO PROMOTE EMPLOYMENT GENERATION ACTIVITIES. HOWEVER, THE LINKAGE BT
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BETWEEN THE PROVISION OF CREDIT AND THE EXPECTED INCREASE IN PRODUCTION AND EMPLOYMENT IS NOT CLEAR. USAID REPS ACKNOWLEDGED THAT AS CREDIT RELATIONSHIPS ARE ESTABLISHED, LOANS FOR SMALL INDUSTRIES ACTIVITIES WILL BE A NATURAL CONSEQUENCE. NEVERTHELESS, IT WAS AGREED THAT THE ECONOMIC ANALYSIS IN THE PP SHOULD DEMONSTRATE THIS LINKAGE AND ECONOMIC FORCES WHICH WILL DISCOURAGE UNPRODUCTIVE USES OF LOAN FUNDS.

E. CONDITION OF ASSISTANCE: THE APAC NOTED THAT ACCORDING TO THE PID, A BUDGETARY SQUEEZE COULD SLOW THE RATE OF FUNDS RELEASED TO THE PROVINCES FOR ONLENDING TO LOWER LEVEL FINANCIAL INSTITUTIONS. GIVEN THIS, SHOULDN,T AID REQUIRE MINIMUM GOI CONTRIBUTIONS AS A CONDITION OF AID INVOLVEMENT? MISSION REPS AGREED THAT A MATCHING CONTRIBUTION FOR LENDING CAPITAL MAKES SENSE AND ,HAT AID SHOULD NOT GO OUT IN FRONT UNTIL THE GOI COMMITS RESOURCES TO THE PROJECT. THIS INTENDED GOI COMMITMENT AND THE TRIGGERING MECHANISM WHICH WOULD DISBURSE AID FUNDING SHOULD BE SPELLED OUT IN THE PP. ALSO, AS REATER PRIVATE SECTOR PARTICIPATION IS EVIDENT AND EATER AMOUNTS OF FUNDING ARE MOBILIZED FOR CREDIT, SSION SHOULD TAKE INTO ACCOUNT AID'S SCHEDULING AND NTRIBUTION VIS A VIS INDONESIAN, AS OPPOSED TO STRICTLY I, CAPITAL INPUTS.

F. OTHER ISSUES: THE APAC WONDERED IF THE PROJECT TITLE AS MISLEADING AS THE PROJECT WAS NOT INTENDED TO IMPACT

ON THE FINANCIAL INSTITUTION SECTOR OF INDONESIA BUT ON A RELATIVELY SMALL SEGMENT DEALING WITH RURAL FINANCE. APAC ALSO URGED THE MISSION TO REQUEST ASSISTANCE FROM OHIO STATE REGARDING PP DEVELOPMENT AS THIS PROJECT IS INNOVATIVE AND IS EXPERIMENTAL IN SCOPE. FINALLY, AS THE PROJECT IS INNOVATIVE, IT WAS SUGGESTED AFTER THE APAC MEETING THAT THE MISSION MAY WANT TO SUBMIT A DRAFT OF THE EVALUATION PLAN FOR THE PROJECT TO AID/W FOR COMMENT/REVIEW PRIOR TO INCLUSION INTO PP.

WITH REGARDS TO COMMODITIES, IT WAS NOT CLEAR TO THE APAC IF AID PROJECT FUNDS WILL FINANCE THE PURCHASE OF OFFICE EQUIPMENT, TRANSPORTATION VEHICLES, AS WELL AS INFRASTRUCTURE (OFFICE EXTENSIONS). IN ANY CASE, MISSION SHOULD BE AWARE OF ANY REQUIRED WAIVERS AND ENVIRONMENTAL STATEMENTS, IF NECESSARY, AND INCLUDE THEM IN THE PP.

3. APAC APPRECIATES INPUTS PROVIDED BY DENNIS ZVINAKIS AND DOUGLAS TINSLER. THEIR PARTICIPATION ASSISTED APAC IN UNDERSTANDING THE EXTENT OF THE PROBLEM AND THE DEVELOPMENT OF THE SPECIFIC AID TO ADDRESS THE PROBLEM. MISSION IS AUTHORIZED TO PROCEED WITH DEVELOPMENT OF THE PP. SHULTZ

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Annex K

5C(2) PROJECT CHECKLIST

Listed below are statutory criteria applicable to projects. This section is divided into two parts. Part A. includes criteria applicable to all projects. Part B. applies to projects funded from specific sources only: B.1. applies to all projects funded with Development Assistance Funds, B.2. applies to projects funded with Development Assistance loans, and B.3. applies to projects funded from ESP.

A. GENERAL CRITERIA FOR PROJECT

1. FY 1982 Appropriation Act Sec. 523; 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)?

The Committees in Appropriation of Senate and House were notified of the project through the FY 84 Congressional Presentation (Asia Program Page 71) and through a Congressional Notification

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

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 is required
4. FAA Sec. 611(b); FY 1982 Appropriation Act 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? (See AID Handbook 3 for new guidelines.)	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 Adminsitrator taken into consideration the country's capability effectively to maintain and utilize the project?	N.A.
6. FAA Sec. 209. Is project susceptible to 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.	No
7. FAA Sec. 601(a). Information and conclusions whether project will encourage efforts of the country to:	The project should directly encourage B, C, and E and indirectly encourage D by

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(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.

providing credit to private borrowers.

8. FAA Sec. 601(b). Information and conclusions 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 will finance small entrepreneurs who may be involved in sub-contracting arrangements or suppliers to U.S. private business and whose purchasing power will improved.

9. FAA Sec. 612(b), 636(h); FY 1982 Appropriation Act Sec. 507. 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.

Normal project disbursement procedures insure this.

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

Yes

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where applicable procurement rules allow otherwise?

12. FY 1982 Appropriation Act Sec. 521. 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 operative, and is such assistance likely to cause substantial injury to U.S. producers of the same, similar or competing commodity?

N.A.

13. FAA 118(c) and (d). Does the project take into account the impact on the environment and natural resources? If the project or program will significantly affect the global commons or the U.S., environment, has an environmental impact statement been prepared? If the project or program will significanlty affect the environment of a foreign countrt; has an environmental assessment been prepared? Does the project or program take into consideration the problem of the destruction of tropical forests?

The project has a limited impact on the environment, since it primarily provides technical assistance, capital and training funds for rural banks.

14. FAA 121(d). If a Sahel project, has a determination been made that the host government has an adequate system for accounting for and controlling receipt and expenditure of project funds (dollars or local currency generated therefrom)?

N.A.

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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?

The project is designed to benefit the rural poor. It focuses on developing rural banks that provide small loans to labor-intensive family enterprises. These banks will operate with a interest rate structure that insure long term viability. Loan operations will be located close to the village to lower borrower transaction costs. All supported financial institutions are autonomous and locally managed. A majority of borrowers are women.

b. FAA Sec. 103, 103A, 104, 105, 106. Does the project fit the criteria for the type of funds (functional account) being used?

Yes

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c. FAA Sec. 107. Is emphasis 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 is the latter cost-sharing requirement being 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"? (M.O. 1232.1 defined a capital project as "the construction, expansion, equipping or alteration of a physical facility or facilities financed by AID dollar assistance of not less than $100,000, including related advisory, managerial and training services, and not undertaken as part of a project of a predominantly technical assistance character.

No

f. 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
g. 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 builds on a credit system model well accepted by Indonesians. It supports institutional development of a rural banking network and develops manpower skills in rural areas.

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.	The GOI is able to repay the loan
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.

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c. ISDCA of 1981, Sec. 724(c) and (d). If for Nicaragua, does the loan agreement require that the funds be used to the maximum extent possible for the private sector? Does the project provide for monitoring uder FAA Sec. 624(g)? N.A.

3. Economic Support fund Project Criteria

a. FAA Sec. 531(a). Will this assistance promote economic or political stability? To the exte possible, does it reflect t. policy directions of FAA Sectic. 102? N.A.

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

c. FAA Sec. 534. Will ESF funds be used to finance the construction of the operation or maintenance of, or the supplying of fuel for, a nuclear facility? If so, has the President certified that such use of funds is indispensable to nonproliferation objectives? N.A.

d. 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.

5C(3) - STANDARD ITEM CHECKLIST

Listed below are the statutory items which normally will be covered routinely in those provisions of an assistance agreement dealing with its implementation, or covered in the agreement by imposing limits on certain uses of funds.

These items are arranged under the general headings of (A) Procurement, (B) Construction, and (C) Other Restrictions.

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?	Yes through competitive procurement
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 marine insurance companies authorized to do business in the U.S., will commodities be insured in the United States against marine risk with such a company?	N.A.
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	N.A.

could not reasonably be procured in U.S.)

5. FAA Sec. 604(g). Will construction or engineering services be procured from firms of countries otherwise eligible under Code 941, but which have attained a competitive capability in international markets in oneor these areas? — N.A.

6. 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

7. FAA Sec. 621. If technical assistance is financed, will such assistance be furnished by private enterprise on a contract basis to the fullest extent practicable? 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

8. International Air Transport. Fair Competitive Practices Act, 1974. If air transportation of persons or — Yes

property is financed on grant basis, will U.S. carriers be used to the extent such service is available?

9. FY 1982 Appropriation Act Sec. 504. 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? — N.A.

B. Construction

1. FAA Sec. 601(d). If capital (e.g., construction) project, will U.S. engineering and professional services to be used? — N.A.

2. FAA Sec. 611(c). If contracts for construction are to be financed, will they be let on a competitive basis to maximum extent practicable? — N.A.

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 (except for productive enterprises in Egypt that were described in the CP)? — N.A.

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-bloc countries? — Yes

4. Will arrangements preclude use of financing:

   a. FAA Sec. 104(f); FY 1982 Appropriation Act Sec. 525: (1) To pay for performance of abortions as a method of family planning or to motivate or coerce persons to practice abortions; (2) to pay for performance of involuntary sterilization as method of family planning, or to coerce or provide financial incentive to any person to undergo sterilization; (3) to pay for any biomedical research which relates, in whole or part, to methods or the performance of abortions or involuntary sterilizations as a means of family planning; (4) to lobby for abortion? — Yes

   b. FAA Sec. 620(g). To compensate owners for expropriated nationalized property? — Yes

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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. FY 1982 Appropriation Act, Sec. 503. To pay pensions, annuities, retirement pay, or adjusted service compensation for military personnel? — Yes

g. FY 1982 Appropriation Act, Sec. 505. To pay U.N. assessments, arrearages or dues? — Yes

h. FY 1982 Appropriation Act, Sec. 506. To carry out provisions of FAA section 209(d) (Transfer of FAA funds to multilateral organizations for lending)? — Yes

i. FY 1982 Appropriation Act, Sec. 510. To finance the export of nuclear equipment, fuel, or technology or to train foreign nationals in nuclear fields? — Yes

j. FY 1982 Appropriation Act, Sec. 511. Will assistance be provided for the purpose of aiding the efforts of the government of such country to repress the — Yes legitimate rights of the population of such country to the Universal Declaration of Human Rights?

k. <u>FY 1982 Appropriation Act, Sec. 515.</u> To be used for publicity or propaganda purposes within U.S. not authorized by Congress? Yes