PD-AAU-458

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: Bolivia

3. PROJECT NUMBER: 511-0577

4. BUREAU/OFFICE: LAC 05

5. PROJECT TITLE (maximum 40 characters): INDUSTRIAL TRANSITION (INTRA)

6. PROJECT ASSISTANCE COMPLETION DATE (PACD): MM 09 DD 30 YY 91

7. ESTIMATED DATE OF OBLIGATION (Under 'B:' below, enter 1, 2, 3, or 4)
A. Initial FY 87 B. Quarter 4 C. Final FY 90

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

A. FUNDING SOURCE	FIRST FY 87			LIFE OF PROJECT		
	B. FX	C. L/C	D. Total	E. FX	F. L/C	G. Total
AID Appropriated Total						
(Grant)	(600)	(1,000)	(1,600)	(3,218)	(6,782)	(10,000)
(Loan)	( )	( )	( )	( )	( )	( )
Other U.S. 1.						
Other U.S. 2.						
Host Country		3,745	3,745		7,500	7,500
Other Donor(s) Private Sector		15,000	15,000	12,500	40,000	52,500
TOTALS	600	19,745	20,345	15,718	54,282	70,000

9. SCHEDULE OF AID FUNDING ($000)

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

10. SECONDARY TECHNICAL CODES (maximum 6 codes of 3 positions each)
049 | 110 | 150 | 134 | 819 | 830

11. SECONDARY PURPOSE CODE: 150

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

A. Code	BR	BL	BF	BU			
B. Amount							

13. PROJECT PURPOSE (maximum 480 characters)

To increase the role of the Bolivian private sector in the country's economy through its enhanced participation and investment in productive industrial and selected service enterprises.

14. SCHEDULED EVALUATIONS
Interim MM 09 YY 88 | MM YY | Final MM 09 YY 91

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

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

The USAID Controller has reviewed the financial procedures described herein and hereby indicates his concurrence.

for Steven G. Liapis
Controller

17. APPROVED BY
Signature:
Title: George A. Wachtenheim
Acting Director, USAID/Bolivia
Date Signed: MM 4 DD 7 YY 87

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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INDUSTRIAL TRANSITION
(511-0577)

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ACRONYMS

ALBAPOR	-	Planta de Alimentos Balanceados de Portachuelo (Portachuelo Feed Mill).
ALBAT	-	Planta de Alimentos Balanceados de Tarija (Feed Milk Chicken Producers Association).
APA	-	Agricultural Producers Association.
CBF	-	Corporación Boliviana de Fomento (Bolivian Development Corporation)
COBOCE	-	Cooperativa Boliviana de Cemento (Cement Plant).
CODETAR	-	Corporación Regional de Desarrollo de Tarija (Regional Development Corporation of Tarija).
COFADENA	-	Corporación de las Fuerzas Armadas para el Desarrollo Nacional (Armed Forces Development Corporation).
COMIBOL	-	Corporación Minera Boliviana (Bolivian Mining Corporation).
CORDEBENI	-	Corporación Regional de Desarrollo del Beni (Regional Development Corporation of Beni).
CORDECRUZ	-	Corporación Regional de Desarrollo de Santa Cruz (Regional Development Corporation of Santa Cruz).
DDC	-	Departmental Development Corporation (Corporación Departamental de Desarrollo).
ENA	-	Empresa Nacional del Arroz (National Rice Company).
ENAF	-	Empresa Nacional de Fundiciones (National Smelting Enterprise.)
ENDE	-	Empresa Nacional de Electricidad (National Electricity Enterprise).
ENFE	-	Empresa Nacional de Ferrocarriles (National Railway Company).
ENTEL	-	Empresa Nacional de Telecomunicaciones (National Telecommunications Company).
EOPS	-	End of Project Status.
ESF	-	Economic Support Fund.

FABOCE	-	Fábrica Boliviana de Cerámica (Ceramic Plant).
FAC	-	Fábrica de Aceites (Edible Oil Plant).
FANCESA	-	Fábrica de Cemento S.A. (Cement Plant).
FANVIPLAN	-	Fábrica de Vidrio Plano (Glass Factory).
FVC	-	Fábrica de Envases de Vidrio (Glass Containers Plant).
GDP	-	Gross Domestic Products.
GOB	-	Government of Bolivia.
ICI	-	Intermediate Credit Institution.
IDB	-	Interamerican Development Bank
IEE	-	Initial Environmental Examination.
IESC	-	International Executive Service Corps.
IFC	-	International Finance Corporation.
INMETAL	-	Industrias Metálicas (Metals Plant).
INTRAC	-	Industrial Transition Commission.
IQC	-	Indefinite Quantity Contract.
IRR	-	Internal Rate of Return.
LAB	-	Lloyd Aéreo Boliviano (Bolivian National Airline).
MACA	-	Ministerio de Asuntos Campesinos y Agropecuarios (Ministry of Peasant Affairs and Agriculture).
MTCF	-	Market Town Capital Formation.
NEP	-	New Economic Program.
NSC	-	Bolivian National Securities Commission.
PAM	-	Planta de Alimentos de Maíz (Corn Feed Mill).
PAOM	-	Programa Agrícola de Oleaginosas y Maíz del Gran Chaco (Edible Oil Program).
PEQ	-	Planta Elaboradora de Queso (Cheese Plant).

PID	-	Project Identification Document.
PIL	-	Planta Industrializadora de Leche (National Milk Company).
PITASA	-	Industrias del Papel (Paper Plant).
PL-480	-	Public Law 480.
PPO	-	Privatization Promotion Officers.
SEC	-	Securities and Exchange Commision.
SOE	-	State-Owned Enterprise.
TA	-	Technical Assistance.
USAID	-	United States Agency for International Development.
YPFB	-	Yacimientos Petrolíferos Fiscales Bolivianos (Bolivian Petroleum Company).

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PROJECT AUTHORIZATION

Name of Country: Bolivia

Name of Project: Industrial Transition (INTRA)

Number of Project: 511-0577

1. Pursuant to Section 106 of the Foreign Assistance Act of 1961, as amended, I hereby authorize the Industrial Transition Project for Bolivia, involving planned obligations of not to exceed Ten Million United States Dollars (US$10,000,000) in grant funds (the "Grant") over a four-year period from the 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 project is four years from the date of initial obligation.

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

a. Source and Origin of Goods and Services (Grant)

Commodities financed by A.I.D. under the Grant shall have their source and origin in Bolivia or the United States, except as A.I.D. may otherwise agree in writing. Except for ocean shipping, the suppliers of commodities or services shall have Bolivia or the United States as their place of nationality, except as A.I.D. may otherwise agree in writing. Ocean shipping financed by A.I.D. under the Grant shall, except as A.I.D.

may otherwise agree in writing, be financed only on flag vessels of the United States.

b. Conditions Precedent to First Disbursement of Assistance

Prior to the first disbursement of the Assistance or to the issuance by A.I.D. of documentation pursuant to which disbursement will be made, Bolivia will, except as A.I.D. may otherwise agree in writing, furnish to A.I.D., in form and substance satisfactory to A.I.D.:

(i) an opinion of the Attorney General of Bolivia or other counsel acceptable to A.I.D. that this Agreement has been duly authorized and/or ratified by, and executed on behalf of, Bolivia and that it constitutes a valid and legally binding obligation of Bolivia in accordance with all of its terms;

(ii) a statement of the names of the persons holding or acting in the office of the Bolivian authorized representative specified in Section 9.2 of the Agreement, and a specimen signature of each person specified in such statement.

(iii) a written notification approving the creation of INTRAC with the names of the Board of Directors.

c. Covenants

Bolivia will covenant to take whatever legal steps are appropriate during Project implementation to effect the privatization of selected state-owned enterprises.

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I. SUMMARY

A. Background

The Industrial Tansition (INTRA) Project Identification Document was reviewed by the DAEC and approved for final design in December 1986. The DAEC requested that the PP: 1) set forth the Mission's privatization strategy, 2) describe the scope and functions of the Industrial Transition Commission (INTRAC), 3) analyze the probable sources of financing which could be mobilized for divestitures, 4) consider the different privatization options (rather than identifying specific enterprises to be divested), and 5) identify probable areas for divestiture in order to assess the kinds and amounts of inputs (such as technical assistance and credit) that may be required.

The Project Paper reflects these DAEC requests. In the case of specific privatization actions, the design team was able to go beyond the DAEC suggestion of identifying only probable areas for divestiture. Based on visits to the various Departmental Development Corporations (DDCs) and state-owned enterprises (SOEs), it was possible to identify certain state enterprises which are priority privatization candidates and can be expected to be ready for privatization shortly after Project implementation begins. A listing of these enterprises is included in Table 1 and on page 40 of this Paper.

B. Summary Strategy

The Project is a key component of USAID/Bolivia's private sector strategy as it has evolved during the last two years, particularly in the context of the free enterprise orientation of the democratic government of President Victor Paz Estenssoro. The strategy seeks to increase the role of the private sector in addressing the key constraints to Bolivia's economic development, which include: state control of the economy, inefficient financial markets, low levels of investments, and stagnant exports. It takes advantage of the existing policy "window of opportunity" to increase further the GOB's commitment to market mechanisms to set prices and wage levels and to allocate resources.

The Project strategy is to support the GOB efforts in privatization (as innitially described in its New Economic Program of August 1985), through technical assistance in the areas of management, valuation of assets, sales negotiations, public relations, and credit financing for working capital needs of privatized enterprises. A major ouput of this assistance is expected to be its catalytic role in attracting private investment. In carrying out the Project, USAID will maintain a relatively low profile, in recognition of the political sensitivity and nationalistic emotion surrounding privatization/divestiture decisions.

C. The Project

Privatization of SOEs is a high GOB priority and a key USAID/Bolivia policy objective. As a key element of USAID's assistance program and private sector strategy, the Industrial Transition Project will contribute to the attainment of two of USAID/Bolivia's program objectives: (1) economic stabilization and recovery, and (2) maintenance and strengthening of democratic government. The Project will further these objectives by facilitating successful implementation of the GOB's economic recovery program and by assisting the private sector to play a larger, more effective role in the country's economy. The Project is fully consistent with AID's privatization policy (State 189806), which directs USAIDs to assist with the divestiture of SOEs and the reduction of the role of governments in productive enterprises.

The goal of the Project is to promote Bolivia's economic recovery and sustained growth through more rational allocation of resources. The Project purpose is to increase the role of the Bolivian private sector in the country's economy through its enhanced participation and investment in productive industrial and service enterprises.

To attain the purpose, the Project will: (1) help establish a temporary Commission which will develop and implement an action plan to privatize SOEs, (2) assist in the actual privatization of selected enterprises currently owned by Bolivia's Departmental Development Corporations (DDCs) as a pilot effort which would subsequently be replicated on a larger scale, (3) assure that privatized SOEs are provided with sufficient technical assistance and start up capital to ensure the viability of their operations, and (4) promote the use of other privatization options, such as contracting for the management of state enterprises, in cases where outright divestiture is not feasible.

The Project will have three components:

1. Establishment of an Industrial Transition Commission (INTRAC). The INTRAC will consist of a mixed Commission of high level private and public sector representatives who will work under the policy guidance of the Minister of Planning. Initially, the main task of the Commission will be to develop a feasible privatization strategy and a plan for its implementation. Thereafter, the critical role of the INTRAC will be to develop, coordinate and carry out all actions leading to the transfer of SOEs to the private sector. INTRAC will also support the initiation of other privatization options for strategic state enterprises or for enterprises not suitable for immediate divestiture or closure.

2. Privatization Actions, under which divestitures and other privatization options will be carried out and technical assistance provided to help selected privatized SOEs during their initial stages of operation. The technical assistance will vary from enterprise to

enterprise, but it is anticipated that privatized enterprises will need assistance in the areas of production methods, management, marketing, and methods of financing operations. The purpose of this component will be to assure the operational viability and survival of the privatized SOEs in a competitive free-market environment.

3. Development of Financing Mechanisms to facilitate the transfer of SOEs to the private sector. This component entails the preparation of alternative financing packages, based on feasibility studies and understandings with DDCs and related GOB entities, for the transfer of SOEs to the private sector. A.I.D. funding for the financing packages will be minimal and limited to selected partial financing, through Bolivia's private banking system, of working capital requirements of privatized SOEs. A prime purpose of this limited financing would be to serve as a catalyst to attract additional investments from the private sector and the banking community and to facilitate the difficult transition period of privatized SOEs.

D. Project Funding

A.I.D. Life-of-Project (LOP) funding of $10 million in grant funds is proposed to finance Project activities during a four-year period. The A.I.D. contribution constitutes only 14.3 percent of the LOP cost, which is estimated at $70 million, including the planned GOB contribution of $7.5 million in local currency, $37.5 million in investment capital from Bolivia's private sector and a projected foreign investment total of $15 million.

The A.I.D. contribution is broken down as follows:

Category	($000)
Industrial Transition Commission	$ 995
Technical Assistance	$ 2,579
Working Capital for privatized SOEs	$ 5,496
Other Costs	$ 505
Contingencies	$ 425
Total	$10,000

E. Project Approval Factors

The project design team which prepared the Project Paper has concluded that the Project has a sound financial, economic, technical and social basis, and that Bolivia will establish an Industrial Transition Commission to implement it effectively. Also, it has determined that the Project will not have an adverse effect on the environment, and, therefore, a categorical exclusion has been recommended and approval based on the provisions of Section 262.2(C) of 22 CRF part 216 on environmental procedures.

F. Project Design Team

1. The USAID/Bolivia Project Design Team was composed of:

Angel M. Díaz	USAID/PD&I
Jaime Vizcarra	USAID/PD&I
Clark Joel	USAID/ECON
T.David Johnston	USAID/PRD
Mahlon Barash	USAID/PRD
Ernesto García	USAID/PRD

2. USAID/Bolivia contracted the services of the International Science and Technology Institute (ISTI) to assist in carrying out the various Project Analyses. The ISTI team of Consultants was composed of:

Robert Bond	Chief of Party
Ismael Benavides	Privatization Planning Advisor
William M. Berenson	Legal Advisor
Donald Rhatigan	Agroindustrial Specialist
Gastón Kohn	Asset Valuation Advisor

3. The Government of Bolivia counterparts were:

Gerardo Tejerina Villarroel	Consultant to the Ministry of Planning
Lic. Anibal Aguilar	Legal Counsel and Acting Subsecretary, Ministry of Planning.

The Project Paper was reviewed by the following USAID/Bolivia officials:

David A. Cohen	Mission Director
George A. Wachtenheim	Deputy Mission Director
Robert J. Asselin, Jr.	Chief, PD&I
Steven G. Liapis	Chief, Controller

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II. PROJECT BACKGROUND AND RATIONALE

A. Economic Background

Following a long period of military rule and economic deterioration, in 1982 a democratically elected government headed by President Hernán Siles Suazo, was permitted to take office. However, President Siles was unable to rule the country effectively. His attempts at economic reform were characterized by political expediency, acceding to the demands of special interests and key political groups, particularly the labor unions.

During Siles' term in office, the Bolivian economy deteriorated rapidly. Large and persistent fiscal deficits, an inelastic and dysfunctional revenue system, and large operating deficits of state enterprises resulted in substantial Central Bank credit expansion and increases in the money supply. The country's economic problems were aggravated by GOB attempts to control prices and interest rates, and to peg the official exchange rate at an increasingly overvalued level. As a result, the annual inflation rate increased from 30 percent in 1981 to 22,256 percent in 1985, while GDP dropped by 19 percent during the same period.

A major cause of the economic chaos under the Siles administration was the rapid growth of the operating deficits of the state-owned enterprises (SOEs). In addition to the financial drain of SOEs on the national treasury, the burden of harmonizing economic policies and managing the resources of the state enterprises overtaxed the limited capacities of the public sector, resulting in a significant loss of efficiency to the economy as a whole.

By late 1984, President Siles' inability to deal with the nation's difficulties and his faltering popular support led to the dissolution of his ruling coalition. To resolve the crisis, presidential elections were held in July 1985, a year earlier than scheduled. These national elections provided the country with its first critical opportunity to continue the democratization process begun in 1982. Victor Paz Estenssoro was elected President and took office on August 6, 1985.

The Paz Estenssoro government moved quickly to stabilize the economy, relying on market forces to allocate resources, set prices, establish wage levels, and fix the value of the exchange rate. Within a month of taking office, the new government had promulgated comprehensive economic reform measures designed to control inflation, rationalize government spending, improve the government's revenue base, reactivate productive activities and reorient the economy along free enterprise lines.

The main measures of the New Economic Program (NEP), otherwise known as Supreme Decree 21060, were the unification of the exchange rate, elimination of interest rate ceilings, removal of most restrictions on imports and exports, tax and tariff reforms, a wage freeze for public employees, liberalization of labor laws, reduction in credit expansion to both public and private sectors, and elimination of all price controls, except for state marketed goods and services, (e.g., petroleum products, electricity, the prices of which were increased in an attempt to eliminate the substantial operating deficits of SOEs). Moreover, the government signed an IMF Standby agreement specifying explicit targets for money supply, reducing the fiscal deficit, and increasing international reserves.

The results of these policies have been impressive. The rate of increase in the consumer price index was reduced from 22,756 percent to about 66 percent between January 1985 and December 1986 and is now averaging 24 percent on an annualized basis. As a proportion of GDP, the budget deficit of the consolidated public sector declined from 30 percent in 1984 to 13 percent in 1985 and 3.8 percent in 1986. The annual rate of expansion of bank credit to the public sector declined from 17,000 percent in 1985 to 20 percent in 1986, with a nearly parallel reduction in the rate of credit expansion to the private sector. As a result, the rate of increase in the money supply (M1) declined from over 6,000 percent in 1985 to only 25 percent in 1986.

The IMF team that visited Bolivia from August to September 1986 found the GOB in full compliance with all the June 30, 1986 targets in its Stand-By Agreement, except for the reduction of arrears to private suppliers, which was remedied by mid-July 1986.

Thus, a year and a half after assuming power, the Paz Government has made substantial progress towards economic stabilization. Significant progress has also been made toward restoring private sector confidence in the government and its economic policies. However, full economic reactivation has not yet occurred and the ownership and management of the SOEs remains a difficult political and economic problem.

The NEP provided the policy framework for a major step to rationalize the operation of state enterprises in order to improve their management and eliminate their contribution to the fiscal deficit. The two major policy decisions on SOEs included (a) the decentralization of COMIBOL (the State Mining Corporation) and YPFB (the State Petroleum Company) into regional enterprises; and (b) the dissolution of the Bolivian Development Corporation (CBF), which took place in March 1987, following the transfer of its companies to the Departmental Development Corporations (DDCs). The GOB's initiatives regarding reorganization of COMIBOL and YPFB and the dissolution of CBF represent two extremely important GOB policy decisions. The first of these is the decision to reduce the role of the state in productive activities. The second is the decision to use decentralization as a means of increasing the management efficiency of SOEs.

Now that initial economic stabilization has been achieved, the main task confronting the GOB is to reactivate the economy, which had a negative GDP growth rate of 2.9 percent in real terms in 1986. To arrest this decline, the GOB is currently implementing a series of activities designed to reactivate the economy and reinforce the NEP. These activities are establishing the essential basis for a market-based economic recovery program in which a vigorous private sector role in productive activities is an essential ingredient. The GOB's goal is to achieve a 3.5 percent yearly growth rate over the next three years. The plan calls for US$1,177 million in public investment spending during the period 1987-1989, a 10 percent increase in public salaries in 1987, lower domestic interest rates, an increase in concessional resource flows and an increase in private sector investment.

B. The Nature of Bolivia's Public Sector Enterprises

The Bolivian public sector is involved in a wide array of economic activities and is a significant source of employment. Currently, there are some 107 SOEs operating throughout the country. The state (both the central government and the Departmental Development Corporations) owns enterprises in virtually every sector of the economy, including agribusiness (dairy processing plants, sugar mills, feed plants, food processing), light industry (cement, bottling, matches, glass, ceramics, bricks) mining, hydrocarbons, transportation, banking, public utilities and services (hotels, airlines, gas stations, etc.).

These enterprises employ over 50,000 people and represent 13.3 percent of total public employment. In 1986, the operations of all SOEs accounted for 66 percent of the total public sector budget deficit of $314.4 million. This statistic becomes even more significant when one realizes that YPFB (the State Petroleum Company) is highly profitable and is the single most important contributor to GOB revenues.[1/] Besides being a drain on the GOB budget, the SOEs tend to discourage private sector investment in the industrial sectors in which they are involved and thus seriously impede the private sector-based recovery the GOB is seeking. Moreover, the goods and services provided by the public sector are typically of high cost and of poor quality.

The GOB classifies SOEs as strategic and non-strategic. Strategic SOEs are those which are perceived to be vital to the nation's national security and/or economic development; in general, a great deal of nationalism and political sensitivity surround strategic SOEs. The principal such enterprises are COMIBOL (Bolivian Mining Company), ENAF (National Smelting Enterprise), YPFB (the State Petroleum Company), ENFE (National Railroad Enterprise), ENDE (National Electricity Enterprise), ENTEL (National Telecommunications), and LAB (the National Airline).

Non-strategic enterprises are concentrated primarily in the agribusiness and light manufacturing sectors, most of which had been part of the CBF and were transferred to the Departmental Development Corporations (DDCs).[2/] Since most of these enterprises produce

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1/ In 1986, for instance, YPFB's contribution to government revenues was $427.5 million, or about 69.2% of the total revenue ($617.3 million).

2/ DDCs are decentralized public institutions charged with the task of designing and implementing development activities in each geographic department of the country. There is keen interest on the part of the DDCs to transfer recently acquired state enterprises to the private sector.

operating deficits, the DDCs are using resources, which could be used for regional infrastructure development projects, to cover these deficits. Many of these non-strategic SOEs are poorly managed since their primary goals are not productivity, efficiency, and profit, but employment. Generally, the managers of these SOEs have had few incentives to reduce costs since the COB has covered their operating deficits. Their existence also discourages private investments in the areas in which they are involved since investors are not inclined to compete with state enterprises which have a continual source of central government transfers.

A common trait of most of these enterprises is that they are over-engineered and over-built, compared with realistic demand. In many cases, SOEs were undertaken without adequate feasibility studies. Information on sources of supply, raw materials, transportation, or existing markets was often not taken into account when new SOEs were being planned. As a result, most SOEs are currently operating at far below (less than 50 percent) their established production capacity. Other plants (such as the ceramic plant in Cochabamba) cannot compete in quality and price with imported goods, because they were built with obsolete equipment.

Some SOEs were established in competition with existing private enterprises. Typical examples of these SOEs are the brick and cheese factories in almost every department. Since SOEs were not required to make a profit (or even to cover costs), they had an unfair advantage over similar private enterprises, and their existence stifled private investment. The low level of private investment has, in turn, affected economic growth, thereby hampering economic reactivation.

C. The Status of Privatization Efforts to Date

The new GOB has already demonstrated its political commitment to privatization, but to date it has been unable to develop a coherent and feasible plan to carry out this commitment. The main reasons for this are lack of resources and technical capability.

With the dissolution of the CBF, the GOB announced its intention to reduce the number of SOEs. While this was clearly a laudable objective, the government's decision to dissolve the CBF and transfer its enterprises to the DDCs has had two unfortunate consequences. First, the dissolution of CBF may have complicated the privatization process by increasing the number of actors and decision-makers involved. Second, these transfers have created a managerial problem and a fiscal drain at the regional level. Some of the DDCs realize this and are searching for ways to privatize these enterprises so that their efforts and resources can be directed to regional development activities. Several DDCs are already proceeding with plans to transfer SOEs to the private sector.

The DDC in Santa Cruz (CORDECRUZ) is the most advanced in its privatization efforts. A major negotiation is underway to lease ENA's rice silos to the Cámara Agropecuaria del Oriente (CAO), a producers association. Feasibility studies are being completed and valuations are in process for three of CORDECRUZ' SOEs which could be sold to producer groups. These are the cheese plant (PEQ), corn feed mill (PAM), and the Portachuelo feed mill (ALBAPOR). Once studies are completed and legal authorization is obtained, the sales can proceed. CORDEBENI is negotiating the sale of its rubber and cashews processing plants. CODETAR has also passed a resolution proposing the sale of ALBAT, its feed mill, to the Poultry Producers Association.

Unfortunately, most DDCs have very limited knowledge of privatization techniques, especially in the areas of valuation of assets and sales negotiations. The possibility exists that inexpert privatization efforts by the DDCs might result in: an illegal sale, a sale at an unfair price due to poor technical valuation of assets, a sale to a politically unacceptable buyer, or a business failure by the newly privatized enterprise due to poor management or inadequate capital. Any of these developments could set back the DDCs', and ultimately the GOB's privatization efforts.

One privatization effort which has already been completed is the conversion of seed processing plants. This USAID-sponsored effort has established an important model for public and private sector collaboration. Under this activity, more than 900 farmers have become seed producers and eight private seed processing plants have been installed nationwide with an average investment of $160,000 per plant. Originally, the production and processing of seeds was under the complete control and ownership of public entities (i.e., MACA and CODETAR). The privatization process began in 1985, with the GOB continuing the processing of seeds but with the private sector in control of production. The seed plants were initially administered by mixed (50 percent public, 50 percent private) enterprises, and in 1986, the plants were completely privatized.

Another significant GOB effort towards privatization and increased efficiency of state enterprises was the decentralization of the State Mining Company, (COMIBOL), a company which the GOB classifies as strategic. In the process, the GOB has closed a number of inefficient mines, laid-off nearly 15,000 employees and has established a precedent for additional privatization actions of several of its mines. The decentralization of politically sensitive COMIBOL has been a successful test of the Government's resolve to reduce its role in productive activities.

D. The Bolivian Private Sector

Despite the significant role of Bolivia's public sector in productive activities, the private sector is the most important source of employment and national income. Currently, private entities contribute an estimated 75 to 80 percent of the country's Gross National Product of $3.7 billion and employ approximately 78 percent of the labor force.

The Bolivian private sector is dominated by family-owned enterprises which control many of the larger firms and have interlocking interests in banking, commercial, mining, industrial, and agricultural concerns. The rest of the private sector consists of a multitude of independent small businessmen engaged in farming, animal husbandry, mining, manufacturing, artisanry, trade, and services.

As in the case of the public sector, the private sector is affected by structural and historical factors which affect its efficiency and ability to realize its potential. Probably the most detrimental factors have been political instability and erratic government policies, which, coupled with the public sector's heavy involvement in key productive enterprises, have inhibited the growth of private sector enterprises and led to a heavy private sector dependence on the GOB for subsidies and protection. This situation is changing as a result of the Paz Estenssoro Government's emphasis on market forces to promote Bolivia's economic recovery and growth, but it will take some time for the private sector to adapt to this new situation. Currently, the private sector is seriously affected by the recession resulting from the GOB's attempts to control inflation. For economic reactivation to take place, the private sector needs access to credit for working capital at rational interest rates, real incentives for investment (not protectionism), a general restoration of confidence in the economy and its continued stability, and a reaffirmation of public trust in the private sector to further the development/growth objectives of the country.

III. THE PROBLEM

The success of the INTRA Project will depend on a continuing strong GOB commitment to privatization, the timing of Project implementation and the availability of the necessary human, technical and financial resources. Given Bolivia's history of statism and the political sensitivities of a large number of Bolivians concerning the desirability of public versus private enterprises, it will also require a well thought out public education campaign to help the public understand and accept the Project. The time is now propitious to carry out privatization activities in Bolivia because the GOB: has been successful in stabilizing the economy, has relatively broad public and congressional support, and is at the middle of its term and can focus somewhat more on project development rather than political matters. However, for the government to maintain its momentum, it is important that economic reactivation begin soon. The INTRA Project could play a key supportive role to economic recovery by stimulating private productive investment and reducing the fiscal deficit of the state.

The Project will address four interrelated problems which limit the transfer of SOEs to the private sector. These problems are as follows:

A. Policy

The GOB's current overall economic policy, which relies on market forces, is a positive foundation for the privatization of the SOEs, but the GOB's specific privatization objectives and the strategy to achieve them are unclear. Currently, there is no explicit GOB plan to privatize SOEs, although Supreme Decree 21060 provides a very general framework for privatization with its reference to the possibility of transferring to cooperatives the SOEs held by the DDCs. Also lacking are the specific procedures for privatization actions, which would include considerations such as valuation of SOEs to be privatized, transfer and financing mechanisms. Morever, the GOB has not yet issued industry-specific policy measures to help ensure that there are no impediments to the success of the divestiture process.

B. Political

Statism is a deeply entrenched philosophy which has been created by years of state intervention in productive activities. The NEP is attempting to change this orientation, but it is a slow process. The GOB's decentralization effort is not a privatization strategy (only a first step), nor has it been presented to the public as such in part due to sensitivities regarding the sale of the "national patrimony" and a historical distrust of the private sector in certain Bolivian circles. Even in the case of the CBF enterprises which have been transferred to the DDCs, the only mechanism envisioned for their "privatization" is their conversion into cooperatives. The GOB seems to be very aware of the potential political costs of undertaking a major privatization effort -- particularly given the labor problems associated with the dissolution of COMIBOL. The labor movement is still strong, and, although currently less influential with the COB, both labor and management of the SOEs can be expected to resist the loss of privileges that privatization would bring.

In general, the sheer size of the SOE problem, the potential for corruption in divestiture, the socio-economic and political environment, and the lack of human resources and time to devote to the task, all inhibit the government from making an explicit, forceful public commitment to privatization.

The public in general does not appear to perceive the need for a major privatization effort. The public is largerly unaware of the problems of the SOEs, including the drain on the state's resources, and consequently of the reasons for a GOB privatization strategy. Once the public is better able to understand the benefits of this Project, it is important that they feel it is being implemented fairly. Given the public's current lack of understanding regarding the benefits of privatization, it can be expected that there will be resistance from groups and individuals with a vested interest in continued state operation of SOEs.

C. Structural

The Bolivian private sector today is characterized by a large number of weak, small, disadvantaged firms and a small number of wealthy groups which control virtually all of Bolivia's larger enterprises. The concentration of wealth in a few large groups poses a serious problem in that it may be difficult to find suitable buyers for the larger SOEs. This problem will be much less serious for the smaller agroindustrial or industrial SOEs. Efforts to identify potential buyers for the smaller SOEs will include not only investors, but also employees and producer groups. Transfer of SOEs to employees or producer groups may require that the Project assist once with working capital and the provision of technical assistance to run the SOEs. This would be done as a follow-on activity to the actual transfer of ownership.

Currently, both the central government and the DDCs are poorly prepared to implement a concentrated privatization effort. Government offices do not have the quality of technical personnel needed for this type of politically sensitive task, nor do they have the administrative flexibility required to implement it. A small highly competent office of qualified personnel must be created to carry out this Project. This office will work under the policy guidance of senior GOB officials to ensure that various Project elements are implemented and to secure the firm political support which will be needed for the initial privatizations.

D. Financial

As discussed below, there is insufficient capital and a lack of capital markets to finance the sale of SOEs. During the Siles Administration, the private sector was badly damaged, both psychologically and financially. The banking system was also critically affected and now faces serious difficulties. Since credit from the financial sector will continue to be tight in the short to medium term, financing for working capital and technical assistance for the privatization effort will be required from external sources.

1. The Banking System

The Bolivian banking system today is fragmented, decapitalized and inefficient. The system's failure to perform adequately its intermediation function constitutes one of the most serious obstacles to the Government's current economic reactivation program and the divestiture of SOEs.

Fourteen private Bolivian banks, associated with major private sector economic groups, emerged in the 1960s and 1970s. These banks, together with five branches or affiliates of foreign banks, four "special function" private sector credit institutions, and four public sector financial institutions, in addition to the Bolivian Central Bank, make up the Bolivian financial system. There is also a savings and loan system with 13 member associations.

In the early 1980s, hyperinflation sharply reduced economic activity and the de-dollarization of dollar denominated deposits and loans seriously affected the viability of Bolivia's financial institutions. The system contracted as depositors and banks shifted resources into real assets and/or dollars. Deposits shrank from $725 million in December 1981 to $68 million in June 1985. Commercial bank loans fell from $452 million in 1981 to $165 million in December 1985. Although financial institutions survived, they became inefficient and unprofitable, and encountered a serious liquidity problem. Two foreign banks closed their branches in Bolivia, while others have scaled down their operations.

Some recovery has been accrued in 1986, but the condition of the financial system is still precarious. Most banks are undercapitalized, their deposit base is fragile and many of their loans and other assets are worthless. Various banks are reported to be capitalizing interest to avoid writing off bad loans. The entire system is in need of a thorough overhaul. Measures to help the banking system are being developed by the GOB, with primary assistance from USAID, the Interamerican Development Bank (IDB), and the World Bank.

2. Capital Markets

There is no functioning stock market in Bolivia at present. In 1978, members of the Bolivian Confederation of Private Businessmen agreed to subscribe to publicly offered shares. A year later, the Bolivian National Securities Commission (NSC) was created by the Government with functions similar to those of the U. S. Securities and Exchange Commission. Although the Bolsa Boliviana de Valores was organized in 1980, the Government has yet to authorize it to begin operations. A modest over-the-counter market, which had developed for the securities of a very limited number of banks and industrial corporations, was almost totally destroyed by hyperinflation.

Presently, there is renewed private sector interest in developing a Bolivian stock market. The NSC may begin to function as a legal entity in 1987 and a capital market may eventually emerge. Unfortunately, this is not likely to occur in time to serve as a source of capital to finance the privatization of SOEs. Also, local currency refinancing facilities are either inadequate or not available for financing the types of activities envisioned under the Project. Therefore, there is a need for outside financing of divestitures and other privatization options.

IV. PROJECT STRATEGY

A. USAID/Bolivia's Private Sector Strategy

During the Presidency of Hernán Siles Zuazo, the hostile political/economic environment required USAID/Bolivia to concentrate much of its private sector support efforts through the Central Bank and Intermediate Credit Institutions (ICIs). USAID resources during this period were used to improve the functioning of the rediscount credit lines in the Central Bank, and to develop the basis for expanded support and the provision of agricultural and agroindustrial credits to the private sector.

During the last twenty-one months, USAID/Bolivia has broadened its private sector activities to include other projects (Management Training Institute, Handicraft Export Development, Private Agricultural Organizations, Market Town Capital Formation, etc.) which provide assistance to Bolivia more directly through the private sector. USAID's private sector strategy during this period has been to support the GOB's economic stabilization and recovery programs and to increase further the GOB's commitment to market mechanisms for setting price and wage levels and for allocating resources.

In February 1987, USAID evaluated its private sector activities and formulated a revised private sector strategy to address the key constraints to Bolivia's economic development: state control of the economy, structurally weak and inefficient financial markets, investment promotion, small business development, and export diversification. As a result, two projects -- Strengthening Financial Markets and Industrial Transition -- have been developed to address the first two problems mentioned above, and projects in the other three areas are expected to be designed and implemented in FY 1988 and FY 1989. (In February 1987, the Mission contracted ISTI to carry out an extensive private sector assessment. This study is now available through LAC/PS).

B. USAID/Bolivia's Privatization Project Strategy

The essence of USAID/Bolivia's privatization strategy is to support the GOB in its efforts to carry out its free enterprise policies. This will be done primarily by assisting the GOB in developing a feasible action plan for implementing a privatization strategy which will address the four problems discussed in Part III of this Paper. The plan will be one which can be implemented in the context of Bolivia's social and political environment. The heart of this plan is the development of a model or models of a privatization process and the actual transfer of several state enterprises to the private sector. This model(s) will be used for replication of privatization actions throughout Bolivia. This privatization approach, if successful, will lead to increased participation by the Bolivian private sector in the country's economy and a corresponding reduction in the role of the state in the country's productive enterprises.

While strongly supporting the GOB privatization efforts, USAID will maintain a low profile, in recognition of the political sensitivity and nationalism surrounding privatization/divestiture decisions. Existing resources within the Mission's project portfolio -- including the Market Town Capital Formation Project, PL 480, and ESF funds -- will be used, where appropriate, to support the INTRA Project. Moreover, the thrust of the INTRA Project -- particularly its focus on the agribusiness sector, the provision of working capital, and the attempt at policy reform -- will complement USAID/Bolivia emphasis on strengthening the role of the private sector in the economy.

Assisting the GOB in designing and implementing a privatization/divestiture program will not be easily accomplished. While the GOB is committed to such a course, and isolated privatization activities are already occurring, the obstacles to success are formidable. As explained above, a number of important constraints to the execution of a privatization/divesture strategy exist, including: public perception that most SOEs are "strategic," the absence of clearly-defined legal mechanisms for the valuation and sale of SOEs, exaggerated expectations on the part of the GOB and the DDCs on the returns to be gained by the sale of SOEs, a domestic private sector lacking in entrepreneurial spirit and capacity, serious weaknesses in the Bolivian financial system, a strong labor union movement, and the narrow time frame for effective government action in this area. The INTRA Project is designed to begin immediately to divest SOEs in the agribusiness and light industry sectors, mostly at the DDC level, while simultaneously supporting privatization initiatives which arise for SOEs regarded as strategic.

The Project will assist the GOB achieve economic reactivation through the reduction of fiscal deficits attributable to SOEs, the promotion of private investment, and a more rational and productive allocation of resources. The main elements of the Project strategy are:

1. To improve the policy environment to attract domestic and foreign investment critical to the success of economic reactivation and continued support for democracy.

2. To support the creation of an Industrial Transition Commission (INTRAC) to design and implement a GOB privatization program, to coordinate and provide technical assistance to the privatization activities of the DDCs, and to foster a public opinion climate favorable to free enterprise.

3. To begin the divestiture process (both transfers and closures/liquidations) with important, but non-strategic, SOEs to demonstrate the benefits and feasibility of privatization, including increased efficiency, lower costs, and the "democratization of capital."

4. To support privatization initiatives among the strategic SOEs.

The Project will provide: (1) assistance to the INTRAC, including support for technical consulting services, in the areas of management, valuation of assets, sales negotiations, legal aspects of transfers, and public relations; (2) credit financing for working capital needs of privatized enterprises; and (3) limited initial management consulting services for newly privatized enterprises which need financial, organizational, or marketing expertise to succeed. No provision is made for financing investments by private investors in privatized SOEs. Twenty-three state enterprises have been selected as potential priority privatization/closure candidates. These twenty-three may be divided as follows: 5 enterprises involved in light industry, 10 SOEs in the agribusiness sector, 4 state enterprises which should be closed/liquidated, and 4 strategic SOEs susceptible to privatization actions other than divestiture. The total estimated value of the fixed assets of those enterprises to be divested/liquidated exceeds $100 million (See Table I page 48).

INTRAC's main goal is to carry out privatizations/divestitures and to provide assistance to assure the survival of privatized firms. It will exist only for as long as it is needed to achieve privatization objectives. The actual life of the INTRAC will depend on how long it takes to achieve momentum. Its performance and future need will be evaluated after four years.

C. Project Benefits

The Project will have both macro and micro economic benefits of importance to Bolivia's population. The main benefits include:

-- The GOB deficit will be reduced by removing the SOEs from government control and responsibility. A direct effect of the Project will be a reduction in the number of people working for the government and increased efficiency in the operation of the transferred SOEs. This will reduce the financial drain of SOEs on the public budget, while also increasing revenue collections from the private sector. The reduction in the number of people employed by the public sector will be more than offset by increases in private sector employment as the privatized enterprises expand their production to the limits of their installed capacity, and as ex-SOE workers seek employment in other areas of the private sector.

-- Since the Project will promote the use of free enterprise mechanisms, it is expected that the overall level of efficiency in the utilization of Bolivia's productive resources will increase. The improved allocation of productive resources is expected to result in improved social benefits to the country's population.

-- Since the privatized SOEs will be operating under the same conditions as other private enterprises (e.g., they will no longer be subsidized), it is expected that Bolivian enterprises will become more competitive, both in the domestic and the international markets.

-- There will be an increase in the amount of private sector investments in former SOEs, which will stimulate economic growth. The private sector contribution to GDP will increase and, as such, will contribute to the reactivation of the economy.

-- To the extent that certain agro-industries are sold to producer groups, as planned by some of the DDCs (such as CORDECRUZ), there will be a democratization of ownership in the private sector, thereby reducing the traditional concentration of wealth.

-- The potential for economic growth caused by divestitures will attract foreign capital investments (ideally in the form of joint ventures with Bolivian investors) and, with it, the transfer of technology.

-- The demonstration effect from the successful transfers of public enterprises is expected to promote a change in the ingrained statist orientation, thereby increasing confidence/trust in the private sector.

D. Relationship to USAID/Bolivia Program Objectives and Other Projects

USAID/Bolivia's development program is focused on three objectives: (1) private sector led economic stabilization and growth, (2) sustaining and strengthening democratic government, and (3) narcotics control. This Project will support the attainment of the first two of these objectives. It will facilitate attainment of the economic recovery and growth targets of the GOB's NEP, reduce the contribution of inefficient SOEs to the fiscal deficit, and assist the private sector to be more efficient.

The proposed Project is fully consistent with A.I.D.'s privatization policy statement (State 189806) which directs A.I.D. Missions to assist with the divestiture of SOEs and help reduce the state's role in productive enterprises.

The USAID/Bolivia project portfolio is heavily private sector oriented. Almost all projects involve private sector participation. Some of the existing projects and programs in which the private sector is most heavily involved are: the Market Town Capital Formation (MTCF) Project, the Agricultural Producers Associations (APA) Project, the PL-480 Program, the Agribusiness and Artisanry Project, the Management Training Project, the Agro-Industrial Reactivation Component of the

Disaster Recovery Project, the Handicraft Export Development Project, the Chapare Project, the Emergency Agricultural Credit Project, and the Self-Financing Health Care Project.

USAID/Bolivia possesses the experience in dealing with the private sector necessary to undertake this Project. Now that the GOB has made its political commitment to privatization clear, USAID is able to assist the GOB with its privatization plans, which represent a major step forward in strengthening Bolivia's private sector. This Project is complementary to, and will expand, private sector activities which are being carried out under the terminating Departmental Development Corporations and the new MTCF Projects to promote private sector investment throughout the country. It will also complement work currently being carried out under the Private Agricultural Producers Association Project, the Policy Reform Project, and the Title III Program.

F. Other Donor Objectives

Bolivia's other international donors have objectives similar to A.I.D.'s and are also increasing their assistance programs particularly directed at strenghtening the private sector and promoting economic recovery. The proposed Project provides assistance to facilitate the GOB privatization and economic reactivation process which will complement the IMF stabilization program and related other donor programs, such as the World Bank's new Financial Sector Loan and the Interamerican Development Bank's new Agricultural Credit Loan which are designed to strengthen financial sector institutions and increase the flow of credit to the private sector as a means of increasing the pace of economic recovery.

V. PROJECT DESCRIPTION

A. Goal and Purpose

The goal of the Project is to promote Bolivia's economic recovery and growth through a more rational and efficient allocation of resources.

The purpose of the Project is to increase the role of the Bolivian private sector in the country's economy through its enhanced participation and investment in productive industrial and selected service enterprises.

Accomplishment of the Project purpose will be measured by the following End of Project Status (EOPS) indicators, as assessed by an evaluation to be conducted by the Project Assistance Completion Date:

1. Reduction of the SOE contribution to the public sector deficit. Baseline information will be developed as part of the feasibility studies to be carried out for each SOE to be privatized. Benchmarks will then be defined and evaluated by the Project Assistance Completion Date.

2. Reduction in the average operating costs of privatized SOEs. Benchmarks for this EOP will be established as part of the feasibility study of each firms to be privatized.

3. At least 10 SOEs privatized, and perhaps as many as 30.

4. At least 5 additional privatization actions (management contracts, leases of SOEs, closures, etc.) implemented in central

government enterprises not subject to sale.

5. Increased private sector investments in former SOEs will total at least $30 million.

Attaining these EOPS assumes that:

1. The GOB will provide a consistent and continuing commitment to the privatization effort, as expressed through the establishment of INTRAC and the enactment of the necessary legal means to carry out privatization initiatives.

2. The GOB will continue its existing free market-oriented economic policies, as defined by the NEP.

3. Political stability will continue and the private sector, both foreign and local, will be interested in, and willing to, invest and take risks in divested enterprises.

4. The privatization process will have sufficient and strong public support to offset negative reactions by groups with vested interests.

5. Sufficient financial resources from domestic sources and from international donors/financial institutions will be available to facilitate the transfer of SOEs.

6. Qualified individuals with enough influence, prestige and support at the highest levels of the GOB will be available to form the INTRAC and implement the privatization program.

B. Outputs and Inputs

1. Outputs

To attain the Project purpose, the following outputs will be achieved:

a. The INTRAC established.

b. A GOB privatization action plan developed.

c. The legal framework for the privatization of SOEs will be clarified and used as the basis for privatizations.

d. At least 5 privatization plans developed for DDCs.

e. Financing mechanisms for the transfer of SOEs established.

f. At least 10 divestiture feasibility studies conducted.

g. At least 10 investment packages for SOEs to be privatized developed for presentation to private investors.

h. An Investment promotion campaign carried out.

i. At least 10 SOEs privatized.

j. At least 5 additional privatization actions undertaken in the form of management contracts, leases, and closures.

2. Inputs

a. A.I.D.

It is planned to provide $10 million in A.I.D. grant funds [3/] during the LOP to finance: a) the operation of the INTRAC, b) foreign and local technical assistance (detailed job descriptions for the technical assistance team are provided in Annex H), c) a supplementary credit fund for selected financing of initial working capital needs of divested SOEs, and d) other costs (e.g. promotion costs, audits/valuations of SOEs, surveys/feasibility studies, and an A.I.D. project coordinator). A breakdown of the A.I.D. inputs is provided in Table III.

b. COB

The COB will contribute at least $7.5 million to the Project. If available, local currency generated under Economic Support Fund (ESF) arrangements will be used to finance a share of INTRAC's operating costs, local T.A., publicity campaigns, and worker indemnifications. Also, COB-owned local currencies generated under the PL-480 Title III Program will complement loan financing to ex-SOEs for new investments and working capital (see Section VII for a discussion of tentative financing arrangements).

3/ A late FY 1986 Agency decision, which considered Bolivia's extremely low level of development and per capita income (under $400 in 1986), approved future USG assistance to Bolivia on a grant basis.

C. Project Components

The Project will have three components: 1) the Establishment of an Industrial Transition Commission, 2) Privatization Actions, and 3) the Development of Financing Mechanisms.

1. Establishment of the Industrial Transition Commission (INTRAC)

Given the absence of an existing body within the GOB to implement a privatization program, and the pressing need to provide coherence to the privatization activities of the DDCs and the GOB, a high level commission (INTRAC) will be established at the outset of the Project. INTRAC will have a board of directors or advisory board composed of key ministers and private sector leaders, and a small staff headed by an Executive Director. INTRAC's structure will be action-oriented and flexible, emphasizing speed, efficiency, and the ability to gain access to various sources of internal and external technical assistance and financial resources.

Although INTRAC will be part of the administrative structure of the GOB, its operational staff will not include government employees. INTRAC'S staff will consist of highly qualified individuals with private sector experience. The funding for staff salaries will be provided from Project resources. The use of Project funds will allow the INTRAC to pay salaries at levels higher than Bolivian government standards, permitting it to function professionally and objectively.

INTRAC is expected to operate for four years, after which its performance and the future need for its services will be evaluated; a decision will then be made on whether to continue its activities using non-project funds.

Technical assistance in the following areas will be required to establish INTRAC:

-- Preparation of definitive structure and operating procedures and manuals.
-- Recruitment and training of staff.
-- Design of information gathering systems and the building of a data base on SOEs.
-- Design and evaluation of basic legislation.
-- Design of initial strategy and action programs.
-- Preparation of a public education strategy/campaign, as discussed under Section 1.D. below.

a. Scope and Functions of INTRAC

INTRAC's overall responsibility will be to plan, coordinate and oversee the privatization process in Bolivia. It is intended to serve as a resource center for privatization activities, especially in providing technical assistance for valuation of assets and for negotiating sales, and as a clearing house for recommendations on final privatization actions. The issuance of legal decrees and the final decision to divest a state-owned enterprise will remain the responsibility of either the GOB and/or DDCs. INTRAC will also take the lead in creating a climate of public opinion conducive to, and supportive of, privatization.

More specifically, INTRAC's main functions will be to:

1) Develop and implement a comprehensive GOB privatization program in coordination with the DDCs.

2) Provide policy and legal recommendations on privatizations, as needed by the GOB.

3) Work with the DDCs to target SOEs for privatization, prepare detailed privatization plans for each SOE, and recommend

privatization strategies and sales procedures for specific SOEs.

4) Carry out basic industry studies and valuations of SOEs in conjunction with the GOB and DDCs.

5) Develop financing mechanisms to facilitate the transfer of SOEs.

6) Design and implement marketing and promotion plans for the privatization of specific SOEs, including preparation of the prospectus, identification of buyers, etc.

7) Assist the GOB and DDCs on specific sales negotiations.

8) Plan and implement public information campaigns to create a constituency supportive of privatization.

9) Enlist technical and financial support from other international donors to further the GOB privatization efforts.

10) Prepare and maintain an updated inventory of Bolivian SOEs.

b. Institutional framework of INTRAC

INTRAC will operate under the policy guidance of the Ministry of Planning, as indicated in Chart I. The reasons for this are because the Ministry of Planning has:

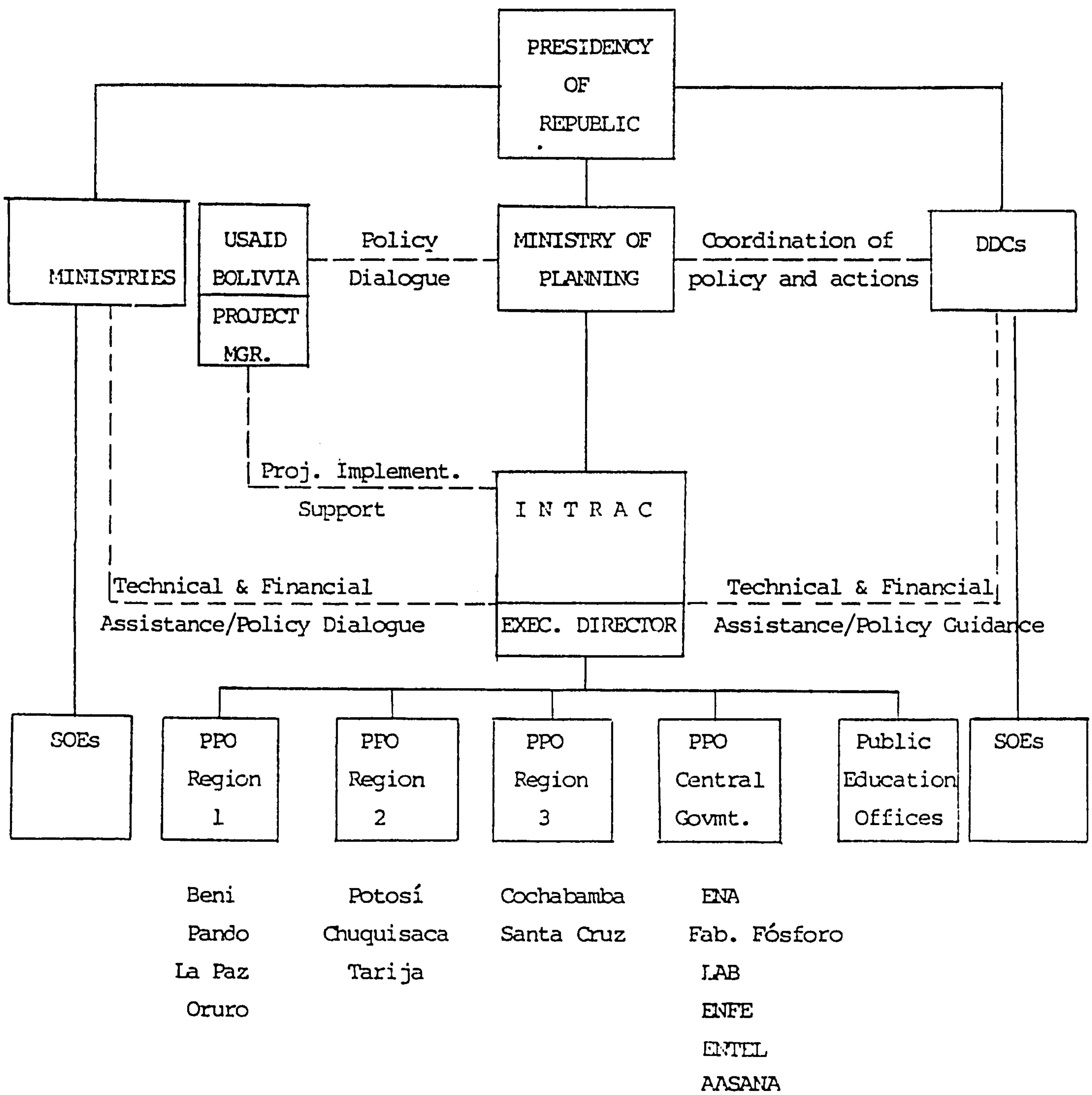
1) The leadership in GOB economic policy formulation.
2) An in-house technical capacity that can be used to support INTRAC.
3) A direct functional relationship with the DDCs.

INTRAC will have direct working relationships with the DDCs and Ministries of the Central government. The Executive Director of the INTRAC will establish liaison directly with influential private sector leaders, and the staff will have contact with producer associations, cooperatives, and potential individual investors.

CHART I

INTRAC

INSTITUTIONAL SETTING



A USAID Project Manager, assisted by a PSC Project monitor, will have general responsibility for managing the Project.

c. Composition of INTRAC

INTRAC's structure should be simple, efficient, and adapted to the organizational structure of the SOEs, the GOB, and the DDCs.

1) Board of Directors or Advisory Board

A board comprised of seven permanent members is planned. The permanent members of the Board will be the Executive Director of INTRAC, three government representatives and three private sector representatives. The three government representatives will be: 1) the Minister of Planning; 2) the Minister of Finance; and 3) the Minister of Industry, Commerce and Tourism. The three private sector representatives will be the President of the Confederation of Bolivian Private Entrepreneurs, and two representatives from regional private sector organizations, including the Chamber of Industries. In addition to the seven permanent members, the Board will include two DDC representatives who will serve for one year and then be replaced by representatives from other DDCs. Initially, it is proposed that the DDC representatives be from the Departments of Santa Cruz and Tarija, given the large number of SOEs operating there and the interest of these DDCs in divesting them. Board decisions would be taken on the basis of a majority vote.

2) Operational Structure

INTRAC will be organized to operate at both the national and regional levels, taking into account the Project's focus on the state enterprises of the DDCs. The Executive Director and Deputy Director will be responsible for the overall management of INTRAC, liaison with government ministries, and coordination of technical assistance for valuation and sales activities. In addition to the Executive Director and Deputy Director, the INTRAC will have four privatization promotion officers who will work at the central government level and also directly with the DDCs to coordinate privatization initiatives.

The alternative of organizing INTRAC on sectoral lines was considered, but the large number of state enterprises in agribusiness and light industry made this impractical. In addition, developing personal relationships and follow-up capacity at the DDC level will be important to the success of the Project. It will be the responsibility of INTRAC's Deputy Director to coordinate technical assistance to similar enterprises (e.g. feed mills, PILs) located in different regions, to avoid overlap.

INTRAC will also have a public relations specialist, an administrative assistant, a part-time legal advisor, three secretaries, and two messengers.

3) Key Operational Staff

The total number of direct staff required would be eight professionals plus six support personnel. In addition, a legal advisor would be retained on a part-time basis.

i) Executive Director

The Executive Director will be responsible for the overall management of INTRAC as well as for design, coordination and implementation of the privatization strategy and action plans. It is recommended that the person selected for this position should come from the private sector, preferably with formal training and experience in management and finance. In addition, this person must be highly respected by the GOB, the DDCs, politicians, and the private sector. He must be committed to the idea of privatization, able to explain and defend the program, and be capable of understanding and dealing effectively with high-level government and private sector leaders and international donors.

ii) Deputy Director

The Deputy Director will be responsible for day-to-day operating aspects of INTRAC, supervising and coordinating the activities of the Privatization Promotion Officers, and external consultants, and controlling the execution of all privatization activities. This person should have a good administrative background, with formal training in business or finance, experience in dealing with government agencies, and the ability to analyze and deal with the multiple issues that arise in the privatization process.

iii) Coordinators or Privatization Promotion Officers (PPOs)

The PPOs will be the direct liaison between INTRAC, the DDCs and other SOEs. They will be responsible for developing privatization policies and activities with the DDCs and central government enterprises, assisting them in targeting enterprises for divestiture, organizing and supervising the technical assistance teams and, in general, assisting and overseeing all privatization actions within their assigned areas.

These individuals should have specialized degrees in business, finance or engineering, and 5 to 8 years experience in responsible positions in private business or banking. They must be committed to, and have a clear understanding of, privatization and the main issues surrounding it. They should also have interpersonal skills necessary to deal effectively with officials in the DDCs and central government. A training program will be organized to better equip these persons to carry out their assigned responsibilities.

Initially, there will be four coordinators or PPOs. Their assignments will be as follows:

No. 1 Beni, Pando, La Paz, and Oruro DDCs.
No. 2 Potosi, Chuquisaca and Tarija DDCs.
No. 3 Cochabamba and Santa Cruz DDCs.
No. 4 All Central Government held SOEs.

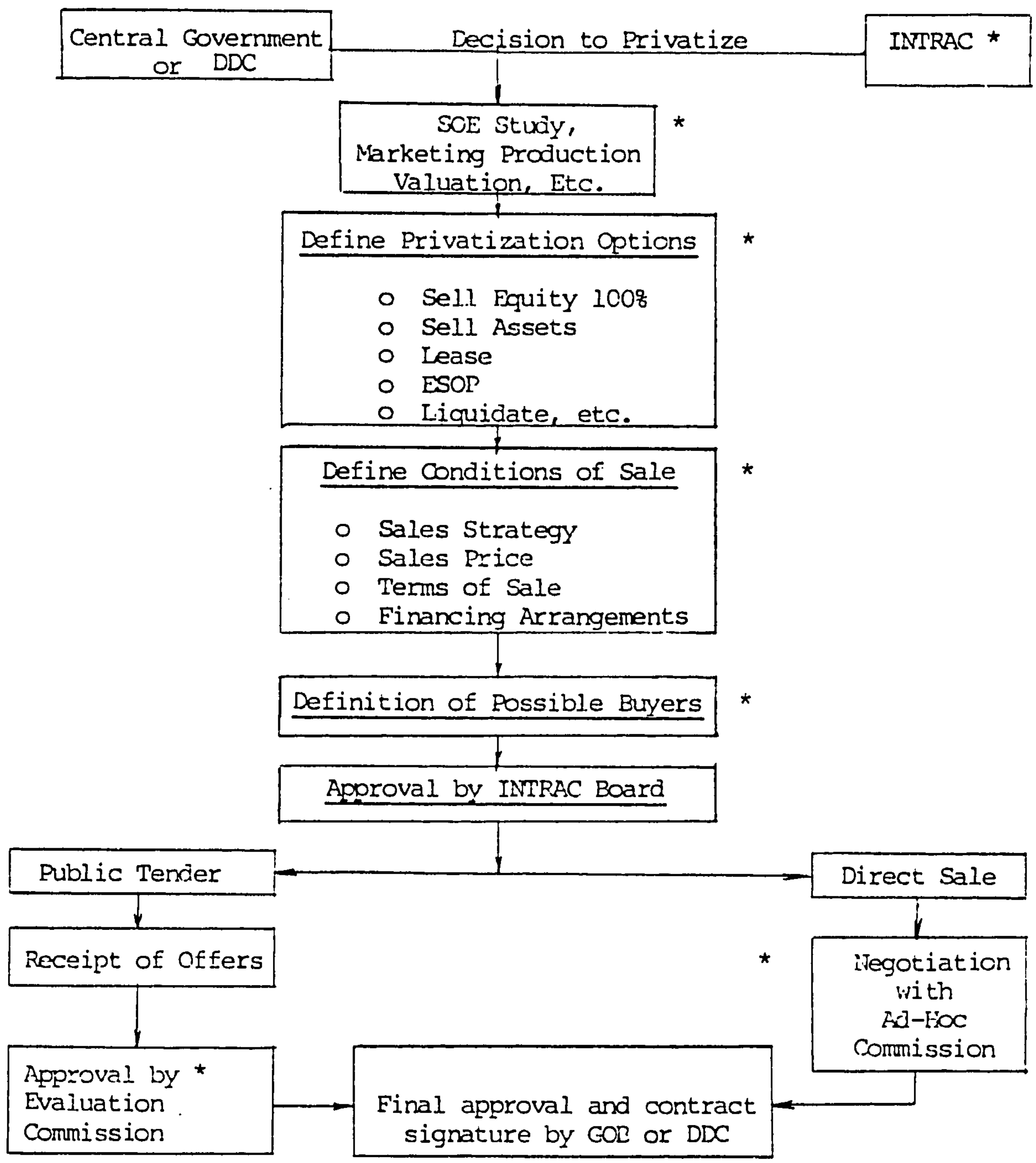
Each of the above six professionals will be required to sign a binding legal contract which prohibits them from working for any divested SOE for at least two years following their completion of employment with INTRAC.

The establishment of INTRAC is the keystone of the entire effort. For this reason, initial Project efforts will focus on establishing INTRAC and making it operational in order to take advantage of the present atmosphere for privatization. The GOB is in a unique position at this time to generate the necessary political support. The government is strong and has good support in Congress; President Paz Estenssoro has firmly established credentials as an effective leader; and the initial successes of the NEP have given the government high credibility.

Chart 2 presents a diagram of the steps required by INTRAC, the GOB, and the DDCs in the privatization process. It is envisioned that most of INTRAC's time and resources would be devoted to actual divestitures, with a secondary emphasis on liquidations/closures and other privatization actions aimed at the strategic SOEs.

CHART 2

PRIVATIZATION FLOW CHART



* Indicates areas where INTRAC and external consultants will participate with the GOB or DDCs.

d. Public Opinion Programs

A vital INTRAC activity which will receive special emphasis at the outset of Project implementation is the mobilization of public support for privatization. Privatization is essentially a political process, one which will probably generate opposition from entrenched interest groups which benefit from state control of the economy (i.e., labor unions, privileged bureaucrats, contractors, etc.). Design of a public education program, which is sensitive to difficult political issues for the government (e.g., prices, employment, nationalism) and which explains clearly to the public and key groups the benefits of privatization, will be essential to the success of INTRAC and the privatization strategy.

INTRAC's Director of Public Relations, assisted by a senior external specialist in public affairs and media contacts (i.e. print, radio and television) will develop a strategic plan to elicit public support for privatization. A key first step will be an assessment of the existing political environment, including a survey of public opinion on the respective images of the government, the private sector, state-owned enterprises, bureaucrats, and labor unions. In addition, information will be sought on public attitudes toward statism versus private enterprise to identify potential sources of support/opposition to privatization and to provide an information base from which to address critical issues.

Following the initial survey and data collection effort, a public education campaign will be developed for target audiences. This campaign will proceed at various levels (e.g., general public opinion, elite opinion, key opposition groups, key support groups) and will use an array of communications media (television, radio, seminars, pamphlets, press releases). The message delivered will have to be clear and straightforward. It should point out the benefits to be derived from privatization, the costs to the public of continuing to support inefficient SOEs with their privileged bureaucrats and employees, and the advantages to society at large of broadening the ownership base of productive assets and "democratizing" capital.

2. Privatization Actions

a. The Target SOEs

The focus of the INTRA Project will be on SOEs engaged in productive activities in the agribusiness and light industry sectors, and on supporting privatization initiatives for selected strategic SOEs of the central government. This strategic thrust of INTRAC is consistent with GOB strategy and existing political realities, takes advantage of ongoing divestiture activities at the DDC level; recognizes the need for INTRAC to achieve early successes to pave the way for future privatization efforts, and, over time, removes the state from direct participation in agroindustry -- the productive sector most important to the country's future economic development.

The environment for privatization in Bolivia mandates rapid implementation of the INTRA Project. As previously analyzed, the major reasons for the strategic focus on SOEs involved in agribusiness and light industry and selected strategic SOEs of the central government are:

** A long established statist mentality on the part of the general public, created by many years of government paternalism.

** A continuing public view that most state enterprises are "strategic," a term which applies not only to enterprises engaged in activities perceived important to national security and economic development (mining, communications, transportation, services) but also to any state enterprise a governmental official does not want to divest for political or economic reasons.

** The complexity, large financing requirements, and prolonged legal and valuation processes that would be involved in divesting the large SOEs of the central government.

** The limited political space available to President Paz' administration given that elections will occur in 1989.

Thus, the option of focussing privatization efforts on a few large SOEs was considered but rejected on political and economic grounds. Moreover, it was felt that an attempt by USAID or any other international organization to assist in the divestiture of the large, strategic SOEs would jeopardize more feasible privatization efforts at both the DDC and central government level.

It is extremely important that INTRAC be established soon (by July 1987) and that it be able to demonstrate to the public in its first year of operation a track record of successful privatizations. Success must be defined not only in terms of the sale/closure of SOEs, but also by securing <u>relatively</u> non-controversial terms and conditions (e.g., valuation of assets), successful management of the privatized entities, and geographic diversity of privatized enterprises. Moreover, INTRAC should carry out an array of privatization actions, involving creative financing and sales mechanisms. INTRAC needs to achieve quickly the reputation as a key resource assisting the central and regional governments in carrying out privatization efforts in the public interest.

Several selection criteria have been used to choose specific priority privatization candidates from among Bolivia's 107 SOEs over the next two years. First, the economic importance of the enterprise, both in terms of the value of its fixed assets and its existing or potential drain on government resources. Second, the level of GOB or DDC interest in actually divesting/liquidating/or initiating other privatization actions. Third, the availability of interested and politically acceptable buyers of the SOEs which considered foreign investors, local entrepreneurs, joint ventures, cooperatives, and producer associations. Fourth, the relative ease with which a highly professional, technical valuation of an enterprise's assets could be conducted. Fifth, alternative financing sources and mechanisms. Sixth, the need to undertake privatization at both the national and regional level, and to carry out actual projects in different DDCs. Finally, the potential working capital and management assistance needed to operate the privatized enterprises profitably.

The methodology for the prefeasibility study included interviews with GOB and DDC officials and with the directors of the SOEs. More than thirty on-site plant visits were made to different SOEs by the Project design team. As a result of these visits, the design team collected information on twenty-three SOEs which were selected as good candidates for privatization in 1987-91 based on the above criteria and on an examination of financial data and conversations with interested parties. Information on these twenty-three firms is presented in Table I. Additional information was obtained for the first two companies listed in Table I, because it was felt that they would make interesting case studies. These two are FANVIPLAN (glass production) and the Fábrica de Fósforos (manufacture of matches), both located in La Paz. FANVIPLAN is owned by CORDEPAZ while the Fábrica de Fósforos is owned by the Ministry of Industry, Commerce, and Tourism in partnership with local investors.

Several conclusions can be drawn from Table I. First, the five SOEs active in light manufacturing are all good candidates for immediate sale to the private sector. These five (FANVIPLAN, Fábrica de Fósforos, INMETAL, FABOCE (cement), and Hilanderia Santa Cruz (yarn)) are excellent candidates because they are located in three different DDCs; they could be easily evaluated technically; and there is already substantial interest in their privatization on the part of both buyers and sellers. Moreover, they should be relatively less complicated to privatize, because several options exist for their divestiture, including: foreign investment, outright purchase, joint ventures, and debt/equity swaps.

The second group of five SOEs involved in agribusiness are also good candidates for immediate divestiture. Four of these are owned by DDCs which are eager to transfer them to the private sector. These four are ALBAPOR (animal feed), PEC (cheese), and PAM (corn meal feed) in Santa Cruz, and ALBAT (animal feed) in Tarija. The fifth is ENA -- the National Rice Company -- which the GOB would like to dismantle. All five of these SOEs would probably be divested to politically acceptable producer associations. However, the relatively weaker financial position of the producers would probably require leveraged buy-outs rather than direct purchases.

The five diaries --Plantas Industrializadoras de Leche (PILs)-- are also candidates for transfer to the private agribusiness sector. However, their sales --even to cooperatives or producers associations-- would be a complex and potentially difficult process (see annex C.1 on PILs). Among the more difficult issues are:

** Varying degrees of interest on the part of the CDLs in selling the PILS, ranging from high in Santa Cruz to low in La Paz.

** Wide discrepancies in their perceived value, making agreement on a sales price very difficult.

** Lack of capital on the part of producer associations.

** Perception on the part of many that PILs are strategic SOEs.

** Necessary reforms in government milk policies, regarding prices, imports, and contraband.

** High need for both working capital and management assistance following the transfer.

A fourth group of SOEs consists of candidates for closure or liquidation. This group includes a bottling plant (FVC) and an edible oils plant (FAC) both located in Tarija, the Ingenio Guabira sugar mill in Santa Cruz [4/], and the Planta de Pollos BB, a chick breeding operation in Chuquisaca. All of these SOEs are not economically viable for reasons of lack of raw materials, insufficient markets, high operating costs, and/or low prices for their products (See Annex G for discussion of these SOEs.). In spite of their problems, the decision to close or liquidate these plants will not be easy because of political considerations. Ingenio Guabira and FAC are expected to be particularly difficult, because Guabira is an important regional source of employment, and FAC is considered by many people to be a development pole and hence is of strategic importance.

Finally, four strategic, economically important SOEs of the central government have been identified as candidates for privatization actions other than divestiture. AASANA, the National Airport Authority, is a logical candidate for contracting part of its services (operation and maintenance of terminals, auxiliary airplane services, fueling) to private companies. AASANA management has indicated an interest in exploring this possibility. Lloyd Aereo Boliviano, which is a mixed enterprise with the GOB holding 99 percent of the shares, might be a candidate for increased private sector participation (51/49), particularly via debt/equity swaps. ENTEL, the national telecommunications Company, might be another candidate for service

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4/ Ingenio Bermejo in Tarija, by contrast, can probably continue to operate profitably due to the quality of cane, a more efficient operating plant, and better market.

BOLIVIAN STATE-OWNED ENTERPRISES; PRIORITY PRIVATIZATION CANDIDATES, 1987-91

TABLE I

SELECTION CRITERIA	Light Industry					Agribusiness				
	FANVIPLAN	FOSFOROS	INMETAL	FABOCE	HILANDERIA	ALBARUK	ALBAT	FEB	PAN	ENA
1. Economic Importance	Medium	Low	Low	Low	High	Low	Low	Low	Medium	High
2. GOB Interest in Privatizing	High	High	High	High	High	High	High	High	High	High
3. Availability/ Acceptability/ Diversity of Potential Buyer	J.V. Foreign Investa.	Currently Mixed; sell	Sale to local Investors	J. V. Foreign Investa. Entrpns.	JV Foreign Investors Producers	Consumers Assoc.	Consumers Assoc.	Prods.	Prods.	Prods.
4. Ease of Technical Valuation	High	High	Medium	High	High	High	High	High	High	High
5. Alternative Financing Mechanisms	Foreign Investa. Debt/ Equity swap; public offering	Purchase	Purchase		For. Invtrs. Debt/Equity Public Offering	Levgd. Buy-out	Levgd. Buyout	Levgd. Buy-out	Levgd. Buy-out	Levgd. Buy-out
6. Geography Diversity	La Paz	La Paz	La Paz	Cochabamba	Santa Cruz	Sta. Cruz	Tarija	Sta. Cruz	Sta. Cruz	Sta. Cruz
7. Need for working capital/management assistance for new enterprises	$125,000/ Loan	$120,000/ High	$200,000 High	$200,000 High	$3,000,000 Medium	$1,500,000 Medium	$1,500,000 Medium	$85,000 Medium	$1,500,000 Medium	$240,000 Low
RECOMMENDED PRIVATIZATION ACTION	SALE	SALE	SALE	SALE	SALE	SALE	SALE	SALE	SALE	SALE (SILOS)

SELECTION CRITERIA	Milk Industry	Closure/Liquidation				Strategic SOEs			
	5 PILS	FNC	INGENIO GUABIRA	FAC	PLANTA DE POLLOS GB	ENTEL	LAB	AASANA	ENFE
1. Economic Importance	High	Low	High	High	Low	High	High	Medium	High
2. GOB Interest in Privatizing	L/M/H	Medium	Medium	Low	Low	Low	Low	Low	Low
3. Availability/ Acceptability/ Diversity of Potential Buyer	Coops. Prdcrs.	None	-	-	-	Possible Mixed	Mixed 49/51	Service Contracts	-
4. Ease of Technical Valuation	Medium	High	Low	Medium	Medium	Low	Medium	Medium	Low
5. Alternative Financing Mechanisms	Levgd. Buy-out	N. A.	Auction	Auction	Auction	Shares	Shares	-	
6. Geography Diversity	Cochabamba La Paz Santa Cruz Sucre Tarija	Tarija	Sta. Cruz	Tarija	Chuquis.	GOB	GOB	GOB	GOB
7. Need for working capital/management assistance for new enterprises	$1,300,000 High	N. A.	N.A.	N.A.	N.A.	-			
RECOMMENDED PRIVATIZATION ACTION	STUDY; LEASE OR SALE	CLOSURE	CLOSURE	CLOSURE	CLOSURE	PREFEAS. STUDY	PREFEAS. STUDY	SERVICE CNTRCTS.	LEASE

contracts. The current Director of ENTEL has expressed interest in exploring the possibility of ENTEL becoming a mixed enterprise with the majority in private hands. It should be noted, however, that ENTEL currently contributes approximately $20 million annually to the national treasury and is encumbered by very strong labor unions. ENFE, the National Railroad Company, has been approached by private entrepreneurs in Santa Cruz about the possibility of operating a railroad company on the Santa Cruz to Corumba route, and paying a fee for use of the track. All of these, and other privatization options will be investigated by INTRAC.

A number of smaller SOEs owned by the DDCs might also be transferred to the private sector in the course of the INTRA Project. While these SOEs are not significant enough economically or sufficiently complex to merit priority attention from INTRAC, it could play a role in assisting transfers. This list of SOEs would include:

COMPANY	LOCATION	PRODUCTS
1. Programa Agrícola Oleagionosas y Maíz Gran Chaco (PAOM)	Tarija	vegetable oil
2. Criadero de Truchas Piusilla	Cochabamba	aquaculture
3. Industrias Agrícolas	Tarija	food crops
4. Planta de Silos Sachojere	Beni	rice silos
5. Laminadora de Coma, SAM	Beni	rubber plant
6. Planta Beneficiadora de Castaña	Beni	Brazil nuts
7. Planta Procesadora de Tarhui	Cochabamba	vegetable oil
8. Planta de Té - Chapare	Cochabamba	tea
9. Planta de Té	La Paz	tea
10. Planta Industrializadora de Ají	Chuquisaca	condiments
11. Planta Beneficiadora de Castaña	Pando	Brazil nuts
12. Fábrica de Cerámica Roja	Oruro	ceramics
13. Fábrica de Cerámica Roja	Santa Cruz	ceramics

14.	Fábrica de Cerámica Roja Camiri	Santa Cruz	ceramics
15.	Fábrica Nacional de Cemento (FANCESA)	Chuquisaca	cement
16.	Fábrica de Cemento	Tarija	cement
17.	Taller Artesanal de Cerámica	Chuquisaca	ceramics
18.	Fábrica de Objetos de Peltre	Oruro	pewter
19.	Fábrica de Cadenas	Oruro	industrial/machinery parts
20.	Industrias de Papel (PITASA)	Tarija	paper

The Project Design Team also considered a number of other industries which were not selected as being priority candidates for privatization at this time. Brief mention should be made of these industries, categorized by their area of economic activity. The first category includes the mining, metallurgy, and hydrocarbon sectors. These were rejected as priority privatization candidates because they are too large, complex and politically charged to be suitable candidates. Second are the four state banks (Banco Agricola, Banco de la Vivienda, Banco del Estado, and Banco Minero). INTRAC will not become involved with these banks, because they are being dealt with by the Central Bank with the assistance of the World Bank and USAID's Strengthening Financial Markets Project. Third, is the public utility and services sector. This sector was rejected as a priority privatization target because it is commonly regarded as strategic and, hence, would be politically difficult to work with. Fourth is the Military SOE, COFADENA (which owns and operates a vehicle assembly plant, a shoe factory, etc.), which was also rejected for political reasons. Fifth, and last, are the thirteen state enterprises involved in livestock breeding and research. These are essentially agricultural extension and development services, and cannot be privatized at this time.

D. The SOE Transfer Process

1. The Process

Once INTRAC, the GOB, and the DDC agree to initiate privatization of a particular SOE, INTRAC will make the necessary arrangements to assemble a team of qualified technicians to develop a "transfer package" to carry out the divestiture or other appropriate privatization option. The composition of the team will vary from SOE to SOE, but, in general, will consist of the following individuals (See Annex H for job descriptions):

(a) The Regional INTRAC Privatization Promotion Officer;
(b) An Asset Valuation Team consisting of a Marketing Expert, an Industry Specialist, and a Business Planner/Management Specialist;
(b) An Investment Financing Expert; and
(d) A Lawyer.

The cost of the technical assistance to INTRAC will be borne by the Project. Financial assistance for privatization will be limited to the provision of working capital loans. Such loans will be provided at real market rates prevailing at the time of the transaction. Reflows from such loans will be deposited in a special account, tentatively under the management of the PL-480 Secretariat and the accounting control of the Ministry of Finance's Project Coordination and Control Unit and used for similar purposes, if justified at the time the reflow is available. Otherwise, such reflows will be used for mutually agreed development purposes, consistent with USAID's development strategy in Bolivia. In special cases (mainly involving the transfer of SOEs to cooperatives, producer associations or similar groups), the Project may provide technical assistance as a grant to help the new owners to manage or run a newly privatized enterprises. This will only be done if the cost of paying for this assistance might jeopardize the financial feasibility of the new firm. These exceptions will be evaluated on a case by case basis.

Chart 3 details the decisionmaking process which would be followed by INTRAC, the GOB, and the DDCs. INTRAC would be most active in the areas of divestiture and liquidation/closure, but could also play a role in partial privatizations of strategic SOEs.

2. <u>The Valuation Issue</u>

Several factors will be taken into consideration to determine the real value of state-owned enterprises. Some state enterprises use obsolete technology and/or equipment and may never be fully competitive in a free market environment. Others are located too far from sources of supply and markets, and are, therefore, at a competitive disadvantage in relation to similar producers in better locations. Still others may be over-equipped or over-built and have production capacities vastly exceeding market requirements.

A basic assumption in the valuation process is that the GOB and DDCs will try to maximize the proceeds from the sale of their SOEs, for both economical and political reasons. They expect to recover, as a minimum, the full value of their revalued assets. Even when the GOB and the DDCs realize that the assets of some SOE's are overvalued, it is difficult for them to mark down the price, because they are exposed to political pressures which make it difficult to dispose of these publicly-owned assets at substantially less than book value.

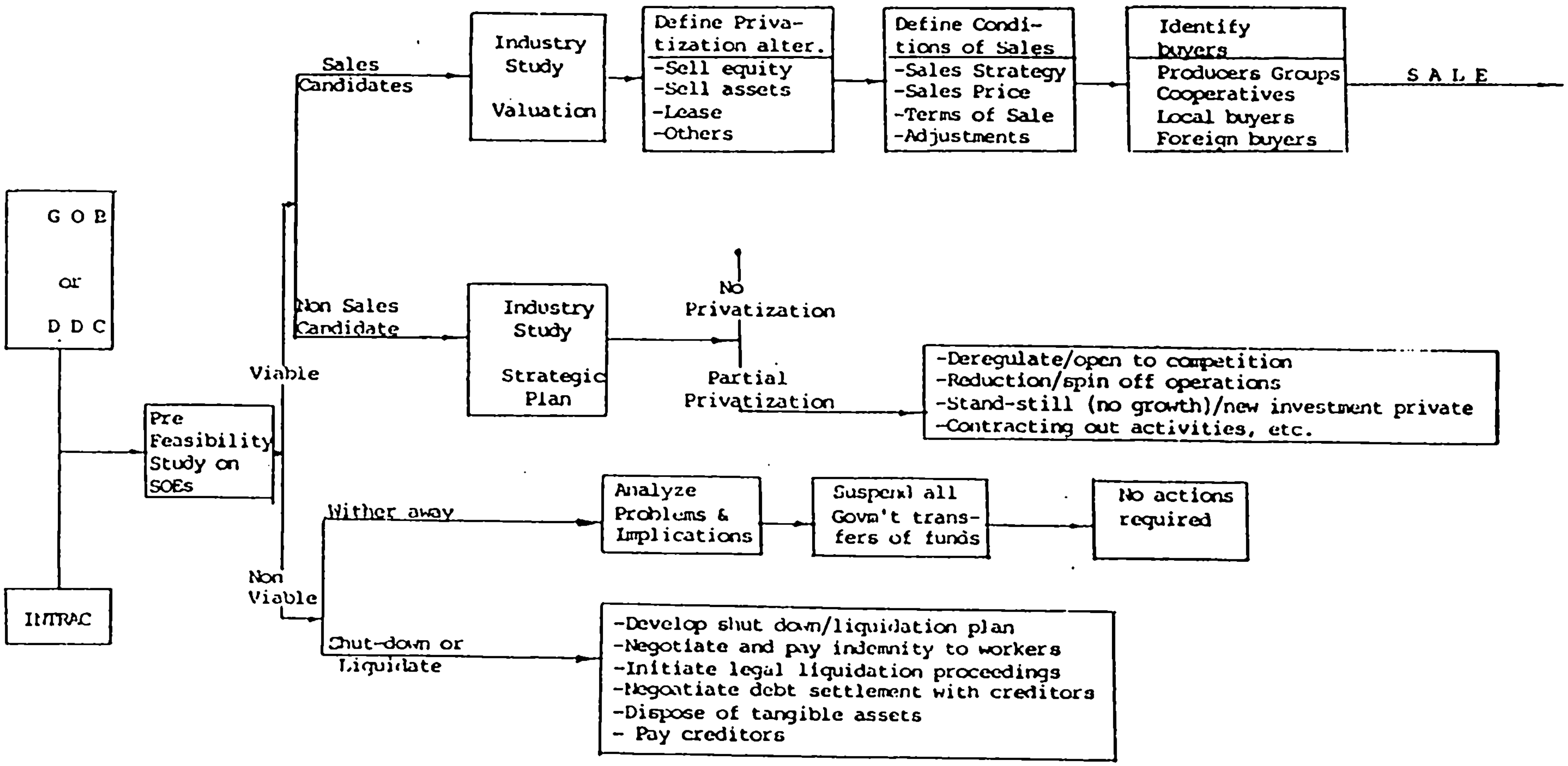
A second key issue is the social obligations owed to employees (severance pay and indemnification for years of service). These are definite liabilities which affect the net worth of the SOE. It is customary in Bolivia to liquidate, at the employee's option, this obligation every five years. Most employees opt for this "<u>quinquenio</u>" or settlement. Upon settlement, employees are usually furloughed and re-hired after two months. Employees who have not opted for the <u>quinquenio</u>, however, may accumulate sizeable sums of money owed to them

DECISION TREE

PRIVATIZATION

CHART 3

DECISION MAKING STEPS



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since the obligations are computed on the basis of their latest salary. The latter may be significantly higher in an inflationary environment (like Bolivia) than was their income in earlier years. Balance sheet reserves may or may not reflect fully this obligation.

Normally, upon the sale of a company in Bolivia, the seller dismisses all employees, discharging all social obligations, and the new owner re-hires those employees he wishes to keep. In such cases, the price paid for the company is not affected by social liabilities. In privatizing SOEs, it may be politically more expedient to dismiss only excess or undesirable personnel when the SOE is sold and continue employment for the majority of workers. In this case, the buyer would assume the social liabilities, the sum of which would have to be deducted from the sales price.

a. Valuation Methodology

Several pricing formulas have been proposed but the only one that is economically sound is one based on the "economic value" of the company. This value will be determined on the basis of a reasonable projection of anticipated earnings, based on the company's existing assets and expected production efficiencies achievable through appropriate management practices.

The "economic value" would be equal to the Net Present Value of the Future Cash Flow discounted at an appropriate rate over a given period of time. The discount rate and the length of the earnings stream should reflect the risks assumed by the investor in the present economic environment of Bolivia. A discount rate of 20 percent of the cash generated over a period of ten years could be appropriate parameters, but this will be determined by the valuation team. The resulting figure will be adjusted by any liabilities, such as social obligations, that the buyer may assume. This then becomes a realistic sales price, subject to negotiation.

A minimum sales price for a particular SOE may be set by the liquidation value of the assets if sold piece by piece in a public auction. Sales below this level could be justified only for reasons of job preservation, if that were deemed advisable for political reasons.

To the extent that a determination of the economic value of SOEs would be based on their earnings potential, it will be necessary to ascertain that potential. In this regard, the Project-financed valuation team will play a critical role in the analysis, evaluation and recommendation of tailored action plans for each SOE to be privatized.

b. Scope of Work for Valuation Teams

Depending on the SOE, tentatively it is planned to provide a three-person team of experts to conduct the valuation. The team members should include an industry specialist, a marketing expert, and an economic/management analyst or business planner. To assure objectivity, members of the team should be non-resident foreign nationals of recognized professional standing. The scope of the valuation would include:

i) Technical Analysis

The technical analysis will answer the following questions: to what extent does the technical process used in the plant is adequate and competitive in the context of the Bolivian environment; do production efficiency, product quality, and work force capabilities meet acceptable levels; what short term improvements are needed to solve bottlenecks, increase production efficiencies, and reduce costs; what are the capital costs of such improvements; what is the physical condition of the manufacturing equipment and machinery, i.e,. state of repair or maintenance, and are operating procedures or an operating plan adequate under existing conditions.

ii) Market Analysis

The market analysis will determine if the product is acceptable in domestic and export markets, the size of these markets and the degree of market penetration achieved to date. The analysis will identify the firm's competitors and their capabilities. It will assess the adequacy of the firm's distribution system, and pricing structure, as well as estimate the price elasticity of the products to be sold. The analysis will also study the possibilities for product diversification and product line extensions within the capabilities of the concerned enterprise. Finally, the analysis must determine sales and manpower requirements, and develop annual sales projections for three years.

iii) Economic Analysis

The economic analysis will include the following: production costs and administrative and selling expenses, cost reduction opportunities, a projected 3-year business plan with a balance sheet, profit and loss statement and cash flow projections, capital investment requirements to implement recommended improvements, working capital requirements, and administrative and accounting manpower requirements.

c. Pricing SOEs For Sale

Two SOEs involved in light manufacturing -- FANVIPLAN and Fábrica de Fósforos -- were analyzed to illustrate the proposed methodology for valuing SOEs and establishing their selling price. This analysis is summarized in Part VI of this Paper (Technical Analysis) and the complete case studies are included in Annex C. Three principal conclusions emerge from this analysis. First, the economic value of most SOEs will probably fall considerably below the book value of the revalued assets. This could pose a political problem for the government. Second, the COB or DDC can probably realize the highest sales price if it is flexible in negotiating a financial package (e.g. debt/equity swap leveraged buy-out). Third, private investors (domestic and foreign) are interested in purchasing SOEs, depending on the purchase price and other incentives which might be provided.

3. Financing Mechanisms

There are two types of financing mechanisms required for the successful implementation of the INTRA Project: funding the acquisition of SOEs and funding working capital requirements. Each will be discussed in turn.

a. Acquisitions

Flexibility and creativity will be necessary to finance the purchase of SOEs. This is the case because of weaknesses in the banking system, the lack of a functioning stock market, and the likely diversity of potential buyers. In spite of this, however, there seems to be enough risk capital available in and outside Bolivia for the purchase of SOEs targeted for near or medium term privatization using one or more of the financing options discussed below. What is needed is to find ways of mobilizing such capital through creation of an appropriate environment and adequate incentives. Thus, the INTRA Project makes no provision for an AID-financed facility to assist potential buyers in acquiring SOEs but assumes that political stability and the present private sector climate of optimism will continue during the life of the project.

Several alternative financing mechanisms were evaluated in the Bolivian political and economic environment. These include:

i) Straight Purchase

Outright sales financed with the investor's own capital would be the most desirable divestiture. It is unlikely, however, that a 100 percent cash payment is a realistic expectation. The

Central Government or the Departmental Development Corporations, whichever may hold a particular SOE, may have to provide some credit to the buyer. The magnitude, term and interest rate would have to be negotiated between buyer and seller and would largely be a function of the final sales price agreed to by both parties. As mentioned previously, the largest negotiable down payment would be demanded by the seller. SOEs engaged in light industry are good candidates for straight purchase by private investors, domestic and foreign.

ii) Debt/Equity Swaps

The debt/equity swap is one mechanism for easing the debt burden of Bolivia while simultaneously stimulating investment in productive sectors. Debt/equity swaps have been successfully implemented in other countries such as Chile, Mexico, Venezuela, and the Phillippines. However, the GOB has not yet promulgated rules approving and regulating this financial activity, although it has repeatedly expressed publicly its interest in exploring debt/equity swaps as a privatization/divestiture option.

Approximately one quarter of Bolivia's US$3.6 billion public sector foreign debt is owed to commercial banks. Currently, Bolivian debt is trading at approximately 15 - 20% of face value. If the GOB were to exchange its equity in SOEs for its own external debt instruments, i.e., swap debt for equity, the Bolivian economy and foreign creditors could both be "better off." One expects that a GOB debt/equity swap initiative would bring back some of Bolivia's flight capital, and result in additional foreign investment in the SOEs. Moreover, it would enable the Government to divest some SOEs at higher selling prices than would otherwise be achievable.

The debt/equity swap scheme may be particularly suitable for the transfer of SOEs such as FANVIPLAN, Hilanderia Santa Cruz, FABOCE, Lloyd Aereo Boliviano and others.

iii) Leveraged Buy-outs

Leveraged buy-outs would be appropriate for sales to producers' or users' associations. Examples are enterprises such as the PILs, ALBAPOR, PAM, PEQ, etc. After negotiating a sufficiently large (20 percent or more) initial down payment to assure the seriousness and risk exposure of the buyer, subsequent payments would be financed from earnings generated by the enterprise. This financing mechanism provides incentives for the seller as well as the buyer to assure the financial success of the company. The seller wishes to see the enterprise succeed in order to get paid, while the buyer needs a successful business to be able to pay off his debts. It also gives the seller a good reason for not inflating the sales price of his assets. Leveraged buy-outs with interest-free or low-interest loans on the balance may allow the Government to obtain a higher selling price for a SOE than its economic value may justify. This may be of importance should political considerations prevent the Government from accepting sales at prices below book value.

iv) Leases

Leasing the physical assets of SOEs to producer's or user's associations may be an alternative to leveraged buy-outs. This approach to privatization would circumvent the need to finance a sale and the political problems that might arise from selling a state-owned asset below its perceived worth. The GOB is currently negotiating the lease of ENA's Silos to the Cámara Agropecuaria del Oriente (CAO) in Santa Cruz, with an option to purchase.

Straight leases may have fees that are fixed and represent a fair return on the value of the leased assets. Alternatively, leases may be variable and related to the net profits of the privatized SOE. In some cases leases are both fixed and variable over different periods of time. Leases are also an interesting privatization option for "strategic" SOEs which cannot be sold for political reasons.

Lease-purchase agreements, commanding higher fees which include depreciation of the assets, may be used to transfer the leased property to the lessee for a token fee upon expiration of a long term lease. This privatization option is particularly useful in effecting the transfer of a firm to a group of employees or a cooperative.

v) Employee Stock Option Plans

Employee Stock Option Plans (ESOP) may not be practical in Bolivia because labor is generally unprepared to assume the responsibilities of ownership. Furthermore, should companies transferred through ESOPs fail, the Government would most likely be forced to take them over again. Nevertheless, employee participation through stock plans will be considered on a case-by-case basis.

In sum, the most appropriate way of financing the divestiture of a SOE will vary from case to case and will depend to a large extent on the potential buyer. While no single mechanism can be recommended, straight purchases might be most appropriate for relatively small enterprises in light industry, debt/equity swaps might be utilized in large manufacturing enterprises and strategic SOEs, and leverage buy-outs and leases might be most successful in the agribusiness SOEs which will be transferred to cooperatives and producer associations. One of the first priority tasks of the INTRAC will be to establish sales and valuation procedures and alternative financing mechanisms for the SOEs.

In any event, the final selling price and method of payment will be determined through negotiations between buyer and seller. Determinations of the value of assets, book value of equity, and economic value of the enterprise will all serve as guidelines to reach a fair selling price during negotiations. The key to achieving the best arrangement for both buyer and seller is to target each sale to the particular buyer who would most benefit from the acquisition.

b. Working Capital

While acquisitions should not be supported by an AID-funded financing facility, the contrary is true with regard to working capital for privatized SOEs. All SOEs, particularly those transferred from CBF to the Departmental Development Corporations, suffer from lack of working capital. In fact, most companies have such an acute liquidity problem that their continued operation is in jeopardy.

Given the serious weaknesses of the banking system, commercial loans which would satisfy the working capital needs of privatized SOEs are practically unavailable. Commercial banks do not grant loans geared to an enterprise's business cycle, have high collateral requirements, and charge high interest rates and spreads. In addition, most loans are currently limited to 30 days, paralleling the term of typical deposits. These revolving credit lines without guaranteed loan renewal do not provide a satisfactory means of financing working capital, which should be provided for terms paralleling an enterprise's business cycle. Finally, as discussed in Section D below and Part VI B (Credit Lines Analysis) of this Paper, existing A.I.D. related credit lines are insufficient to meet the working capital requirements to assure the viability of privatized SOEs.

Making working capital loans available to the new owners of former SOEs would act as a strong incentive for privatization. An A.I.D.-funded credit line for working capital loans would be managed by the PL-480 Executive Secretariat, which will also contribute local currency generated from PL-480 Programs and reflows from other COB/USAID projects. It is planned to leverage this credit line with matching funds from commercial banks. To be most effective, these loans should be in

Bolivian currency, with the exchange risk assumed by the GOB, tentatively through the Executive Secretariat. Additionally, the working capital loans would be for terms to coincide with the borrower's business cycle, and at adjustable rates of interest equal to the current commercial bank rates. The GOB assumption of the exchange risk and the specification of credit regulations for these loans would assure that borrower's costs not exceed commercial rates. These will be critical incentives for the successful implementation of the privatization strategy.

The A.I.D. Project funds for working capital loans, which will be provided through the PL-480 Executive Secretariat, will be channelled to private investors through Bolivia's banking system (the ICIs). The ICI channel will serve a dual purpose: to increase the liquidity of the ICI system and to broaden ICIs' range of operation for productive activities, in complement to the objectives of the companion USAID-sponsored Strengthening of Financial Markets Project. Reflows from working capital loans will be deposited in a special account and used for similar purposes. This scheme has worked very well with other projects and it is expected that it will also work for this Project. Its operation will be assessed during project implementation, and modified as necessary.

c. Estimate of Funding Requirements

The limited data available for projecting future cash flows of SOEs makes it difficult to estimate the working capital required for privatization of the targeted SOEs. To provide this estimate, the working capital requirements of sixteen SOEs were calculated (wherever possible) on the basis of the 1985 year-end balance sheets -- the latest statements available. The total cost of goods sold, administration, selling expenses, and financial expenses (at an annual rate of 20%) was divided by the estimated inventory turnover for each individual enterprise. The resulting figure in Bolivian currency was then converted into U. S. dollars at the average parallel market exchange rate for 1985 (to make calculations consistent with the 1985 financial statements of the 16 SOEs). The results are shown in the following table:

COMPANIES	ESTIMATED WORKING CAPITAL US$
Near Term Privatization Candidates	
Hilandería Santa Cruz	2,987,318
INMETAL	203,375
FABOCE	195,983
FANVIPLAN	163,962
Fábrica de Fósforos	118,816
ALBAPOR	1,500,000*
PAM	1,500,000*
PEQ	85,000*
PEA	85,000
ALBAT	1,500,000
ENA	241,732
TOTAL	8,581,186
Medium Term Privatization Candidates	
PIL Cochabamba	499,436
PIL La Paz	327,222
PIL Santa Cruz	394,295
PIL Sucre	43,468
PIL Tarija	41,572
TOTAL	1,305,993
TOTAL	9,887.179

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* Source: Privatization Program of Public Enterprises of CORDECRUZ, by W. A. Jorgensen and R. Marconi, December 22, 1986.

The total working capital funding requirements of approximately US$10,000,000 does not include the needs of some of the smaller SOEs, about which data could not be obtained but which in the aggregate may require another US$2,000,000 to $4,000,000 for working capital. Also omitted from this estimate were some other enterprises which, while not priority candidates, may eventually be privatized. These include: AASANA, Lloyd Aereo Boliviano, ENTEL, ENFE and various others.

The working capital financing line should also provide medium term loans for spare parts, machinery, equipment, or improvements to a firm's physical plant (when necessary). Normally, USAID financed working capital loans should not exceed one half of the privatized company's requirements. Approximately US$3,000,000 for this purpose would bring the total funding for this line to US$15,000,000 to $17,000,000. This amount would not all be needed immediately and the Project is currently budgeting only $12,037,000 for working capital loans which will be extended to selected privatized SOEs through Intermediate Credit Institutions at real interest rates for a period of up to 2 years. Additional funds may be provided by the PL-480 Title III Program if they are needed.

d. Sources of Financing

USAID/Bolivia reviewed the status of its ongoing project credit lines to determine the availability of funds to finance working capital loans under the INTRA Project. The status of each of the credit lines is detailed in Table II in the Summary of Technical Analyses. Based on a thorough analysis, two A.I.D. projects -- Market Town Capital Formation and Agricultural Producers Associations -- could provide at most $2.75 million in working capital credit. The actual amount available would probably be substantially less, given existing and potential demands on these lines and project restrictions on their uses.

Assuming a maximum of only $2 million available from ongoing projects, this would leave a financing gap of approximately $11 million. USAID/Bolivia proposes a working capital component of $5.5 million, to be matched by participating intermediate credit institutions.

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VI. SUMMARY PROJECT ANALYSES

Several technical analyses were carried out during intensive Project review. These included: (1) a preliminary cost/benefit analysis of the operations of selected SOEs; (2) an analysis of the status of USAID/Bolivia's existing credit lines to determine the availability of funds to finance the INTRA Project; (3) prefeasibility studies of selected agribusiness and light industry SOEs, including preparation of two illustrative case studies of valuation methods; and (4) an assessment of the legal/institutional framework surrounding privatization/divestiture. The most important conclusions of these studies are summarized below.

A. Economic Analysis

A complete quantitative economic analysis, including a benefit/cost or IRR calculation, cannot be undertaken for this Project at this time, for three reasons: first, because reliable 1985 or 1986 financial data are not available for most of the state-owned enterprises slated to be privatized; second, most of these enterprises have only recently been transferred to the DDCs by the CBF and final values have yet to be established; and third, in the case of some of the central government SOEs, the impact of privatization actions is difficult to determine at this point.

USAID/Bolivia has been able to obtain financial data as of 1985 for 28 SOEs presently held by the DDCs, some of which are prime targets for privatization, as expressed in the strategy section of this Paper. However, the economic impact of their privatization will only be determined when the feasibility studies are executed during the privatization process. In the case of most of the SOEs, it is impossible to say without additional analysis whether they are potentially viable or should be liquidated. Only some very tentative and preliminary judgments can be made on the basis of the data currently available.

Furthermore, since 1985 all the debts of the former CBF enterprises have been assumed by the GOB, which considerably changes their financial situation for the time being. Nevertheless, the same problems and inefficiencies continue under DDC administration, and few of the enterprises can turn an operating profit. New debts are being incurred with the DDCs.

Financial analyses carried out on a number of SOEs produced a series of highly negative results, such as a low sales to total assets ratio which is an indication of low capacity utilization, and high indexes of illiquidity expressed in negative working capital and high financial costs.

Total losses of the 15 money losing firms for which there are data amounted to Bs13.1 trillion in 1985, equal to US$29.0 million at the average official exchange rate prevailing in 1985, and US$18.3 million at the average parallel market rate. Note that these data relate to only 15 deficit firms. Since there are over 100 SOEs, it may be conservatively estimated that the combined deficits of all money-losing enterprises (excluding central government SOEs) is at least double that figure. An annual loss of Bs26 trillion would constitute 13.6% of the total 1985 deficit (equal to Bs192.7 trillion) of the consolidated non-financial public sector.

The avoidance of losses does not constitute the only potential benefit from the proposed Project. There are a number of SOEs that are either breaking even or realizing a small surplus. Thus, for the sample of 28 firms for which we have data, 13 or 46% fall into this category. Many of these firms have the potential of becoming considerably more profitable if transferred to the private sector, though there is no firm basis for estimating the order of magnitude of the increased returns.

The positive macro-economic impact expected to result from the proposed Project can be summarized as follows:

1. The elimination of losses can be expected to end or sharply reduce an important drain on the government's budget and/or on the the banking system that is called upon to extend credit to the losing firms. The impact will be even more dramatic on the budgets of the DDCs.

2. The Government will be able to obtain additional tax revenues from privatized firms earning higher profits through increased yields from the net worth tax (currently 2% annually) and the value added tax.

3. The Government would derive significant proceeds from the sale of assets to the private sector. The net worth of the 28 SOEs for which USAID has data amounts to about US$ 68 million. The total for all 108 SOEs must be significantly larger, even after correction is made for the overvaluation of the book value of fixed assets. The sales proceeds can be utilized for high-priority investment projects that only the government could implement--e.g. improvement of the road and communication systems. The successful sale of assets to the private sector would often necessitate the mark-down of the inflated historical or book value of the fixed assets, as initial costs were often substantially larger than could be justified by technical and economic considerations, including the size of the potential market.

4. The transfer of assets from the state to the private sector (combined with closure, when necessary) is expected to improve the allocation of resources within the country. Experience in other countries suggests that firms operated by the private sector under competitive conditions are likely to operate more efficiently than state-owned enterprises, particularly when the latter are granted a monopoly. Concerns operated on the profit motive are likely to avoid padded payrolls, make more effective utilization of their staffs and

equipment, provide incentives to their labor force to enhance productivity, and avoid wasteful expenses. Bolivia is no exception: for the sample of 28 firms for which USAID has data, administrative costs constitute as much as 22% of sales, while sales are only 16% of the net value of fixed assets. Even more importantly, the state is often induced to provide monopoly conditions and other benefits to its enterprises, thus removing the incentive for efficiency that competition provides.

5. Effect on employment: The net effect of the Project on employment is likely to be positive because the transfer of a number of money losing, but potentially viable, firms to the private sector is likely to avoid their eventual closure, which in many cases, cannot be postponed indefinitely. Moreover, the enhanced profitability of marginal firms could lead to the gradual expansion of their work force. As is usual in these cases the initial restructuring of newly privatized SOEs will result in a temporary drop in employment.

Once the privatization process of the smaller and regional SOEs gets under way, as indicated in the strategy statement, it is expected that the GOB will tackle privatization issues in the major central government managed enterprises with much larger impact on the economy and a greater potential for obtaining more benefits from privatization.

B. Technical/Financial Analysis

1. Credit Analysis

The Project design team analyzed the status of A.I.D.'s credit lines to determine the availability of funds to finance some of the activities of the INTRA Project.

There are certain ongoing A.I.D. projects that have credit components which could be used, within limitations, to assist privatized

SOEs by providing medium term loans for working capital needs such as spare parts, machinery, equipment, improvement to a firm's physical plant (plant modernization) or purchases of raw materials.

One such project is Market Town Capital Formation. The credit available consists of $14.5 million from DA funds and $6.5 million from PL-480, Title III. However, $5.75 million of these funds have already been reserved for specific projects. The funds available for assisting privatized SOEs will be limited as the existing demand for non-INTRA projects is extremely large. It is estimated that a minimum of approximately $1.5 million will be needed by each of the nine credit units (UCFs) - one in each department of the country. This would leave only an estimated $1.75 million which potentially could be tapped to finance limited privatization activities. However, funding available under the Market Town Project has been earmarked for secondary cities which could pose a problem because most of the state enterprises are located in the main cities of the country.

Under the Agricultural Producers' Associations Project, $5 million in credit is available from PL-480, Title III Program. The purpose of this credit is to improve services to members. Under INTRA some of this credit line could be used by associations that purchase agro-industries. Again funds are limited because these funds are for associations in all nine departments of Bolivia. It is estimated that a maximum of only $1 million could be available for privatization activities.

The other credit lines listed in Table II will not be available to finance Project activities because such lines have been already earmarked for specific activities under each of the projects. Potentially, some of the local currency generations under the PL-480, Title III Program could be made available to supplement funding to be provided for the INTRA Project. The financial plan already includes $2.5 million from the FY 1987 Title III Program and about $2.2 million from

Status of AID Credit Lines
at December 31, 1986
(US$)

TABLE II

Project Name and Number	A Total Amt. Obligated	B Total Amt. Earmarked	C Amount Obligated	D Amount Earmarked	E Amount Committed	F Amount Disbursed	G Avail. for Commitment (C-E)	H To be Disbursed (E-F)	Life of Project: Start Date	Life of Project: PACD	Beneficiaries and Activities Financed
			For Credit Elements								
Agribusiness and Artisanry, 511-0472	2,150,000	2,032,946	150,000	150,000	150,000	0	0	150,000	1/9/78	1/9/88	Funds not available for INTRA Project Larger private firms. Used for agribusiness and artisanry.
Agribusiness and Artisanry, 511-0472/T-060	6,200,000	6,007,580	6,000,000	6,000,000	6,000,000	6,000,000	0	0	1/9/78	1/9/88	Funds not available for INTRA Project
Agribusiness and Artisanry, 511-0472/T-060A	3,000,000	2,777,357	3,000,000	2,777,357	915,183	140,392					Funds not available for INTRA Project
Departmental Dev. Corporations, 511-0511/T-064	7,000,000	6,691,249	7,000,000	6,691,249	5,236,525	3,640,192	1,763,475	1,596,333	9/20/79	3/31/87	Small and medium agribusiness and artisanry enterprises throughout Used for working capital and investment. Project terminated 9/31/87
Departmental Dev. Corporations, 511-0511/T-065	3,000,000	2,769,104	2,848,499	2,693,378	2,693,378	1,356,125	155,121	1,337,253	9/20/79	3/31/87	Funds not available for INTRA. Project terminated 9/31/87
Chapare Regional Development, 511-0543/T-067	4,039,000	3,538,803	1,000,000	750,394	0	0	1,000,000	0	8/11/83	8/31/88	Small, medium, and large agroindustries. Used for hog fattening, fisheries, fruit processing, etc. Some credit for production cost substituting new crops for coca. Funds not available for INTRA Pro
Chapare Regional Development, 511-0543/T-067A	961,000	0	600,000	0	0	0	600,000	0	8/11/83	8/31/88	
Chapare Regional Development, 511-0543/T-067B	5,000,000	0	3,658,000	0	0	0	3,658,000	0	8/11/83	8/31/88	
Market Town Capital Formation, 511-0573/T-071	3,149,645	0	2,899,645	0	0	0	2,899,645	0	7/23/86	7/23/91	Enterprises in secondary cities of Bolivia. Used for agribusiness Possibility of limited amounts for privatizations. Project purpose and focus on secondary cities limits availability
Market Town Capital Formation, 511-0573/T-071A	3,153,800	0	2,903,800	0	0	0	2,903,800	0	7/23/86	7/23/91	
Industrial Transition 511-0577	10,000,000	0	5,300,000	0	0	0	0	0	1987	1990	Private sector investors, e.g., producer groups. To finance worki in former state-owned enterprises.
Disaster Recovery, 511-0581/F-69B (AIRU)	12,300,000	9,930,298	3,570,000	2,500,000	2,500,000	1,085,201	1,070,000	1,414,799	10/12/83	6/30/87	Small and medium agroindustries and their employees. Some reflows available, as reflected in INTRA budget.
Disaster Recovery, 511-0581/F-69C	7,500,000	7,500,000	7,500,000	7,500,000	7,500,000	7,500,000	0	0	10/12/83	6/30/87	
Disaster Recovery, 511-0581/T-070	3,871,000	2,211,000	1,660,000	1,660,000	0	0	1,660,000	0	10/12/83	6/30/87	

Disaster Recovery, 511-0581/T-070E	1,500,000	1,330,000	170,000	0	0	0	170,000	0	10/12/83	6/30/87	
Potable Water and Sanitation, 511-0582/W-058	2,000,000	350,000	2,000,000	350,000	233,656	233,499	0	0	9/30/83	9/30/88	Public and private institutions benefitting communities. Used for potable water and sanitation.
Emergency Agricultural Credit, 511-0591	2,424,828	2,424,828	2,424,828	2,424,828	2,400,000	1,950,000	24,828	450,000	9/30/86	3/30/88	Small farmers. Used for agricultural production.
Small Enterprise Development, 511-0596	10,000,000	0	7,800,000	0	0	0	0	0	1988	1993	Micro- and small enterprises. Used for financing working capital and investments.
LOCAL CURRENCY*											
PL480 Title I Refinancing Lines:											
Productive Credit Trust Funds	4,000,000		4,000,000		4,000,000	3,977,000	0	23,000			Small and medium farmers, artisans, agribusinesses that benefit small farmers and small-scale businesses. Used for agricultural production, projects that provide employment.
Credit for Housing and Family Related Needs	3,000,000		3,000,000		2,488,410	808,940	511,590	1,679,470			Low and medium income families. Used for consumer loans, home improvement and expansion, construction, and community infrastructure , i.e., electricity.
Chapare Regional Development Activities	1,000,000		900,000		617,000	152,000	283,000	465,000			Small, medium, and large agroindustries. Used for hog fattening, wood manufacturing, fisheries, fruit processing, etc. Some credit for production costs for farmers substituting new crops for coca.
Regional Rotating Development Funds	1,500,000		1,500,000		1,500,000	1,499,131		869			Small and medium agribusiness and artisanry enterprises throughout Bolivia. Used for working capital and investment.
PL480 Title III, 1978 Refinancing Lines:											
Wheat Collection Centers	4,757,000		872,000		0	0	872,000	0			For Wheat Collection Centers to have funds available to pay farmers as they bring their wheat.
Small Farmer Credit	17,000,000		17,000,000		13,969,000	11,700,000	3,031,000	2,269,000			Small farmers. Used for agricultural production, medium- and long-term small-farm investment.
PL480 Title III, 1986 Refinancing Lines:											
Agroindustrial Credit for Small and Medium Enterprises	4,500,000		4,500,000		260,000	0	4,240,000	260,000			Small and medium-sized agro-processing, agro-input manufacturing and artisanry enterprises. Used for equipment, construction of physical facilities, operating costs, training, or raw materials. The $260,000 committed to date is for credit to microenterprises through PRODEM for working capital and expansion.
Small Farmer Agricultural and Livestock Production and Marketing Credit	7,500,000		7,500,000		2,000,000	1,998,000	5,500,000	2,000			Small and medium-sized producers. Used for annual and perennial crops, machinery, productive productive farm infrastructure, small producer livestock improvement, marketing, and inventory needs.
National Wheat Production	2,200,000		7,000		0	0	7,000	0			For Wheat Collection Centers to have funds available to pay farmers as they bring their wheat.
Credit for Small and Medium-Sized Enterprises	2,500,000		2,500,000		0	0	2,500,000	0			Budget of INTEA Project includes up to $2.5 million from the FY 87 Title III Agreement.

*Local Currency funds do not have the stage of funding "Earmarked" reflows from the Agro-Industrial Reactivation Component of the Disaster Recovery Project. Other Project's financial requirements must come from private investors, the COB, the DDCs, and financial institutions, both Bolivian and foreign. The Project provides only limited resources for working capital to complement these other sources of financing.

2. Case Studies

Two companies, FABRICA NACIONAL DE FOSFOROS, S.A.M., and FANVIPLAN, have been selected as case studies to illustrate the proposed methodology for evaluating SOEs and establishing fair selling prices. Detailed descriptions of these cases are included in Annex G. Various "value" concepts were examined (revalued assets, book value, market value, economic value) to illustrate the need for a thorough feasibility study to determine fair market value. In the Bolivian context, the concept of economic value is recommended as the basis for sales negotiation. In preparing the illustrative case studies, several tentative conclusions emerged: the need for three-person valuation teams to conduct the feasibility studies; the likelihood of a substantial discrepancy between the book value and the economic value of SOEs; and the serious interest of private investors in purchasing the SOEs, depending on price.

FABRICA DE FOSFOROS is a "mixed company" with participation of the State through its Ministry of Industry, Commerce and Tourism, combined with private capital. It is the only producer of matches in Bolivia. The original share distribution, giving the State a 51 percent majority was modified in 1981 when the company, faced with complete illiquidity, received a cash contribution from the private shareholders which increased their equity interest to 52 percent. At that time, the private shareholders also received an option to acquire the remaining government-owned shares. This option has not been exercised to date because of the lack of a clearly defined legal mechanism for the transfer of shares and the inability of the parties to reach an agreement on the transfer price. The Government expectation is to recover its original investment plus non-compounded 8 percent annual interest for 23 years of participation in the company. The Government mentioned a price range of US$697,320 to $724,200 for its remaining shareholdings. This compares to an economic value determined by the proposed valuation methodology of US$50,940 and a liquidation value of the existing assets of US$236,766. Partial liquidation of the assets and relocation of the factory to a less expensive area closer to its sources of raw material might allow the private shareholders to pay as much as the liquidation value for the government shares, but this price would still be significantly below the Government's expectation. The valuation was based on arbitrary assumptions for purposes of illustrating the methodology.

FANVIPLAN is a company whose entire capital was owned by the Government through the Bolivian Development Corporation (CBF) and subsequently transferred by Supreme Decree 21060 to a Regional Development Corporation. The only flat glass company in Bolivia, FANVIPLAN was set up as a semi-autonomous enterprise with its own management but without an independent legal personality. The equipment, using an obsolete manufacturing process, is mostly of Polish origin. It supplies about 70% of the domestic market needs and exports some of its glass to Peru. The glass is of second and third rate quality. The oven has reached the end of its useful life and must be rebuilt at an estimated cost of US$1.2 million. The revalued net fixed assets leave a current book value of US$5,898,684 which may possibly be written down to US$4 million on the basis of a new appraisal. The Central Government's absorption of all liabilities except employee benefits left the company with an equity of US$7,005,624. The economic value of FANVIPLAN computed in accordance with the proposed valuation process (Net present value of 10 years of projected cash flows discounted at 20%) is US$2,705,460. A fair market value would be about one half of that amount since the new owner would have to invest another US$1.2 million to rebuild the oven. His total investment of about US$2,550,000 would be recovered (pay-back period) over 4 1/2 years. The liquidation value of FANVIPLAN was estimated at US$1,035,000. As in the case of FABRICA DE FOSFOROS, the valuation was based on arbitrary assumptions and, thus, serves for illustrative purposes only. The most likely investors would be Peruvian glass manufacturers who could use FANVIPLAN's production to service the South Peruvian market. A debt/equity swap would bring the highest price for FANVIPLAN.

C. Legal Analysis

A review of the legal and institutional framework surrounding privatization/divestiture was undertaken. The principal conclusion of this review is that, although the laws relating to valuation of assets and transfers of SOEs are complex, the GOB has existing legal authority to: establish INTRAC, clarify valuation and sales procedures, and to carry out privatization activities, as evidenced by its efforts with several seed plants, rice storage facilities, and COMIBOL.

The legal status of SOEs will need to be addressed by the INTRAC as it carries out the GOB's privatization plan, discussed under Part V of this Paper. First, it is unclear precisely which governmental authorities have the power to transfer state assets and enterprises. Second, valuation procedures contained in existing legislation are limited in scope, too specific, and unsuitable to the application of modern techniques. Third, sales are now limited to public auctions and fail to consider alternative ways to divest state assets in specific cases. Thus, it will be necessary for the government to take steps to clarify the legal framework for privatization/divestiture.

Prevailing opinion in the Bolivian legal community is that the President is empowered by the Constitution to approve the transfer of state enterprises, and, if necessary, to enact the appropriate enabling legislation, such as was done in the case of Decree 21060 and in the recent transfers of some state enterprises (e.g. COLOCE, ENA).

D. Social Analysis

The INTRA Project will have a positive impact on the social environment. Through the elimination of the fiscal losses of the SOEs and from the proceeds gained by the sale of assets to the private sector, the GOB and the DDCs will be able to devote greater resources to health, education, and infrastructure projects. The sale of SOEs to producer and consumer groups will lead to increased incomes and to a broadening of the ownership base of the country. The net employment effect of the Project is also likely to be positive, in terms of preserving jobs which would have been lost by the eventual closure of non-profitable SOEs and in terms of the expansion of the work force as marginal firms enhance their profitability.

Since the Project deals with the privatization of existing state enterprises, it is not possible to define precisely the role women will play in the transfer process and as Project beneficiaries. However, all SOEs employ women and it is expected that they will continue their employment after the privatizations take place. To the extent they have some investment capital to participate in acquisitions, they will benefit from the Project, particularly from the technical assistance to be provided to assure the continued successful operation of the privatized enterprises.

E. Environmental Considerations

The Project design team determine that the Project will not have an adverse effect on the environment because it only entails the transfer of state-enterprises to the private sector. The Project will not change the basic nature of these enterprises. Therefore, a categorical exclusion has been recommended and approved based on the provisions of Section 262.2(C) of 22 CRF part 216 on environmental procedures. (See Annex C).

VII. COST ESTIMATE AND FINANCIAL PLAN

A. Life-of-Project Cost Estimate

1. AID Grant Contribution

A total of $10.0 million will be provided by A.I.D. as shown in the Life of Project Cost Estimates and Financial Plan Chart, (Table III).

These funds are planned to be allocated as follows:

a. Industrial Transition Commission (INTRAC)

A.I.D. grant funds totalling $995,000 will be provided to finance: i) salaries and other direct costs ($945,000) for the INTRA staff (i.e. 7 long-term positions for 3.75 years each at $3,000 (avg)/mo), and ii) other operating costs such as office equipment and vehicles ($50,000).

b. Technical Assistance to INTRAC and SOEs

The technical assistance budget component includes AID grant financing totalling $2,579,000 for a U.S. institutional contract (188 person-months, pms). The selected U.S. firm will provide 45 pms of a long-term advisory assistance at an estimated cost of $720,000 ($16,000(avg)/pm x 45 pms), and 143 pms (see input section for breakdown) of short-term consultants at an estimated cost of $1,859,000 ($13,000 (avg)/pm x 143).

c. Financing Mechanisms

A total of $5,496,000 will be furnished to finance working capital for privatized SOEs from AID grant funds under this component.

d. Other Costs

AID grant funds totalling $505,000 will be provided to finance: a) one mid-course and one final evaluation ($60,000) and annual audits ($40,000), and b) an AID Project Coordinator for 45 pms ($9,000/mo x 45, $405,000).

e. Price/Quantity Contingencies

A 4.25% AID grant contingency ($425,000) is provided for in the Project.

2. Host Country Contribution

a. GOB Contribution

The equivalent of $7,500,000 in Bolivian pesos from local currency will be provided under FY 86 ESF ($300,000), the Agro-Industrial Reactivation Component (AIRC) of the Disaster Recovery Project ($2.2 million), and FY 87/88, PL-480, Title III Program ($5.0 million). The ESF funds will be used to finance: a) all INTRAC support staff (i.e. 5 1/2 positions for 3.75 years each at $730(avg)/mo), and b) a share of INTRAC's operating costs (i.e. rent at $1,500/mo x 45, $67,500; office furniture at $2,500/position x 12.5, $31,250; and office supplies at $5,000/yr x 4, $20,000). The AIRC funds will be applied to fund working capital for privatized SOEs ($2,200,000). The PL-480, Title III Program funds will fund: a) travel/perdiem for INTRAC staff (7 persons for 3.75 yrs each at 350/mo, $110,000), b) local consultants (i.e. 70 person/months at $3,000/pm, $210,000), c) public relations campaigns ($50,000), d) working capital ($1,841,000), e) indemnification payments approximately 1,350 employees to be laid off at $1,852, ($2,500,000), and f) contingencies ($289,000).

b. Local and Foreign Private Sector Contributions

The private sector investment is based on the assumption that the book value of the assets of target SOEs is approximately $100 million. However, the economic value of these assets is estimated at only $50 million. This is the price that investors would be willing to consider in a sale transaction with the DDCs. Of the $50 million, it is estimated that the private sector would be able to mobilize $37.5 million or 75 percent of the required investment. The balance of $12.5 million is expected to be raised from foreign investors.

In addition to these investments, the Bolivian ICIs are expected to finance up to $2.5 million as part of a matching funding arrangement for working capital of privatized SOEs.

Table III shows the LOP Cost estimate by source and by major funding categories. Table IV gives the projection of disbursements by project year and by financing source.

3. Method of Implementation and Financing (AID Funds)

	Major Elements	Method of Implementation	Method of Financing	Approximate Amount
I.	INTRAC			
	a. INTRAC Staff (Executives)	PSCs	Direct Pay	$ 225,000
	b. INTRAC Staff (rest)	HC. PSCs	Direct Pay	$ 720,000
	c. Other operating costs	HCCs	HC Reimb	$ 50,000
II.	Technical Assistance	Direct AID Institutional Contract	Direct Pay	$2,579,000
III.	Working Capital	Loan Refinancing	HC Reimb	$5,496,000
IV.	Other Costs			
	a. Audits/Eva.	Direct AID Contracts	Direct Pay	$ 100,000
	b. Project Coordinator	Direct PSC	Direct Pay	$ 405,000
			Sub-Total	$9,575,000
			Contingencies	$ 425,000
			TOTAL	$10,000,000

TABLE III

LIFE OF PROJECT SUMMARY COST ESTIMATES AND FINANCIAL PLAN

FINANCING SOURCES (IN US$ 000'S)

MAJOR FUNDING CATEGORIES	AID GRANT FX	AID GRANT L/C	GOB L/C	PRIVATE SECTOR L/C	FOREIGN CAPITAL FX	TOTAL FX	TOTAL L/C
A. Industrial Transition Commission (INTRAC)							
a) INTRAC Staff (7 positions for 4 yrs ea)	-	945 (1)	110 (2)	-	-	0	1,055
b) Support Staff (5 1/2 positions for 4 yrs ea)	-	-	181	-	-	0	181
c) Other Operating Costs (i.e. rent, equipment, furniture, supplies and vehicles)	50	-	119	-	-	50	119
B. Technical Assistance							
a) Long Term Advisor (42 person months, pms)	720	-	-	-	-	720	0
b) Short Term Consultants (143 pms) (3)	1,859	-	-	-	-	1,859	0
c) Local Consultants (i.e. lawyers/accountants for a total of 70 pms)	-	-	210	-	-	0	210
C. Financing Mechanisms							
a) Working Capital	-	5,496	4,041	2,500 (4)	-	0	12,037
b) Investment Capital	-	-	-	37,500	12,500	12,500	37,500
c) Indemnification Payments	-	-	2,500	-	-	0	2,500
D. Other Costs							
a) Public Relations Campaigns	-	-	50	-	-	0	50
b) Audits/evaluations (5)	60	40	-	-	-	60	40
c) AID Project Coordinator (U.S. PSC for 45 pms)	405	-	-	-	-	405	0
E. Price/Quantity Contingencies (6)	124	301	289	-	-	124	590
TOTALS:	3,218	6,782	7,500	40,000	12,500	15,718	54,282
	10,000					70,000	

(1) It includes only salaries, benefits and other costs for the INTRAC staff.
(2) It finances travel and per diem for the INTRAC staff.
(3) This total includes 40 pms for valuation, 20 pms for negotiation of sales/promotion, 24 pms for management consulting 20 pms for privatization options for major SOEs, 15 pms for INTRAC star-up, and 24 pms for public relations.
(4) ICI financing for working capital.
(5) Two outside evaluations (3 experts for 3 weeks ea) and 2 local audits.
(6) A 4% reserve to finance unforseen variations in prices/ quantities is included for the AID grant and GOB contributions.

PD&I:JV

TABLE IV

B. DISBURSEMENT SCHEDULE

PROJECTION OF EXPENDITURES BY PROJECT YEAR

(IN US$ 000'S)

FINANCING SOURCES/MAJOR FUNDING CATEGORIES	YEAR 1		YEAR 2		YEAR 3		YEAR 4		TOTAL	
I. AID GRANT	FX	LC	FX	LC	FX	LC	FX	LC	FX	LC
A. Industrial Transition Commission (INTRAC)										
a) INTRAC Staff	-	245	-	245	-	245	-	210	0	945
b) Support Staff	-	-	-	-	-	-	-	-	0	0
c) Other Operating Costs	50	-	-	-	-	-	-	-	50	0
B. Technical Assistance										
a) Long Term Advisor	350	-	150	-	150	-	70	-	720	0
b) Short Term Consultants	900	-	350	-	350	-	259	-	1,859	0
c) Local Consultants	-	-	-	-	-	-	-	-	0	0
C. Financing Mechanisms										
a) Working Capital	-	2,200	-	1,500	-	1,000	-	796	0	5,496
b) Investment Capital	-	-	-	-	-	-	-	-	0	0
c) Indemnification Payments	-	-	-	-	-	-	-	-	0	0
D. Other Costs										
a) Public Relations Campaigns	-	-	-	-	-	-	-	-	0	0
b) Audits/evaluations	-	-	30	20	-	-	30	20	60	40
c) AID Project Coordinator	150	-	100	-	100	-	55	-	405	0
E. Price/Quantity Contingencies	30	60	30	60	30	60	34	121	124	301
TOTAL AID CONTRIBUTION:	1,480	2,505	660	1,825	630	1,305	448	1,147	3,218	6,782
										10,000
II. HOST COUNTRY CONTRIBUTION										
A. GOB										
a) INTRAC staff	-	25	-	25	-	25	-	35	0	110
b) Support staff	-	50	-	50	-	50	-	31	0	181
c) Other Operating Costs	-	30	-	30	-	30	-	29	0	119
d) Local Consultants	-	50	-	50	-	50	-	60	0	210
e) Working capital	-	1,500	-	1,000	-	1,000	-	541	0	4,041
f) Indemnification Payments	-	1,000	-	500	-	500	-	500	0	2,500
g) Public Relations Campaigns	-	20	-	10	-	10	-	10	0	50
h) Price/Quantity Contingencies	-	70	-	70	-	70	-	79	0	289
B. PRIVATE SECTOR AND FOREIGN CAPITAL										
a) Working Capital	-	1,000	-	500	-	500	-	500	0	2,500
b) Investment Capital	5,000	15,000	2,500	7,500	2,500	7,500	2,500	7,500	12,500	37,500
TOTAL HOST COUNTRY CONTRIBUTION:	5,000	18,745	2,500	9,735	2,500	9,735	2,500	9,285	12,500	47,500
										60,000
GRAND TOTALS:	6,480	21,250	3,160	11,560	3,130	11,040	2,948	10,432	15,718	54,282
										70,000

VIII. IMPLEMENTATION PLAN

A. Responsibilities

1. USAID/Bolivia

USAID/Bolivia will contract a U.S. Project Coordinator for the LOP under a Personal Services Contract (PSC) arrangement using grant funds. This PSC will work under the direct supervision of a USAID/Bolivia Direct Hire Project Manager, and will provide a link between USAID/Bolivia, INTRAC, the DDCs and the private sector local and foreign investors which will participate in Project activities. In addition, the Project Coordinator will serve, on a daily basis, as liaison with INTRAC's Executive Director and other GOB/private sector organizations involved in privatization activities in Bolivia. Both the USAID Project Manager and the Project Coordinator will be assisted by a USAID Project Implementation Committee. This Committee will periodically review Project status to identify potential implementation and/or other problems and develop appropriate solutions as required.

The USAID direct hire Project Manager will have direct supervisory responsibility and authority for both Project Coordinator and Technical Assistance team performance. Also, the Project Manager will be the officially designated counterpart of the INTRAC Executive Director and other GOB/Private Sector representatives of the Project.

2. Technical Assistance Team

The technical assistance (TA) team, to be provided through a direct AID contract with a U.S. institution, will be a resource to INTRAC in the areas of financing and transfer procedures, valuation of assets, and overall implementation of the privatization process. Except for the long-term advisor, all other members of the TA team will be short-term (i.e. both local and international) experts to be provided on an as-needed basis to assist in privatizing selected SOEs and to help privatized SOEs during their initial stages of operation. The TA contractor will have the responsibility for arranging all logistical needs including its own office space, office furniture, office materials, housing for the LT advisor, and sub-contracts with local and international short-term consultants. Job descriptions for the technical assistance team are contained in Annex H.

3. GOB

The Project Agreement (ProAg) will be signed with the GOB Ministry of Planning and Coordination (MPC). The MPC will name an authorized representative for the Project, with the concurrence of USAID/Bolivia. This person will be the Executive Director of the INTRAC. As such, the INTRAC Director will be the link with the GOB on major privatization decisions. In addition, he will coordinate the day-to-day operations of the Project with USAID/Bolivia and the TA team.

4. DDCs

The DDCs will be vital participants in the actual transfer process of SOEs to the private sector. They will participate in the selection of the SOEs, valuation of assets, selection of an appropriate privatization method, analysis of legal aspects and finalizing the details of each transfer.

B. Schedule of Major Actions

The Implementation Schedule which follows in next page outlines events during the Life of the Project (4 years).

INDUSTRIAL TRANSITION PP

IMPLEMENTATION SCHEDULE

Item No.	ACTIONS	RESPONSIBLE INSTITUTIONS
	- Sign Project Approval	USAID/Director
	- Sign Project Agreement	USAID/MPC
	- PIO/T for Project Coordinator approved & Position Advertised	USAID/Project Mgr.
	- Project Coordinator selected and on-board	USAID/Project Com.
	- Form INTRAC Board of Directors	USAID/GOB
	- Issue Supreme Decree	GOB
	- PIO/T for INTRAC Exec.& Deputy Directors approved & positions advertised simulta.	USAID/Proj. Mgr./ MPC
	- INTRAC Executives Selected and on-board	
	- Recruit rest of INTRAC profess.& support Staff (HCCs)	USAID/INTRAC Executives
	- PIO/T for TA RFP approved	USAID/Proj. Mgr.
	- TA RFP issued	RCO/Lima
	- TA RFP advertised	RCO/Lima
	- TA contractor Selection made	USAID/INTRAC
	- TA contract negotiated and signed	RCO/Lima
	- TA contractor mobilized	Proj.Coor./Contract
	- Prepare detailed job description & operating manuals	INTRAC Deputy Director/TA
	- Prepare Data Base/Info.Systems on SOEs	TA experts
	- Design Sales and Valuation procedures	TA experts
	- Draft & issue legal documents on sales & valuation	Lawyers/GOB
	- Prepare privatization procedures & financ. manuals	TA experts
	- Develop privatization & implementation strategies	INTRAC Exe.Director TA experts
	- Develop priority list of privatization candidates	INTRAC Exe.Director TA Experts

YEAR 1 MONTHS 1 2 3 4 5 6 7 8 9 10 11 12 — YEAR 2 MONTHS 1 2 3 4 5 6 7 8 9 10 11 12 — YEAR 3 MONTHS 1 2 3 4 5 6 7 8 9 10 11 12 — YEAR 4 MONTHS 1 2 3 4 5 6 7 8 9 10 11 12

INDUSTRIAL TRANSITION PP

IMPLEMENTATION SCHEDULE

Item No.	ACTIONS	RESPONSIBLE INSTITUTIONS	YEAR 1 MONTHS 1 2 3 4 5 6 7 8 9 10 11 12	YEAR 2 MONTHS 1 2 3 4 5 6 7 8 9 10 11 12	YEAR 3 MONTHS 1 2 3 4 5 6 7 8 9 10 11 12	YEAR 4 MONTHS 1 2 3 4 5 6 7 8 9 10 11 12
	- Design Public Education Campaign	INTRAC Exe. Director TA Experts				
	- Initiate & execute public education campaign	INTRAC/PR.Officer				
	- Carry out privatization plans for each target SOEs	GOB/INTRAC/ DDCs				
	- Mid-course Project Evaluation	Contractor/USAID/ INTRAC/DDCs				
	- Final Project Evaluation	Contractor/USAID/ INTRAC/DDCs				
	- Project Audits	Contractor/USAID/ INTRAC/DDCs				

The Project's implementation plan envisions periodic readjustments in the project design and in the financial and TA resource allocations, should these be necessary to attain the Project purpose. The plan also lists other events which are essential for planning initial implementation activities and mobilizing technical assistance. Revisions to this plan would be based on the results of the mid-course evaluation scheduled at the end of the second year of Project operation, or earlier if deemed appropriate.

C. Procurement Plan

INTRAC, in concert with the technical assistance contractor, will coordinate and carry out procurement of the following:

- services of local hire support personnel (i.e. secretaries/messengers, etc.);
- office space and equipment; and
- short-term consultants (local).

The Project Personal Services Contract (U.S.PSC) Coordinator and INTRAC Executive personnel will be hired directly by USAID/Bolivia shortly after Project approval.

All procurement will be carried out on a competitive basis following A.I.D. FAR regulations and qualified 8(a) firms will be considered together with qualified firms with experience in carrying out the planned project activities. The source/origin for these procurements will be the U.S. and Bolivia.

D. Evaluation and Audits

1. Evaluations

The evaluation plan includes one mid-course and one final project evaluation. The first evaluation will assess progress towards accomplishment of the overall Project purpose and suggest mid-course refinements,as necessary. The final evaluation will measure the attainment of purpose indicators (EOPs) and other quantifiable objective parameters. Particularly, the evaluation will assess the effectiveness of the privatization process, the attainment of the specific privatization targets listed in Part V of this Paper, and the impact of the project in reducing the public sector deficit, in increasing private sector investment, and on employment.

2. Audits

The Project budget provides for one audit per every two years during the LOP.

IX. CONDITIONS PRECEDENT AND COVENANTS

The Project Agreement will be signed with the Minister of Planning and will include the following conditions precedent and covenants:

A. Conditions Precedent to First Disbursement of Assistance

Prior to the first disbursement of the Assistance or to the issuance by A.I.D. of documentation pursuant to which disbursements will be made, Bolivia will, except as A.I.D. may otherwise agree in writing, furnish to A.I.D., in form and substance satisfactory to A.I.D.:

1. an opinion of the Attorney General of Bolivia or other counsel acceptable to A.I.D. that the Agreement has been duly authorized and/or ratified by, and executed on behalf of, Bolivia and that it constitutes a valid and legally binding obligation of Bolivia in accordance with all of its terms;

2. a statement of the names of the persons holding or acting in the office of the Bolivian authorized representative specified in Section 9.2 of the Agreement, and a specimen signature of each person specified in such statement.

3. a written notification approving the creation of INTFAC with the names of the Board of Directors.

2. Convenants

Bolivia will convenant to take whatever legal steps are appropriate during Project implementation to effect the privatization of selected state-owned enterprises.

AMB DCM ECON Rec'd 1/14

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PP RUEHLP
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BT
UNCLAS STATE 011844

LOC: 014 348
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CN: 01398
CHRG: AID
DIST: AIDE

AIDAC

E.O. 12356: N/A
TAGS:
SUBJECT: BOLIVIA INDUSTRIAL TRANSITION PROJECT (511-0577) PID GUIDANCE

REF: STATE 189806

1. THE SUBJECT PID WAS REVIEWED BY THE DAEC ON DECEMBER 11, 1986. THE PID WAS APPROVED AND THE MISSION MAY PROCEED WITH DESIGN OF THE PROJECT PAPER SUBJECT TO THE FOLLOWING GUIDANCE.

2. MISSION PRIVATIZATION STRATEGY. REFTEL REQUESTED THAT MISSION SUBMIT PRIVATIZATION STRATEGIES BY JUNE 30, 1986. THIS STRATEGY HAS NOT YET BEEN RECEIVED FROM BOLIVIA. THEREFORE THE MISSION SHOULD ASSURE THAT THE PP CLEARLY SETS FORTH THE MISSION'S PRIVATIZATION STRATEGY. FURTHERMORE, THE SPECIFIC DETAILS REQUESTED IN PARAGRAPH 3.C. OF THE REFTEL MUST BE CABLED TO PPC ASAP. ALSO, WHILE WE CONCUR WITH THE MISSION'S PROPOSAL TO LIMIT PROJECT ACTIVITIES TO THE DIVESTITURE OF RELATIVELY SMALL, NON-STRATEGIC ENTERPRISES, IT IS IMPORTANT THAT: (A) CLOSURE OF UNECONOMIC ENTERPRISES AS WELL AS SALE OF PROFITABLE FIRMS BE CONSIDERED AS AN OPTION AND (B) THE MISSION CLEARLY STATE HOW IT PLANS TO PURSUE ITS POLICY DIALOGUE WITH THE GOB ON THE DIVESTITURE OF THE LARGE, STRATEGIC INDUSTRIES.

3. PROJECT IMPLEMENTATION ARRANGEMENTS. THE SCOPE AND FUNCTIONS OF INTRAC MUST BE MORE CLEARLY IDENTIFIED IN THE PP. IN PARTICULAR THE NATURE OF ITS RELATIONS WITH THE DDCS MUST BE CLEARLY SPECIFIED. THE MECHANISMS THROUGH WHICH IT FACILITATES/COORDINATES THE DIVESTITURE PROCESS MUST BE OPERATIONAL WITHIN THE CURRENT POLITICAL ENVIRONMENT IN BOLIVIA AND MUST MOBILIZE HIGH LEVEL POLITICAL SUPPORT FOR DIVESTITURE AS WELL AS ELICIT INTEREST FROM THE BOLIVIAN PRIVATE SECTOR IN DIVESTITURE. IN THIS CONTEXT, THE DESIRABILITY OF NAMING A REPRESENTATIVE OF THE PRIVATE SECTOR AS THE CHAIRMAN OF INTRAC SHOULD BE EVALUATED DURING INTENSIVE REVIEW.

SUCH AS OVER-CAPACITY OR INAPPROPRIATE GOVERNMENTAL POLICIES WHICH MAY HAVE TO BE MODIFIED AS A PREREQUISITE TO DIVESTITURE. THE ASSESSMENT OF THE POTENTIAL PROFITABILITY OF DIVESTED SOES MUST EXAMINE THE INDUSTRY AND THE FACTORS WHICH AFFECT ITS PERFORMANCE, NOT JUST THE ENTERPRISE TO BE DIVESTED. FOR EXAMPLE, TO ASSESS THE FEASIBILITY OF DIVESTING MILK PROCESSING PLANTS, THE DEGREE OF OVER-CAPACITY OF ALL COMPETING PLANTS AS WELL AS THE IMPACT OF LARGE IMPORTATIONS OF POWDERED MILK MUST BE CONSIDERED. ALSO, THE NEED TO COORDINATE WITH OR ENHANCE OF SOURCES OF RAW MATERIALS, EG. MILK, MUST BE EXAMINED.

6. ALTERNATIVE MECHANISMS TO ACHIEVE PRIVATIZATION OBJECTIVES. THE PID DISCUSSES PRIVATIZATION IN TERMS OF THE SALE OF ENTERPRISES TO THE BOLIVIAN PRIVATE SECTOR (INCLUDING PRODUCERS ASSOCIATIONS AND EMPLOYEES GROUPS) WHICH IS DESCRIBED AS QUOTE GENERALLY WEAK AND LACKING SIGNIFICANT ENTREPRENEURIAL SPIRIT AND EXPERIENCE UNQUOTE. THE IDENTIFICATION OF APPROPRIATE BUYERS IS LIKELY TO BE QUITE DIFFICULT. GIVEN THESE PROBLEMS, OTHER MECHANISMS TO ACHIEVE THE SAME OBJECTIVES SHOULD BE ANALYZED. THESE MIGHT INCLUDE CLOSING ENTERPRISES; LEASING OR ENTERING INTO MANAGEMENT CONTRACTS WITH FIRMS WITH SUBSTANTIAL EXPERIENCE IN OPERATING THE SAME TYPES OF ENTERPRISES; SALE OF ENTERPRISES TO FOREIGN INVESTORS OR TO JOINT VENTURES OF BOLIVIAN AND FOREIGN INVESTORS; OR THE USE OF ALTERNATIVE BUY-OUT MECHANISMS SUCH AS AUCTIONS.

7. PROJECT DESIGN STRATEGY. THE PID STATES THAT THE ENTERPRISES TO BE DIVESTED WILL BE IDENTIFIED DURING THE PROJECT'S INTENSIVE REVIEW. HOWEVER, IT DOES NOT SEEM DESIRABLE TO MAKE DEFINITE JUDGEMENTS IN THIS REGARD DURING PROJECT DESIGN. INDEED, THIS WOULD SEEM TO BE A PRIMARY FUNCTION OF INTRAC. RATHER, THE PP SHOULD IDENTIFY THE PROBABLE AREAS FOR DIVESTITURE IN ORDER TO ASSESS THE KINDS AND AMOUNTS OF INPUTS (TECHNICAL ASSISTANCE, CREDIT) THAT MAY BE REQUIRED.

8. PROJECT IMPLEMENTATION MONITORING. THE CURRENT COMPOSITION AND LEVEL OF MISSION STAFF IS NOT CONDUCIVE TO ADEQUATE MONITORING OF PROJECT IMPLEMENTATION. THE MISSION SHOULD ADDRESS THE ISSUE OF STAFFING IN THE FORTHCOMING ACTION PLAN. THIS ISSUE MUST BE RESOLVED BEFORE PROCEEDING WITH PROJECT IMPLEMENTATION.

9. PROJECT APPROVAL AUTHORITY. GIVEN FUNDAMENTAL QUESTIONS ABOUT THE PROJECT STRUCTURE, THE POLITICAL SENSITIVITY OF PRIVATIZATION IN BOLIVIA, AND THE RAPID INCREASE IN EXPERIENCE WITH AND KNOWLEDGE ABOUT PRIVATIZATION IN LAC, THE PP WILL BE REVIEWED IN AID/W. ARMACOST

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4. PROJECT STRUCTURE:

(A) THE NEED FOR AN INVESTMENT FINANCING FACILITY. THE NEED FOR THIS FACILITY IS QUESTIONABLE GIVEN THE STAFFING AND BUDGET CONSTRAINTS WHICH EXIST AS WELL AS THE AVAILABILITY OF MULTIPLE CREDIT LINES FINANCED BY A.I.D. AND OTHER DONORS WHICH NOW EXIST, WILL BE SOON ESTABLISHED, E.G. IDB AGRO-INDUSTRIAL CREDIT, OR COULD BE QUICKLY MOBILIZED, EG. THE PRE REVOLVING FUND. THE MISSION SHOULD UNDERTAKE A CAREFUL ANALYSIS OF OTHER SOURCES OF FINANCING WHICH COULD BE MOBILIZED FOR DIVESTITURE DURING PROJECT DEVELOPMENT.

A CREDIT LINE SHOULD BE INCLUDED IN THIS PROJECT ONLY IF IT CAN BE CLEARLY SHOWN THAT THE DIVESTITURE PROCESS WILL PROCEED SO EXPEDITIOUSLY THAT SUFFICIENT RESOURCES CANNOT BE MOBILIZED FROM OTHER SOURCES. (AN ALTERNATIVE PROJECT DESIGN WHICH LIMITS A.I.D. FINANCING TO THE COSTS OF INTRAC, TECHNICAL ASSISTANCE AND FEASIBILITY STUDIES WITH ANY FINANCING FACILITY POSTPONED TO A SECOND PHASE SHOULD BE CONSIDERED.) IF A CREDIT LINE IS INCLUDED IN THE PROJECT IT WILL FINANCE ONLY WORKING CAPITAL OR THE PURCHASE OF NEW EQUIPMENT/SPARE PARTS. IT WILL NOT FINANCE TRANSFER OF ASSETS OR SEVERENCE PAY.

(B) TECHNICAL ASSISTANCE REQUIREMENTS. THE PP SHOULD CLEARLY DEFINE THE TYPES AND LEVELS OF TECHNICAL ASSISTANCE REQUIRED IN THE PROJECT. IT APPEARS THAT THREE TYPES OF TECHNICAL ASSISTANCE WILL BE REQUIRED: TECHNICAL ASSISTANCE TO INTRAC TO HELP IT ESTABLISH ITSELF AS AN OPERATIONAL ENTITY; TECHNICAL ASSISTANCE

RELATED TO DIVESTITURE, EG. FEASIBILITY STUDIES OF OPERATING DIVESTED ENTERPRISES AND IDENTIFICATION OF SPECIFIC DIVESTMENT PROCEDURES; AND SHORT TERM TECHNICAL ASSISTANCE TO PRIVATE SECTOR OWNERSHIP TO ASSIST WITH START-UP AFTER DIVESTMENT. THE PP SHOULD SET FORTH THE SPECIFIC TECHNICAL ASSISTANCE REQUIREMENTS AND SHOULD DEFINE HOW FAR THE PROJECT WILL GO TO ASSIST BUYERS AFTER DIVESTITURE. THE TECHNICAL ASSISTANCE REQUIREMENTS IMPLIED BY DIVESTITURE TO PRODUCERS ASSOCIATIONS OR EMPLOYEES GROUP WHICH MAY NOT HAVE STRONG MANAGEMENT SKILLS ARE POTENTIALLY QUITE SIGNIFICANT. THESE SHOULD BE MINIMIZED.

5. FEASIBILITY OF DIVESTITURE. THE PID IMPLIES THAT MOST STATE OWNED ENTERPRISES (SOES) ARE MONEY-LOSING PROPOSITIONS BECAUSE OF ENTERPRISE LEVEL INEFFICIENCIES THAT ARE A CONSEQUENCE OF PUBLIC OWNERSHIP. OTHER CAUSAL FACTORS MAY ALSO CONTRIBUTE RED INK TO SOE BALANCE SHEETS. THESE MAY INCLUDE INDUSTRY-WIDE FACTORS
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ANNEX B

AID 1020-26 (7-71)
SUPPLEMENT 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

(INSTRUCTION: THIS IS AN OPTIONAL FORM WHICH CAN BE USED AS AN AID TO ORGANIZING DATA FOR THE PAR REPORT. IT NEED NOT BE RETAINED OR SUBMITTED.)

Life of Project:
From FY 1987 to FY 1990
Total U.S. Funding $10,000,000
Date Prepared: April 6, 1987

Project Title & Number: INDUSTRIAL TRANSITION (511-0577)

PAGE 1

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Program or Sector Goal: The broader objective to which this project contributes:	**Measures of Goal Achievement:**		**Assumptions for achieving goal targets:**
To promote Bolivia's economic recovery and growth through more rational allocation of resources.	- Private sector investments in former SOEs will have increased by at least $30 million. Reduction of the SOE contribution to the public sector deficit.	Analysis of GOB & International organizations' related statistics. Baseline information will be established during project implementation based on specific privatization actions. This baseline information will be used to assess the project contribution towards the goal.	Continued GOB commitment to privatization. Political stability and private sector confidence.

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ANNEX B

AID 1020-26 (7-71)
SUPPLEMENT 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY 1987 to FY 1990
Total U.S. Funding $10,000,000
Date Prepared: April 6, 1987

Project Title & Number: INDUSTRIAL TRANSITION (511-0577)

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Project Purpose:	**Conditions that will indicate purpose has been achieved: End of project status.**		**Assumptions for achieving purpose:**
To increase the role of the Bolivian private sector in the country's economy through its enhanced participation and investment in productive industrial and service enterprises.	1. Reduction of the SOE contribution to the public sector deficit. 2. Reduction in the average operating costs of privatized SOEs. 3. At least 10 SOEs privatized, possibly up to 30. 4. At least 5 additional privatization actions (management contracts, leases of SOEs, etc.) implemented in central government enterprises not subject to sale. 5. Private Sector investments in former SOEs will have increased by at least $30 million.	Impact evaluations. Baseline information will be developed as part of the feasibility studies to be carried for each SOE to be privatized. Benchmarks will then be more precisely defined and evaluated by the Project Assistance Completion Date.	- the GOB will provide a consistent and continuing commitment to the privatization effort, as expressed through the establishment of INTRAC and the enactment of a Supreme Decree, if deemed necessary, to carry out privatization initiatives. - The GOB will continue its existing free market-oriented economic policies, as defined by the NEP. - The private sector will be interested in, and willing to, invest & take risks in divested enterprises. - The privatization process will have strong public support to offset negative reactions by groups with vested interests. - Sufficient financial resources from domestic sources and from international donors/financial institutions will be available to facilitate the transfer of SOEs. - Qualified individuals with enough influence, prestige and support at the highest levels of the GOB will be available to form the INTRAC and implement the privatization program.

AID 1020-28 (7-71)
SUPPLEMENT 1

ANNEX B

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY 1987 to FY 1990
Total U.S. Funding $10,000,000
Date Prepared: April 6, 1987

Project Title & Number: INDUSTRIAL TRANSITION (511-0577)

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Outputs:	Magnitude of Outputs:		Assumptions for achieving outputs:
1. The INTRAC established.	1. One established.	- Monthly, semi-annual and final project implementation reports.	- Project is able to overcome effectively SOEs' problems which limit privatizations.
2. A GOB privatization action plan developed.	2. One developed.	- Mid-term evaluation.	- Sufficient financial resources from the local private and public sectors and from international donors and financial institutions will be available to facilitate the transfer of SOEs.
3. The legal framework for the privatization of SOEs will be clarified and used as the basis for privatizations.	3. Clarified.	- ex-post project evaluations.	- Qualified individuals with enough influence, prestige and support from the highest levels of the GOB will be available to form INTRAC and implement the privatization program.
4. Privatization plans for DDCs.	4. At least 5 developed.		
5. Financing mechanisms for the transfer of SOEs established.	5. Established.		
6. feasibility studies conducted.	6. At least 10 feasibility studies for divestiture conducted.		
7. Number of investment packages for SOEs to be privatized developed for presentation to private investors.	7. At least 10 developed.		
8. An investment promotion campaign carried out.	8. Carried out.		
9. Number of SOEs privatized.	9. At least 10 SOEs privatized, possibility of up to 30.		
10. Other privatization actions, management contracts, leases, and closures.	10. At least five.		

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ANNEX B

AID 1020-25 (7-71)
SUPPLEMENT 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY 1987 to FY 1990
Total U.S. Funding $10,000,000
Date Prepared: April 6, 1987

Project Title & Number: INDUSTRIAL TRANSITION (511-0577)

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Inputs:	Implementation Target (Type and Quantity)		Assumptions for providing inputs:
A. Industrial Transition Commission	($000) AID GRANT / GOB A. (1) INTRAC staff 945 / 110 (2) Support staff - / 181 (3) Other ope.costs 50 / 119 Sub-total 995 / 410	- USAID/Bolivia, TA contractor GOB/ESF accounting and financial records. - Annual audits.	- Project which is to be incrementally funded, receives OYB funds as programmed. - GOB/ESF funds are provided to the project in a timely way.
B. Technical Assistance	B. (1) 1 LT Consultant for 42 pms. 720 / - (2) ST Consultants (143 pms) 1,859 / - (3) Local consultants (lawyers, accountants, etc.) - / 210 Sub-total 2,579 / 210		
C. Financing Mechanisms	C. Fin. Mechan. 5,496 / 4,041 Indem. payments / 2,500 Sub-total 5,496 / 6,541		
D. Other Costs	D. (1) Public Relations Campaign - / 50 (2) Project Audits/ Evaluation 100 / - (3) AID Project Coordinator 405 / - (4) Inflation/ unanticipated costs 425 / 289 Sub-total 930 / 339 GRANT TOTAL 10,000 / 7,500		

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ANNEX C

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

LAC/DR

ENVIRONMENTAL THRESHOLD DECISION

Project Location	:	Bolivia
Project Title	:	Industrial Transition
Project Number		511-0577
Funding	:	$10 million (G)
Life of Project	:	Four Years (FY'87-FY'91)
IEE Prepared by	:	Angel M. Diaz LAC/DR
Recommended Threshold Decision	:	Categorical Exclusion
Bureau Threshold Decision	:	Concur with Recommendation
Comments	:	
Copy to	:	David A. Cohen, Director USAID/La Paz
Copy to	:	Angel M. Diaz, LAC/DR
Copy to	:	Howard Clark, REMS USAID/Lima
Copy to	:	IEE File

Marea E. Hatziolos Date 12/11/86

Marea E. Hatziolos
Deputy Environmental Officer
Bureau for Latin America
and the Caribbean

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ANNEX C

ENVIRONMENTAL DETERMINATION

Project Location:	Bolivia
Project Title:	Industrial Transition Project
Project Number:	511-0577
Funding:	$10 million

Project Description: The goal of the Project is to promote Bolivia's recovery and sustained growth through more rational allocation of resources. The Project purpose is to reduce the GOB's direct participation in productive industrial enterprises and simultaneously to increase private sector participation in such endeavors.

The Project will help establish an independent temporary commission which will develop and implement an action plan to privatize selected state-owned enterprises (SOEs). Specifically, the Project will have three inter-related components, as follows: (1) Establishment of an Industrial Transition Commission (INTRAC) to coordinate all actions leading to the privatization of SOEs; (2) An Investment Financing Facility which will develop and fund financing schemes for the transfer of SOEs to the private sector; and (3) Follow-up assistance to help selected privatized SOEs during their initial stages of operations.

Statement of Categorical Exclusion: It is the opinion of USAID/Bolivia that the project does not require an Initial Environmental Examination, because its activities are within the class of actions described in Section 216.2, paragraph (c)(1)(i) and 216.2(c)(2)(i) of 22 CFR part 216 on "Categorical Exclusions", which read as follows:

"Section 216.2(C)(1)(i)"
"The action does not have an effect on the natural or physical environment", and

"Section 216.2(C)(2)(i)"
"Education, technical assistance, or training programs except to the extent such programs include activities directly affecting the environment (such as construction of facilities, etc.)."

Concurrence of Mission Director

I have reviewed the above statement and concur in the determination that the Industrial Transition Project does not require an Initial Environmental Examination.

David A. Cohen
Mission Director

Date: 11/28/86
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ANNEX D

Section 611 (E) Determination

CERTIFICATION PURSUANT TO SECTION 611 (E) OF THE FOREIGN ASSISTANCE

ACT OF 1961, AS AMENDED

I, George A. Wachtenheim, as Acting Mission Director of the Agency for International Development Mission to Bolivia, having taken into account, among other things, the maintenance and utilization of projects previously financed by USAID/Bolivia, do hereby certify that in my judgement The Government of Bolivia and the implementing agency have the financial capacity and human resources capability to effectively utilize and maintain the proposed Industrial Transition (INTRA) Grant Project.

George Wa

George A. Wachtenheim
Acting Mission Director
USAID/BOLIVIA

DATE: 4/7/87

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ANNEX E

INDUSTRIAL TRANSITION PROJECT

(No.511-0577)

STATUTORY CHECKLISTS

I. PROJECT CHECKLIST

A. General Criteria for Project

1. FY 1986 Continuing Resolution, Sec. 524 FAA Sec. 634A; Sec.653(b). (a) Describe how authorization and appropriations committees of Senate and House have been or will be notified concerning the project?	Committees notified using congressional notification procedures.
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 expectations that such action will be completed in time to permit orderly accomplishment of purpose of the assistance?	Privatization of state enterprises have taken place. If deemed necessary, a Supreme Decree, which is believed can be expeditiously issued, will allow project implementation.
4. FAA Sec. 611(b); FY 1986 Continuing Resolution, Sec. 501. If for water or water-related land resource construction, has project met the principles standards and procedures established pursuant to the Resources Planning At (42 U.S.C. 1962, et.seq)? (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 Assistance Administrator 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. Project is unique to Bolivian situation.
7. FAA Sec. 601(a). Information and conclusions whether project will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; and (c) encourage development and use of cooperatives, and credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture and commerce; and (f) strengthen free labor unions.	The project seeks to help the GOB transfer state enterprises to the private sector and to promote private investment.
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).	One of the objectives of the Project is to stimulate private investments.
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.	The GOB will provide counterpart contributions in local currency, as possible, during the life-of-project, to attain the project purpose. This contribution will be at least 25% of the LOP Cost.
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.

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11. FAA Sec.601(e). Will the project utilize competitive selection procedures for the awarding of contracts, except where applicable procurement rules allow otherwise?	Yes.
12. FY 1986 Continuing Resolution, Sec.522. If assistance is for the production of any commodity for export, is the commodity likely to be in surplus on world markets at the time the resulting productive capacity becomes operative, and is such assistance likely to cause substantial injury to U.S. producers of the same, similar or competing commodity?	No. It is unlikely that the Project result in icreased competition to U.S. producers.
13. FAA 118(c) and (d). Does the project comply with the environmental procedures set forth in AID Regulation 16? Does the project or program take into consideration the problem of the destruction of tropical forests?	Yes. It has been determined that the project will not have adverse effects on the environment. The project falls within the provisions of Section 216.2(1)(i)and 216.2(C)(2)(i).
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 expenditures of project funds (dollars or local currency generated therefrom)?	N/A
15. FY 1986 Continuing Resolution Sec.533. Is disbursement of the assistance conditioned solely on the basis of the policies of any multilateral institution?	No.
16. ISDCA of 1985 Sec. 310. For development assistance projects, how much of the funds will be available only for activities of economically and socially disadvantaged enterprises, historically black colleges and universities, and private and	None.

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voluntary organizations which are controlled by individuals who are black Americans, Hispanic Americans, or Native Americans, or who are economically or socially disadvantaged (including women)?

B. Funding Criteria for Project

1. Development Assistance Project Criteria

a. FAA Sec.102(b), 11, 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?

(a) Many project beneficiaries will be members of Producers' Associations who fall within Bolivia's lower income groups.

(b) Some of the state enterprises are expected to be transferred to cooperatives which will be strengthened through technical assistance.
(c) Bolivian self-help efforts are significant. The A.I.D. assistance only complements local efforts and resources.
(d) Women will participate in the acquisition of state enterprises to the extent they will be able to invest. Also, they will benefit as employees of privatized SOEs.
(e) N/A.

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)?

N/A.

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. The GOD and private investors will account for over 50% of the life of project cost.

e. 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.

f. FAA Sec. 128(b). If the activity attempts to increase the institutional capabilities of private organizations or the government of the country, or if it attempts to stimulate scientific and technological research, has it been designed and will it be monitored to ensure that the ultimate beneficiaries are the poor majority?

N/A.

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.

N/A.

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2. Development Assistance Project Criteria (Loans Only)

a. FAA Sec.122 (b). Information and conclusions on capacity of the country to repay the loan, at a reasonable rate of interest. — N/A

b. FAA Sec.620(d). If assistance is for any productive enterprise which will compete with U.S. enterprises, is there an agreement by the recipient country to prevent export to the U.S. of more than 20% of the enterprise's annual production during the life of the loan? — N/A

3. Economic Support Fund Project Criteria

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

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

c. ISDCA of 1985 Sec. 207. Will ESF funds be used to finance the construction of, or the operation or maintenance of, or the supplying of fuel for, a nuclear facility? If so, has the President certified that such country is a party to the Treaty on the Non-Proliferation of Nuclear Weapons or the Treaty for the Prohibition of Nuclear Weapons in Latin America (the "Treaty of Tlatelolco"), cooperates fully with the IAEA, and pursues nonproliferation policies consistent with those of the United States? — N/A

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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

II. Standard Item Checklist

A. Procurement

1. FAA Sec. 602. Are there arrangements to permit U.S. small businesses to participate equitably in the furnishing of commodities and services financed? — Yes.

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. U.S. and Bolivia

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? — Bolivia does not so discriminate.

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 a provision against such procurement, when the domestic price of such commodity is less than parity? (Exception where commodity financed could not reasonably be procured in U.S.) — N/A.

5. FAA Sec. 604(g). Will construction or engineering services be procured from firms of countries which receive direct economic assistance under the FAA and which are otherwise eligible under Code 941, but which have attained a competitive capability in international markets in one of these areas? Do these countries permit United States firms to compete for construction or engineering services financed from assistance programs of these countries? — No.

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 percent 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?	Yes.
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?	N/A
8. International Air Transport. Fair Competitive Practices. Act. 1974. If air transportation of persons or property is financed on grant basis, will U.S. carriers be used to the extent such service is available?	Yes.
9. FY 1986 Continuing Resolution 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?	Yes.

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B. Construction

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

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 manner which, contrary to the best interests of the United States, promotes or assists the foreign aid projects or activities of Communist-bloc countries? — Yes.

4. Will arrangements preclude use of financing?

a. FAA Sec. 104(f); FY 1986 Continuing Resolution Sec.526: (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 involuntary sterilization as method of family planning, or coerce or provide financial incentive to any person to undergo sterilization; (3) to pay for any biomedical research which relates, in whole or in 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.488. To reimburse persons, in the form of cash payments, whose illicit drug crops are eradicated? — Yes.

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

d. 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.

e. FAA Sec. 662. For CIA activities? — Yes.

f. FAA Sec. 636(i). For purchases, sale, long-term lease, exchange or guaranty of the sale of motor vehicles manufactured outside U.S., unless a waiver is obtained? — Yes.

g. FY 1986 Continuing Resolution, Sec.503. To pay pensions, annuities, retirement pay, or adjusted service compensation for military personnel? — Yes.

h. FY 1986 Continuing Resolution, Sec.505
To pay U.S. assessments, arrearages or dues? — Yes.

i. FY 1986 Continuing Resolution, Sec. 506
To carry out provisions of FAA Section 209(d) (Transfer of FAA funds to multilateral organizations for lending? — Yes.

j. FY 1986 Continuing Resolution, Sec.510.
To finance the export of nuclear equipment, fuel, or technology? — Yes.

k. FY 1986 Continuing Resolution, Sec.511.
For the purpose of aiding the efforts of the government of such country to repress the legitimate rights of the population of such country contrary to the United States Declaration of Human Rights? — Yes.

l. FY 1986 Continuing Resolution, Sec. 516.
To be used for publicity or propaganda purposes within U.S. not authorized by Congress? — Yes.

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Presidencia de la República
MINISTERIO DE PLANEAMIENTO
Y COORDINACION
BOLIVIA

ANNEX F

SUBCOORD Nº 15/87 1053

La Paz, 3 - ABR. 1987

Señor
David A. Cohen
DIRECTOR USAID /BOLIVIA
Presente.-

Señor Director:

Como es de su conocimiento, el Supremo Gobierno dentro su nueva política económica considera que es imprescindible acelerar el proceso de transferencia de un número de empresas estatales al sector privado. El propósito de dichas transferencias es el mejoramiento de la utilización de los recursos de nuestra economía y el movilizar los recursos, tanto económicos como financieros del sector privado, para reactivar la economía del país.

Al tomar esta decisión, estamos conscientes de la necesidad de crear los mecanismos necesarios para facilitar el proceso de transferencia de ciertas empresas. Al respecto, nos proponemos crear una comisión mixta que se encargue de coordinar todas las acciones que sean necesarias para lograr nuestro objetivo de transferir al sector privado todas aquellas empresas que sean factibles de transferencia. Deseamos que esta comisión sea lo más ágil posible, para lo cual consideramos que la misma debe tener la mayor autonomía de acción posible. Las políticas para su plan de acción estarán sujetas, sin embargo, a las políticas generales que serán establecidas por el Ministerio a mi cargo.

Por lo anteriormente expuesto, el Supremo Gobierno, mediante mi persona, solicita a usted considere la manera en que la Misión de USAID/BOLIVIA, a través de sus canales establecidos, facilite un programa de cooperación para cubrir parte de los gastos de la creación y funcionamiento de la comisión que estará encargada, bajo las normas establecidas por mi Gobierno, de ejecutar nuestra política de privatización de empresas estatales. Asimismo pensamos que será necesario se incluya en el programa de cooperación una pequeña línea de

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financiamiento que sirva como catalizador para la promoción de la inversión privada en las empresas a transferirse. El Supremo Gobierno considera que este tipo de proyecto deberá tener una duración inicial de cuatro años, a partir de la firma del convenio. Una vez transcurrido este período y en base a una evaluación, se podrá determinar si se continúa o no con el proyecto.

Para este fin, el Supremo Gobierno solicita una donación de hasta US$ 10.000.000 en moneda extranjera, provista por USAID/BOLIVIA. El Gobierno de Bolivia aportará por lo menos el 25% del costo del proyecto.

Otro aporte de gran magnitud, por parte del Gobierno y las CDD, será el financiamiento mediante condiciones en los términos de venta que facilitará la transferencia de ciertas empresas al sector privado.

Finalmente, una vez tomada la decisión sobre la transferencia de una determinada empresa o grupo de empresas, el Ministerio a mi cargo se compromete a tomar las acciones necesarias para concretar la transferencia definitiva al sector privado de dichas empresas.

Con este motivo, saludo a usted, muy atentamente.

GONZALO SANCHEZ DE LOZADA
MINISTRO DE PLANEAMIENTO Y COORDINACION

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PLANTAS INDUSTRIALIZADORAS DE LECHE (PILs)

La Paz Santa Cruz Tarija

Cochabamba Sucre

Prefeasibility Analysis

1. Executive Summary

The Plantas Industrializadoras de Leche (PILs) are the only domestic source of pasteurized milk products in Bolivia (except for a small private concern reportedly recently established in Trinidad). However, there is a substantial presence in the market of milk products from neighboring countries, both legally imported and contraband. The Cochabamba plant was established in 1960, financed by a UNICEF grant. La Paz (1972), Santa Cruz, Tarija, and Sucre (all 1978), were financed, equipped, and personnel trained by the Danish Government. The plants' chronic shortage of raw milk supply has been alleviated through cooperation with the Programa Mundial de Alimentos Fomento Lechero program, through the donation of powdered milk and other food commodities.

The design capacities and average processing volumes of the plants are as follows:

	Installed Capacity 000 liters/day	Average Processing Volume 000 liters/day	%
Cochabamba	120	45	38
La Paz	55	35	64
Santa Cruz	120	33	27
Sucre	8	2.5	31
Tarija	40	1.5	4
TOTAL	343	117	34

Potential for significantly increased raw milk supply is limited in Sucre and Tarija, and somewhat in La Paz. The three larger plants supposedly operate at break even or better while Sucre and Tarija are incurring deficits. Due to relationships with the Danish Government and PMA, and generally high public esteem, the privatization of the PIL system raises difficult policy and operational issues.

2. Background

Until 1960, fresh pasteurized milk was unavailable in Bolivia. Per capita consumption of milk was estimated at 12 l/capita/year. In that year, the first milk pasteurization plant was inaugurated in Cochabamba -- financed by a UNICEF grant. Among the conditions of the grant was a clause stating that after twelve years, ownership of the plant should be turned over to the Milk Producers Association of Cochabamba. This remained the nation's only milk plant until 1972. Then, with the aid of Danish credit and technical assistance, another plant was inaugurated in El Alto, La Paz. Three additional plants were established in 1970, in Santa Cruz, Sucre and Cochabamba. The original Cochabamba plant was dismantled and moved to Tarija. All five plants were originally owned by the CBF, but were transferred to their respective regional development corporation in 1986.

Even though annual milk consumption is currently in the 27-30 liters per capita range, milk production and consumption are not strongly entrenched traditions in Bolivia, with the partial exception of the Cochabamba valley and the Beni and Santa Cruz cattle grazing lowlands. Consequently, production of sufficient fresh milk to feed these plants has been a continuing problem, which has been aggravated by government controlled producer and retail sales prices.

To promote the growth of milk production, the World Food Program (PMA) of the United Nations works very closely with the PILs in a project whose field activities are financed by the sale by the PILS of PMA donated powdered milk in several reconstructed and processed forms. In spite of the PMA program, common operational problems are noted in each of the PILS. These are:

-- Low level of capacity utilization.

-- Relatively low levels of total milk production produced in each region is sold to the PILs. The remainder is used for direct on farm conversion to cheese, or is sold directly in non-pasteurized from to consumers, on a cost basis, often at prices higher than the retail selling price of PIL pasteurized milk.

-- Commercialization is obviously a problem.

Additionally, a problem peculiar to the Sucre, Tarija, and to certain extent, the La Paz PILs is that of limited milk production potential in their respective zones. PILs have not been established in Oruro or Potosi, as the high altitude of the region makes survival of pure bred herds virtually impossible.

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Table 1

PLANTAS INDUSTRIALIZADORES DE LECHE (PILs)

Comparative Production Data

	La Paz	Cochabamba	Santa Cruz	Sucre	Tarija
1. Year Production Started	1972	1960, 1978	1978	1978	1978
2. Nominal Design Capacity (l/day)	55,000	120,000	120,000	8,000	40,000
3. Average Total Processing Volume (l/day)	35,000	35-45,000	30-35,000	2,500	700-1,500
4. Average Fresh Milk Supply (l/day)	11,000	35-45,000	30-35,000	1,250	700-1,500
5. Average Regional Total Mil Prod. (l/day)	60,000	80,000	80-100,000	2,000	4,000
6. Average Volume Powdered Milk Processed (l/day)	23,000	-	-	1,250	-
7. Estimated Number of Producers Delivering to PIL	2,000	1,200	2,000	120	84
8. Average Volume per Producer l(l/day)	5.5	29-38	15-17.5	10	9 -17
9. PMA Program Production Expansion Potential	Fair	Good	Good	Very Limited	Limited
10. Total Employees (Plant, Admin, PMA)	123	143	92	19	29
11. Prod. Lines & Est. Vol.					
-Past. Milk (l/day)	16,000	20,000	22,000	2,500	1,200
-Powdered Milk	-	2,600 kg/d	9,000 l/d	-	1,000 kg/month
-Yogurt (l/day)	5,000	300	900	500	50
-Cheese	9,000 l/d	1,000 l/d	(?)	200 l/d	None
-Ice Cream	None	None	200 l/d	300 l/d	None
-Misc. (l/day)	5,000	2,500	Butter	Butter	Butter

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3. Description of Operations

3.1 Physical Plant and Production Characteristics

Each of the PIL plants is equipped almost entirely with Danish equipment. Design capacities vary considerably. All of the plants produce liquid pasteurized milk using either fresh milk (Santa Cruz, Cochabamba) or a mixture of fresh and reconstituted powdered milk (La Paz, Sucre, Tarija). The Cochabamba, Santa Cruz and Tarija plants have the capacity to produce powdered milk. The Santa Cruz plant has condensation in evaporation lines installed but they have never been used. All plants produce yogurt, cheese, and butter; and the Cochabamba, Sucre and Santa Cruz plants produce ice cream.

With the exception of the Tarija plant, most of whose equipment is now twenty-seven years old, the general physical condition of both plant and equipment is good to excellent. The Santa Cruz plant is in need of some routine repairs of instrumentation and control systems, and apparently has a serious boiler and cabling water hardness problem.

Table 1 summarizes in comparative form the key production characteristic for the five plants. Several points are worthy of note.

** The La Paz PIL is heavily dependent on powdered milk to achieve its total processing volume, relying on PMA shipments to make up the difference between market demand and delivered raw milk supply.

** In aggregate, the PILs receive less than half the raw milk produced in their respective regions. The reasons for this apparently are that large volumes of raw milk go directly into the production of non-pasteurized cheese, and that the PIL price to producers at Bs0.55 per liter is less than available through direct sales to consumers.

** Capacity utilization of the PILs is only 34%.

** Average liters per producer delivered daily to the PIL is low. This suggests that most PIL fresh milk is obtained from small-scale producers. This fact indicates the potential for high collection costs, and suggests that most producers are lightly capitalized, particularly in La Paz, Sucre, and Tarija.

3.2 Market Demand

More questions were raised than answered in the areas of market demand, raw material supply, and commercialization of PIL system production during the course of the field visits.

By regulation the PILs pay producers Bs0.55/l, and sell to agents at Bs0.65/l. The agent sells to the public at Bs0.70/l.

It is easy to understand why some producers would sell directly on cash basis rather than to PIL for lower prices and deferred payments. On the other hand, it is difficult to understand why a mostly urban clientele would want to pay more for a non-pasteurized product, as is reportedly the case in Santa Cruz. There is a decided need for more knowledge vis-a-vis the profiles of PIL and non-PIL consumers.

There would also appear to be a need for better consumer education, public relations and advertising on the part of PIL management. The managers, having mostly come from the production side of public sector enterprise, as a group do not appear to have the proper background to design or conduct aggressive and effective marketing programs.

3.3 Raw Material Supply

Producer prices to PIL suppliers are now fixed at Bs0.55/liter. This is reported to be a reason for the low percentage of total production to the PIL plants in each region. It is difficult to comment intelligently on problems in the area without having good production cost data. It does seem apparent, however, that the government imposed prices and yield spread take the initiative away from the Pils' ability to use some creative marketing in order to entice more suppliers.

The PMA Fomento Lechero Program and its regulations are very much intertwined with PIL operations, another factor leading to excessive organizational rigidity in the marketing area.

4. PIL Organization and Management

The five PILs were originally centralized under the CBF. Each is now the property of a different CDC, all with varying priorities concerning the pace of privatization actions. CORDELE, a liaison organization for the PILs, is located in La Paz, presumably to lobby for the PILs' interests. It is not clear how effective CORDELE is.

Plant management has been stable at La Paz, Cochabamba and Sucre, while recent changes have taken place at Santa Cruz and Tarija. Santa Cruz has reportedly had in the past more labor difficulties than the other plants.

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5. Financial and Economic Analysis

5.1 Financial

Financial data for the PILs was generally not available at the time of the field visits. The following comments are based entirely on interview responses with plant managers, or the DDC.

Debt Structure

The construction and subsequent installations in the PILs have been financed by Danish government supplied credit on very soft terms. It was not clear if all of the Danish debt was absorbed by the central government at the time of transfer, since some plant managers referred to outstanding obligations vis-a-vis Danish credit. CORDECRUZ stated that any long-term debts would not be factored in to transferral price negotiations.

Operating Results

The La Paz, Santa Cruz and Cochabamba PILs stated that they are operating above the break even point, whereas Tarija and Sucre are deficit operations at the moment, being supported to some extent by their DDCs. The Tarija plant is hopeful of gaining some ground through a plan to import powdered milk in bulk and repackage it for sale in the Tarija and Potosi markets.

Asset Valuation

PIL Santa Cruz is the only plant which has completed a recent technical evaluation of fixed assets. The study, carried out in 1986, produced a valuation of $6,000,000.

Cochabamba estimated that its assets would be valued at about $10,000,000 in a technical evaluation, a figure which would appear reasonable based upon the Santa Cruz valuation.

Based upon the above, the study teams very cursory valuation of the other PILs fixed assets would be:

La Paz	$6 - 8,000,000
Sucre	$ 750,000
Tarija	$1,000,000

It is to be emphasized that these last three are rough order of magnitude estimates.

5.2 Economic

Evaluation of the economic impact of the PILs must take into

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account the integrated nature of their operation, and the impact the PMA Fomento Lechero program has had on its beneficiaries. While it is true as alleged, that many producers do not deliver to the PIL because of their low prices and deferred payments, it is also true that most of the smaller PMA program beneficiaries would have readily accessible market outlet were it not for the existence of the PILs.

The close link between the supply side development work of the PMA program, and successful PIL operation is a complicating factor in divestiture alternatives for the PILs.

6. Privatization Issues

6.1 Basic Issues

Given the perception by many that domestic production of pasteurized milk is strategic to Bolivia, the intertwined nature of PIL and PMA Fomento Lechero operations, the Danish financial assistance, and the fact that each PIL is essentially a regional monopoly, a number of issues surrounding eventual privatization are raised. None can be resolved without considerable further dialogue, study, and negotiation. Among these are:

-- If the PILs are transferred to private individuals or corporate entities, access to Danish credit lines and technical assistance, and the relationship with the PMA Fomento Lechero program would be immediately terminated. If, however, a mixed enterprise or cooperative arrangement were to be organized both would reportedly continue, particularly if producer groups were involved.

-- The essentially small size and weak capital base of the La Paz, Sucre and Tarija producer associations would appear to call into question their financial and managerial capability to buy out and operate the regional PILs. The Cochabamba and Santa Cruz producer groups are probably more capable, but considerable intensive technical assistance in dairy management and general business orientation would be required.

-- Government pricing policies, import restrictions on dairy products, and control of contraband would be critical to the success of PIL divestiture.

6.2 Privatization Recommendations

** Conduct an industry-wide feasibility study of the possibility of divesting the PILs.

** Investigate the level of technical/managerial assistance required by the PILs if transferred, particularly focussing on marketing and commercialization.

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ALIMENTOS BALANCEADOS PORTACHUELO (ALBAPOR)

Prefeasibility Analysis

1. Executive Summary:

ALBAPOR is a CORDECRUZ-owned animal feed mill located in Portachuelo, 90 km. north of Santa Cruz. Its recent annual production has averaged 15,000 tons per year; 90% of sales value is for chicken feed and 10% cattle and pork feed. Design capacity is about 18,000 tons per year per one shift. Raw material silo storage is 2,000 tons, which poses somewhat of a price and availability constraint on current operations.

ALBAPOR is the largest of seven chicken feed mills in Santa Cruz, accounting for a 25-30% market share of external sales. Due to the vertically integrated nature of the privately owned mills, ALBAPOR faces a deteriorating market situation unless it can also integrate vertically with broiler and egg producers to provide a captive market.

ALBAPOR appears to have a financially viable operating position at present, in a growing but highly competitive overall market. A Portachuelo based producers group of 30-40 producers is interested in buying ALBAPOR and is in the process of also establishing an incubation and broiler reproduction operation. These elements would provide both ALBAPOR and the individual producers with better market prospects. A recent valuation study placed the plants fixed assets value at $1,100,000. The interested producer group states that it can raise $250,000 equity capital. Each investor would be limited to a maximum participation of one of approximately forty to-be-issued shares to avoid concentration of ownership. Several alternative buy-out possibilities are being investigated.

ALBAPOR represents the best concrete test case of how INTRAC might assist in privatization efforts. It is recommended that a dialogue be opened with CORDECRUZ and ALBAPOR in order to identify specific forms of technical and financial assistance which INTRAC could provide.

2. Background:

ALBAPOR is an animal feed mill production operation located in Portachuelo, approximately 90 km. to the north of the city of Santa Cruz. It began operations in December 1976. Initial financing was provided by the Comite de Obras Publicas. The mill is one of seven commercial scale animal feed mill preparation operations in the Santa Cruz area, but the only one which is owned by a public sector entity. CORDECRUZ owns 100% of its stock. A broiler chicken producer group whose operations are concentrated in the Portachuelo area is actively seeking to purchase the mill from CORDECRUZ, as one step in a plan to establish a vertically integrated broiler production operation in the Portachuelo area. The principal market would be metropolitan Santa Cruz.

Description of Operations:

3.1 Physical Plan and Product Lines

The ALBAPOR plant is a grain blending and concentrate preparation operation with a design capacity of approximately 1,500 tons per month of feed production. It has recently been producing an average of 1,200 tons per month. Principal product lines are chicken feed (90% of sales) and cattle and pork food preparation (10% of sales). The plant has only 2,000 tons of raw material storage capacity in four silos, and would like to add an additional two silos of 1,000 ton capacity each, at an estimated capital cost of $100,000.

3.2 Markets

ALBAPOR currently accounts for a 25-30% share of chicken feed sales in the Santa Cruz area, and is the largest of the seven commercial scale animal feed mills there. Forty five percent of its sales are to local Portachuelo broiler producers, with the remainder being sold in other areas of Santa Cruz Department. ALBAPOR faces a deteriorating market situation in its current form. The six privately owned feed mills are all part of vertically integrated operations for which internal sales account for the greatest share of productions. The continued expansion of these operations makes increasingly difficult the situation of smaller non-integrated producers, even though total broiler chicken consumption in the Santa Cruz area continues to grow. The basis appears to exist in Portachuelo to create a vertically integrated broiler production.

There are now about 40 to 50 commercial scale broiler producers who now must depend upon their integrated competitors for supply of one day old chicks. They are now in the process of establishing a cooperative (AVIPOR) for a chick incubation and reproduction operation. With the addition of AVIPOR, they would be able to establish a competitive integrated broiler production operation. ALBAPOR management and CORDECRUZ are both of the opinion that unless ALBAPOR becomes part of a vertically integrated operation, it will be forced out of business within a 2-3 year period of time.

Most Portachuelo-based broiler operations average about 5,000 broilers capacity in size. Santa Cruz area mortality rates are 7% versus 2% for Cochabamba. Purchase price of one day old chick is $0.10 each but availability is becoming

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an increasing problem. Total broiler production in the Portachuelo area is estimated to be 275,000 per two month cycle.

3.3 Raw Material Supply

ALBAPOR purchases its corn and soya directly from Santa Cruz area producers. Due to the limited current storage capacity (2,000 tons) in relation to annual production (13,000 tons), it is often forced to purchase grain during periods of relatively high off season prices. The grain silo storage loading capacity is approximately 10 tons per hour.

4.0 Plant Organization and Management:

ALBAPOR is 100% owned by CORDECRUZ. The plant has a total employment including production, administration, management and sales force of fifty-two employees. A sales a liaison office is maintained in Santa Cruz.

5. Financial and Economic Assessment:

5.1 Financial

Partial preliminary financial records for 1986 were made available. According to these, total gross income for the year from all sources was $4,673,000 and total variable and fixed costs amounted to $3,854,000 having a gross operating surplus of $819,000. The average value of raw grain in inventory is approximately $1,000,000. This is normally financed on terms of 60 days with maintenance of value and 2-5% interest.

ALBAPOR has already had a fixed assets valuation carried out. The estimate was $1.100,000. A second independent estimate paid for by an interested producer group was to have been available by 15 February 1987.

5.2 Economic Assessment

Broiler and egg production in Santa Cruz is, by Bolivian standards, a large and growing industry. All broilers are currently consumed in the local market as there is not yet a frozen chicken industry in Bolivia, and distances to La Paz are too far to permit marketing of Santa Cruz produced broilers on a fresh basis. Santa Cruz does export eggs to La Paz, as their production costs are lower than in Cochabamba (lower feed costs).

The existence of large numbers of producers and seven feed mills in Santa Cruz is ample evidence of a competitive market structure. The increasing vertical integration of larger producers would tend to lessen this competition and force many smaller producers out of business. Given this structure, it would definitely be in the public interest if ALBAPOR via the privatization plan envisioned could become a competitive, producer owned operation.

6. Privatization Issues:

6.1 ALBAPOR Privatization Policy

Of the enterprises visited during this study, ALBAPOR is probably the furthest advanced in terms of privatization planning. The current general manager is one of a group of thirty local Portachuelo-based broiler producers, who have signed a letter of willingness to purchase, which was officially transmitted to CORDECRUZ on 7 January 1987 (copy available). This group accounts for 30-40% of total current feed sales of ALBAPOR.

6.2 Financial Plan for Purchase

The ALBAPOR general manager indicated that among the thirty signees of the letter, and possibly 10 additional participants, all of whom are also Portachuelo area producers, capital availability for purchase is estimated to be in the rage of $250,000. In order to avoid concentration of ownership within the buyer/producer group, it is contemplated that each individual producer would have the right to only one of forty stock shares to be issued. Fractional shares could be acquired by smaller producers.

ALBAPOR would like to explore several ownership alternatives, among which are a 49%/51% CORDECRUZ-ALBAPOR (majority) and a 20% CORDECRUZ-80% ALBAPOR arrangement. At the present, the ALBAPOR purchase group is thinking in terms of 5 to 8 years payment terms. They would also require financing for working capital and construction of the additional storage silos.

6.3 Specific Privatization Recommendations

ALBAPOR represents the most concrete case visited of a privatization buy-out which appears to be "doable" over the near future. It would appear to represent a specific test case to determine what types of technical and financial assistance, and coordination efforts the INTRAC project can bring to privatization efforts. It is, therefore, recommended that a dialogue be opened with CORDECRUZ and ALBAPOR to identify the assistance to be provided which will facilitate a transition.

6.4 Environmental

As is characteristic of feed mills, ALBAPOR is a very dusty operation. Environmental regulations for USAID's participation in a project of this nature should be reviewed to see if any amelioration requirement exists.

ALIMENTOS BALANCEADOS TARIJA (ALBAT)

Prefeasibility Analysis

1. Executive Summary:

ALBAT is a CODETAR-owned animal feed mill located on the outskirts of Tarija City. Its recent production has averaged 5,000 tons/year, or about 20-25% of one shift capacity utilization.

ALBAT is virtually a carbon copy of the ALBAPOR Portachuelo mill in design and size. It is the only commercial scale feed mill in the Tarija market with outside sales. Its only viable market is local broiler and egg producers, who account for 95% of sales.

Lack of raw material grain supply in Tarija during the dry season, coupled with insufficient storage capacity (2,400 tons) for such conditions has sometimes led to shutdowns for lack of raw material.

ALBAT management states that the company is operating in a more or less break-even position at present, although financial reports were not made available.

Two groups are reportedly interested in purchasing ALBAT. The first is the local broiler producers association; and the second, a private individual investor with no other broiler or egg producing industry affiliation. Public interest would dictate that in a monopoly situation which this plant represents, caution should be exercised before permitting an individual buy-out.

CODETAR has passed a resolution authorizing divestiture of ALBAT and IAT, an inactive chicken processing operation. No concrete buy-out plans have materialized as yet. The IAT plant is adjacent to ALBAT but ceased operations two years ago.

It is recommended that ALBAT be given high priority as a test case for INTRAC to establish a dialogue with the concerned parties concerning specific technical assistance requirements which could be provided.

2. Background:

ALBAT is an animal feed mill production operation located in Tarija city. It was built and is completely owned by CODETAR. The original construction cost was $960,000. Operations commenced in 1978. ALBAT is the only commercial scale feed mill in the Tarija area with outside sales. A second local mill supplies a related integrated operation. Two groups have expressed an interest in purchasing the mill. One is the local Asociacion de Avicultores, and the second is reportedly the owner of a local brewery. The producers' association is also interested in acquiring a CODETAR owned broiler processing operation which has been closed for two years (IAT). Resolutions have been passed by the CODETAR board authorizing the right to divest these two operations.

3. Description of Operations

3.1 Physical Plant and Product Lines

The ALBAT plant is virtually a carbon copy of the ALBAPOR plant in Portachuela, Santa Cruz. Its design capacity for one shift operation is 18,000 tons/year of blended feed grains, or 9-10,000 tons/years of feed pellets. Production has been averaging 5-6,000 tons annually in recent years, with a 50-50% split between grain and pellets. Raw material storage capacity of 2,000 tons is reportedly a more serious limitation at Tarija than Portachuela due to the virtual non-availability of grain supplies in Tarija during the dry season.

3.2 Markets

There is basically only one market for ALBAT production, the chicken producers of the surrounding Tarija area. Chicken feed accounts for 95% of sales. Local consumption of broilers is estimated at 2,000/day.

An assumed conversion of 2.5 kg feed/kg chicken, and an assumed chicken weight of 2 kgs, the total local demand for feed grain for broilers would be 3,700 tons/year. This indicates the limited potential of the local market under current consumption patterns. The only alternative source of supply for local producers is to purchase feed from Santa Cruz sources or import from Argentina, both of which are very high-cost alternatives. ALBAT is, therefore, essentially a regional monopoly.

3.3 Raw Material Supply

Raw material supply is apparently a problem in Tarija during the dry season. Combined with the somewhat limited storage capacity (2,000 tons), the dry season unavailability has sometimes resulted in plant shutdowns for lack of raw material. Plant management states that the problem is resolvable by expansion of storage capacity to 5,000-6,000 tons.

4. Plant Organization and Management

ALBAT is 100% owned by CODETAR. The plant has a total employment of 18, which would appear to indicate a more efficient operation than that of ALBAPOR.

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5. Financial and Economic Assessment

5.1 Financial

Financial statements were not available. The plant manager stated that production costs in 1986 were Bs0.407/kg ($0.21/kg) and average sales prices were slightly higher. Labor accounts for 5% of production cost and raw material purchases 72%. The plant would by these measures, appear to be breaking even on operations.

An assets valuation study is planned, but has not as yet been carried out. The plant manager estimates the value of fixed assets to be in the neighborhood of $1,000,000.

5.2 Economic Assessment

The fact that ALBAT is an apparently financially stable monopoly supplier of feed grains in a limited scale market, raises an important public interest policy issue concerning the nature of eventual private sector purchases. If owned by a producer association of many members, it can be assumed that their interests would best be served by minimizing their total production costs from incubator to consumer, a factor which would trend to lead towards an efficient feed mill operation.

If in the hands of a private individual investor whose only interest is maximizing his profit on mill operations, his interest would best be served by raising feed grain prices to somewhat less than the Argentine import or Santa Cruz sources alternatives.

6. Privatization Issues

6.1 Potential Buyer Group

The privatization process of ALBAT and IAT, though authorized by the CODETAR board, does not seem to have acquired momentum. Contrary to ALBAPOR, where plant management is a part of the interested buyer group, ALBAT management would appear to be at best lukewarm to the concept.

The local chicken producers association has not yet produced any financial plan nor given evidence of how much of its own capital it could assemble for equity purposes.

It would appear at this time that a buy-out offer by an individual would not be well received by CODETAR.

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6.2 Specific Privatization Recommendations

ALBAT represents a case, along with ALBAPOR, where a buy-out might be a "doable" proposition under the right circumstances. It, too, should be included as a test case for early provision of INTRAC technical and perhaps financial assistance. It is, therefore, recommended that a dialogue be established with CODETAR, ALBAT, and potential buyers to identify the specific needs in assistance which the project could provide to facilitate a transition.

EVALUATION OF SOEs FOR PURPOSE OF DETERMINING A JUSTIFIABLE SALES PRICE FABRICA DE FOSFOROS and FANVIPLAN

To illustrate the proposed methodology for evaluating SOEs for the purpose of determining justifiable selling prices, two companies -- Fabrica de Fosforos and FANVIPLAN -- were selected as case studies. They are not actual evaluations since the assumptions made to arrive at the selling prices were arbitrarily chosen, and are not necessarily based on facts. In an actual evaluation, such facts would have to be determined through a detailed feasibility study, which was not within the scope of this consulting assignment. Thus, the two cases serve illustrative purposes only.

Case 1 -- Fabrica de Fosforos -- refers to a "mixed company" with participation of state and private capital. State-owned shares are owned directly by the Central Government represented by the Ministry of Industry, Commerce and Tourism. Case 2-- FANVIPLAN -- examines a company whose entire capital was owned by the government through the Bolivian Development Corporation (CBF) and subsequently transferred to a Regional Development Corporation (RDC) by Supreme Court Decree No. 21060.

Case 1: FABRICA NACIONAL DE FOSFOROS, S.A.M.

Background:

The Fabrica Nacional de Fosforos or National Match Company was established as a Sociedad Anonima Mixta (S.A.M.) or mixed company in 1954 with a capital of $500,000 distributed among the State, 51% ($255,000) and private shareholders, 49% ($245,000)

The share distribution was subsequently modified as shown below:

Shareholders	No. of Shares	%	$Bs	US$
State	8,280	54.00	16,983,013	828,089
Israel Sanderey	4,662	30.40	9,510,141	466,388
Rodolfo Matta	1,414	9.22	2,884,327	141,389
Banco Central	561	3.66	1,144,971	56,126
Imprex Incobil	104	0.68	212,727	10,428
Jose Gamarra Z.	34	0.22	68,833	3,379
Bearer	279	1.82	569,357	27,910
	15,334	100.00	31,373,369	1,533,709

Banco Central's ownership of 3.66% represents, in effect, also government capital. The Central Bank received these shares as collateral from another bank which went bankrupt. However, title to the shares is not clear since they were never legally transferred to the Central Bank. As of this moment, the shares in question are still considered part of the private sector package.

As a result of total illiquidity experienced in 1981, the private shareholders entered into an agreement with the Government approved by CONEPLAN (the Government's Economic and Planning Council) in its meeting No. 37, on 11/20/81, which resulted in the private shareholders making a capital contribution of Bs3,348,721 ($167,436) and taking over management of the company. In addition, the Government granted an option to the private shareholders to acquire the remaining state-owned shares within six months subject to the completion of a financial evaluation of the Company's equity by an independent consulting firm. Such evaluation was to serve as a basis for the Direccion General de Bienes del Estado to establish a fair price for the shares. The option was granted on June 17, 1982.

The capital increase, entirely subscribed by Mr. Sanderey, resulted in the following share distribution:

Shareholders	Capital (Bs)	Revaluation of Fixed Assets (Bs)	Total	%
	17,492,128	164,549,264	182,041,392	48.34
Private	18,249,423	176,307,316	194,556,739	51.66
	35,741,551	340,856,580	376,598,131	100.00

The acquisition of the optioned shares, repeatedly demanded by the private shareholders, has not been completed to date in spite of compliance by the private shareholders with all the conditions stipulated in the option agreement. In the meantime, private shareholders had to contribute additional cash to support continuous operating losses. The additional contributions totalling Bs266,767,550 ($138,581, at the average 1986 exchange rate) will increase private ownership to 71.7% if and when capitalized.

There are apparently two reasons for the delay in completing the transfer of optioned shares. One is the legal mechanism and the other is an agreement on price. With regard to the legal problem, the company was properly incorporated as a Sociedad Anonima Mixta in accordance with Article 424 of the law of Sociedades de Economia Mixta.

As such, it is subject to the regulations of the commercial law. Thus, the transfer of state-owned shares should be able to be accomplished simply through a Supreme Decree issued by the President of the Nation. A draft of a Supreme Decree has been prepared and was apparently submitted to the Ministry of Industry, Commerce and Tourism. Officials of this Ministry, however, argue that in accordance with the Constitution of Bolivia, government-owned property can be transferred to private ownership only through an act of Congress. This conflict of opinion has not been resolved to date.

With regard to selling price, the Government is awaiting a new revaluation of assets as of 12/31/86 before deciding an asking price and commencing serious negotiations. In the meanwhile, the Ministry of Industry, Commerce and Tourism has established as the minimum price for the state-owned shares the original value of its investment in U.S. dollars plus non-compounded interest at an annual rate of 8% for 23 years:

	U.S. dollars
Original Investment	255,000
Non-compounded interest at 8% annually, for 23 years	469,200
Minimum Sales Price	724,200

On the other hand, the option agreement indicates the value of the 8,280 state-owned shares to be the equivalent of US$679,320.

The Fabrica Nacional de Fosforos initiated production in December 1958, four years after its formation. The best years occurred between 1965 and 1974. Production has decreased steadily since 1971 and profits turned into steady losses as may be observed from the following figures.

Year	Production (Million Boxes)	Profits or (losses) (Bs000)	(US$000)
1971	60.6	387.7	32.3
1972	53.6	38.7	3.2
1973	51.0	450.3	22.1
1974	53.2	336.1	16.5
1975	52.4	(483.5)	23.7)
1976	59.4	4.9	0.2
1977	58.1	692.1	33.9
1978	48.4	(640.1)	(31.4)
1979	44.4	(8,682.8)	(354.3)
1980	28.3	(14,320.2)	(584.3)
1981	29.4	(7,538.3)	(307.6)
1982	40.1	(14,912.0)	(76.1)
1983	37.1	(61,762.3)	(123.5)
1984	23.4	(176,770.3)	(20.6)
1985	27.9	(323,120.1)	(177.5)
1986*	6.5	(479,207.0)	(248.9)

* (Estimated)

There were three basic reasons for the poor performance of the company:

1. Loss of market to illegal imports, first from Peru and later from Brazil. Upon its formation, the company was granted exclusivity by the Government for an initial period of ten years. This exclusivity was renewed twice for 10-year periods, expiring in June 1989. The company interprets the exclusivity to mean both exclusive manufacturing and selling rights in the territory of Bolivia. The exclusivity was revoked in August 1985 by Supreme Decree No. 21060. The revocation was of little significance since the Government had never enforced the exclusivity by failing to make any attempt to stop illegal imports. The smuggled matches readily captured the Bolivian market because of better quality and lower prices. To defend itself against this unfair competition, Fabrica Nacional de Fosforos registered the Brazilian brand in Bolivia in their own name and has started to use recently an identical copy of the Brazilian label on their own match boxes.

2. Poor quality was due to lack of appropriate wood (poplar) for matchsticks in Bolivia and poor appearance of the package. The problem of appropriate wood has been partially solved by using certain varieties of naturally grown trees in virgin forests of Chapare, State of Cochabamba. Since various types of trees are used, there is no uniformity of raw material and costs are high due to the difficulty of getting trees out of the natural forest and the long haul to La Paz. The company has some forestation projects on the way which may solve the problem eventually.

3. High manufacturing costs are partly due to the high cost of wood and partly to inefficient operation. The latter is caused by poorly maintained equipment in need of a thorough overhaul and by inadequate factory and production management.

Valuation Concepts

The price per share is most equitably determined through actual transactions in a stock market or, in the absence of a stock market, through free negotiations between seller and buyer. To determine an offering price that could serve as a basis for negotiations, one must determine the fair market value of the company and then divide this value by the number of outstanding shares.

There are various "value" concepts which may be defined as follows:

Revalued assets

The updated values assigned to tangible assets through the process of "technical revaluation" as prescribed by Bolivian law. The technical revaluation may consist of an appraisal by experts, a computation based on original value adjusted by deflation factors to reflect monetary inflation, or a value derived from replacement cost depreciated for the years in use at the customary rate of depreciation.

Book value

The value shown in the financial statements, preferably audited statements, of a business. Book values may or may not reflect revalued assets, depending on whether or not the "technical revaluation" has been completed prior to the date of the financial statement.

Market value

The price that a prudent businessman would pay for an asset acquired through public auction or negotiated in an arms-length transaction.

Economic value

The reasonable price that may serve as basis for negotiating the sale of an enterprise which has been determined from the discounted cash flow that a company is capable of producing with its existing asset base.

Determination of the fair market value requires in most cases a complete feasibility study to be able to project future earning's streams achievable with existing assets. To illustrate the valuation concepts, certain assumptions have to be made without the benefit of a proper feasibility study. Thus, the figures presented herein should not be regarded as anything but illustrative.

The assumptions are that by imitating the Brazilian label on their match boxes, improving quality and lowering production costs, the company will be able to regain a large share of the Bolivian market. Thus, it is assumed that sales of 48 million units will be reached within two years, and 72 million units within four years. The latter volume would require adding a second shift. It is further assumed that match boxes are sold for US$10.00 per thousand, and that net profits are 9.5% of sales at the 48 million volume level and 12% at the 72 million level. Other assumptions are that there will be no new capital expenses (investments) and that depreciation is insignificant ($249 in 1985) since most of the fixed assets are almost 30 years old. Thus, bottom line (net) profits are equal to cash flow.

On the basis of the above assumptions, the cash flows projected for the next ten years and their Net Present Value (NPV) discounted at 20% are shown in the following table. The 20% discount rate was chosen because this is the current rate of interest paid on bank deposits. NPV is a financial concept and means that a dollar received in the future is worth less than a dollar received today because today's dollar can be invested and earn at least the current interest paid on bank deposits. Thus, NPV is the present value of each dollar at the end of the year indicated on the table below discounted at the cost of capital.

Year	Cash Flow (US$)	20% Discount Factor (From Discount Table)	NPV (US$)
1	22,800	0.83	18,924
2	45,600	0.69	31,464
3	45,600	0.58	26,448
4	86,400	0.48	41,472
5	86,400	0.40	34,560
6	86,400	0.34	29,376
7	86,400	0.28	24,192
8	86,400	0.23	19,872
9	86,400	0.19	16,416
10	86,400	0.16	13,824
Total			256,548

The sum of the net present value of all cash flows over the ten-year period is US$256,548. This means that if the investor were to deposit US$256,548 in a bank at 20% compounded interest, he would earn over a ten-year period an amount equal to the sum of all the cash flows compounded at 20% or US$1,589,000. The compounded computations are illustrated on the following two tables:

Compounding Cash Flows Invested at 20% Interest

Year	Investment		Interest		Cash Flow		Next Year's Investment
	(a)	+	(b)	+	(c)	=	(d)
1	-		-		22,800		22,800
2	22,800		4,560		45,600		72,960
3	72,960		14,592		45,600		133,152
4	133,152		26,630		86,400		246,182
5	246,182		49,236		86,400		381,818
6	381,818		76,363		86,400		544,581
7	544,581		108,916		86,400		739,897
8	739,897		147,979		86,400		974,276
9	974,276		194,855		86,400		1,252,253
10	1,252,253		250,506		86,400		1,589,159

Compounding US$256,548 Invested at 20% Interest

Year	Investment (a)	+	Interest (b)	=	Next Year's Investment (c)
1	256,548		51,309		307,857
2	307,857		61,571		369,428
3	369,428		73,886		443,314
4	443,314		88,663		531,977
5	531,977		106,395		638,372
6	638,372		127,674		766,046
7	766,046		153,209		919,255
8	919,255		183,851		1,103,106
9	1,103,106		220,621		1,323,727
10	1,323,727		264,745		1,588,472

Based on these considerations, an investor would have to be able to buy the company that produces the above indicated cash flows for an amount less than US$256,548 to compensate for the risk he assumes in operating the company and to give him an incentive to assume such risk.

In view of the above consideration, a fair offering price to start negotiations between seller and buyer, would lie somewhere between 0.66% ($170,000) and 0.75% ($192,000) of the net present value of cash flows produced over a 10-year period. This is what may be called the "economic value" of the enterprise. This value divided by the number of outstanding shares would be the offering price per share. It would allow an investor to recover his investment in little less than four years. This is considered the maximum reasonable pay-back period for prudent investments under the present social, political and economic environment of Bolivia.

Having established the economic value of the enterprise, it must be compared to its liquidation value. Assuming that the revalued worth of fixed assets as of 12/31/86 is an acceptable figure, the liquidation value may be computed as follows:

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	Balance Sheet 12/31/86 (Bs)	%	Recovery Bs	US$
Cash Items	3,466	100	3,466	1,733
Inventory	15,030	100	15,030	7,515
Goods in Process	17	0	0	0
Investments	58,208	80	46,566	23,283
Land	970,000	80	776,000	388,000
Buildings	1,357,497	80	1,085,998	542,999
Equipment	457,116	50	228,558	114,279
Total Assets	2,861,334		2,155,618	1,077,809
Less Liabilities	482,362*	100	482,632	241,181
Liquidation Value			1,673,256	836,628

* Bs266,767 is the cash contribution made by private shareholders and is shown on the tentative unaudited 12/31/86 balance sheet as a liability to Agencia Distribuidora. This amount was deducted from total liabilities under the assumption that it will be capitalized and corresponding new shares will be issued.

It will be noted that the liquidation value of US$836,628 is considerably higher than the economic value previously calculated.

Valuation figures determined so far lead to two apparent conclusions:

1. The Government can recover a larger amount of its investment by closing the company and selling its assets (i.e., liquidation) than it may achieve through the sale of its share holdings.

2. Even upon liquidation, the Government would not be able to recover the amount stipulated in either the stock option agreement or the proposed Supreme Decree as can be observed from the following summary:

	Total Price of 8,280 State-owned Shares (US$)
Stock Option Agreement	679,320
Proposed Supreme Decree	724,200
Economic Value (180,000 x 28.3%)*	50,940
Liquidation Value (836,628 x 28.3%)*	236,766

28.3% State ownership assumes that all of private shareholders cash contributions have been capitalized.

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Further analysis, however, indicates still another possibility. The capital base of the company may be reduced by relocating the factory to a less expensive location closer to the source of raw material in the Chapare forest area and selling the La Paz facility. The sale of the La Paz property would generate about US$931,000 which could be applied to paying off all liabilities (US$241,000), building a small new light construction plant and improving the manufacturing equipment (US$290,000), and leaving a cash balance of US$400,000. A private investor could use this cash balance plus another US$436,000 of his own funds to acquire the company at its liquidation value. The improved production efficiency in a modernized plant and the reduced cost of raw material may generate sufficient profit improvements to raise the economic value of the company to its current liquidation value. A complete feasibility study should consider this possibility. Jobs lost in the La Paz area would be counterbalanced by new jobs created at the relocated facility.

There is one more consideration to be investigated during a thorough feasibility study and that is the distribution system. It seems that there may exist some kind of exclusive distribution arrangement with an agent related to one of the private shareholders. A note to that effect in the 1985 audited statement indicates that the auditors were unable to determine the legal status of the "Agencia Distribuidora" nor the contractual basis for the company's substantial liabilities to this agency. The company's profitability could be seriously distorted unless an arms-length deal exists between the company and its distributor.

As can be seen from the above analysis, valuation of a company's shares, in the absence of stock market transactions, is a complicated process which requires thorough analysis by a professional management team.

Case 2: FABRICA NACIONAL DE VIDRIO PLANO "FANVIPLAN"

Background:

FANVIPLAN is the only flat glass factory in Bolivia. It was designed by an East German consulting company GOPA in 1971. The projected capacity of 9,6000 metric tones per year was to cover the entire needs of the Bolivian market plus enough exports to generate sufficient hard currency for the importation of soda ash.

The Corporacion Boliviana de Fomento (CBF), a development agency of the GOB, was authorized by Supreme Decree 11002 of July 27, 1973 to contract for a turn-key installation of the plant. The public bid was won by a Polish firm POLIMEX CEKOP and start up was schedules for December 1977. Design changes during construction and late receipt of funds from the Central Bank and National Treasury delayed actual start up until July 1981. The design changes involving conversion from fuel oil to liquified gas and back to fuel oil increased costs by more than US$650,000.

CBF set up FANVIPLAN as a semi-autonomous enterprise with its own management but without an independent legal personality. It operated the company until March 31, 1986 when FANVIPLAN was transferred by Supreme Decree 21060 to CORDEPAZ, the Regional Development Corporation of La Paz. At present, FANVIPLAN continues operating as a 100% regional government-owned enterprise (CORDEPAZ) without legal personality.

The equipment is mostly of Polish origin, except for the combustion system (Stordy of Holland and Laidlaw Drew of the UK) and refractory material (Motim of Hungary). Some of the equipment was reported to be overhauled used machinery. The process uses the "Fourcault" system developed in 1915 which has been obsoleted by the "Pittsburgh" (1940) and the "Float" (1960) systems. Nevertheless, the simplicity of the process and its low investment cost was felt to be adequate for the Bolivian market requirements.

The nominal production capacity of the plant is 6,700 metric tons/year or 1,340,000 square meters RAS of flat glass. The single oven with two outlets holds 350 tons of glass and has a melting capacity of 30 tons/day. It produces flat glass from 2 to 8 mm thick and up to 1.80 meter wide. Some glass is converted manually into opaque glass (sand blasting) and mirrors. Employment includes 140 labor and 20 administration.

Glass produced by FANVIPLAN is wavy and considered of second and third quality. Nevertheless, the plant supplies about 70% of the domestic market and also exports to Peru. The waviness is reportedly caused by certain spare parts made in Bolivia which should be replaced when the oven is cooled down for replacement of the refractory material. This major overhaul will be necessary within the next 12 months, at a cost of approximately US$1.2 million and estimated minimum down-time of three months.

The plant's present output of approximately 40,000 square meters per month is 42% of its effective capacity of 95,000 square meters per month. The production cost at this rate is US$2.35/sq. mt. (excluding depreciation). The cost would decrease to US$1.50/sq. mt at a production level of 70,000 sq.mt/month and to US$1.35/sq. mt at a production level of 95,0000 sq mt/month.

The above figures suggest that FANVIPLAN's strategy of eventually improving the quality of its glass (when oven is shut down to be rebuilt) in order to increase both domestic and export sales is appropriate. For 1 87, the company projects sales of 411,500 sq. mt. domestically and 123,800 sq. mt for export. The domestic sales prices is US$2.80 per sq. mt. and the export price is US$2.25/sq. mt. The resulting sales volumes are US$1,152,000 and US$278,500, respectively, for a total projected income of US$1,430,500. For comparison purposes, the price of imported glass from Brazil is US$4.00 per square meter in Santa Cruz.

Production and sales since the plant's start up in July 1981 until June 1986 are summarized below:

Year	1981 (6 mos)	1982	1983	1984	1985	1986 (6 mos)
Production (sq. mts)	361,321	1,109,158	707,548	736,113	903,047	223,318
Sales (sq. mts)						
Domestic	-	636,866	607,245	457,781	418,624	164,610
Export	-	181.959	67,082	25,603	26,324	41,518
Total	-	818,825	674,327	483,384	444,948	206,128

It is interesting to note that best production (nearly 100% of effective capacity) was achieved during the first full year of operation after start-up. Sales have steadily decreased from the 800,000 square meters annual level to about 400,000 square meter annually. This may partly be due to a lack of technical skills in the plant resulting in poor production and poor quality which in turn may have affected sales. Most likely, however, decreased sales are the reason for reduced production. High production and low sales in 1985 were probably caused by an unusual economic environment experienced during that year.

Valuation Concepts

The closing balance sheet as of March 31, 1986 when FANVIPLAN was transferred from CBF ownership to CORDEPAZ is summarized below:

TABLE
FANVIPLAN BALANCE SHEET
(as of 3/31/86)

ASSETS	Bs	US$	LIABILITIES	Bs	US$
Cash & Receivables	95,653	48,735	Current Liabilities	10,645,394	5,423,852
Inventories	1,515,980	772,395	L. T. Debt	49,311	25,124
Prepaid Expenses	1,541,479	785,387	Various Liabilities	5,528	2,817
			Employee Benefits	194,669	99,184
Current Assets	3,153,112	1,606,517			
Other Investments	3,154	1,607	Total Liabilities	10,894,702	5,550,977
Fixed Assets (net of depreciation)	11,573,421	5,896,684	EQUITY		
Total Assets	14,729,687	7,504,808	Capital	106	54
			Revaluations	4,368,533	2,225,777
			Less Accum. Losses	(533,854)	(272,000)
			Shareholders Equity	3,834,785	1,953,831
			Total Equity & Liabilities	14,729,687	7,504,808

According to Supreme Decree 21060 which authorized the transfer, the Central Government was to absorb all liabilities except for employee benefits (severance and indemnization for years of service). Accordingly, the opening balance sheet of FANVIPLAN under CORDEPAZ ownership should look as follows:

ASSETS	US$	LIABILITIES	US$
Current Assets	1,606,517	Employee Benefits	99,184
Less Obsolete Inventory*	(400,000)	Shareholders Equity	7,005,624
	1,206,517		
Other Investments	1,607		
Next Fixed Assets	5,896,684		
Total Assets	7,104,808	Total Equity & Libaility	7,104,808

* According to FANVIPLAN's present General Manager, Mr. Gonzalo Urquidi, a large part of the inventory is not saleable and should be written off.

Inasmuch as the GOB has absorbed almost all liabilities, the shareholders equity has increased to a little over seven million U. S. dollars.

CORDEPAZ has indicated that it would be willing to sell the company to private investors for the value of its assets. These may be further written down to US$4 million, according to Mr. Urquidi, supposedly on the basis of a new appraisal. Thus, it is assumed that CORDEPAZ would sell the company for a price somewhere between US$4,000 and US$7,000,000.

The fair market value should be determined, however, on the basis of future earnings streams achievable with a rebuilt oven, improved quality and increased sales. To illustrate the determination of the economic value, certain assumptions have been made which must be verified by means of a thorough feasibility study. In the absence of such a study, the following calculations serve to illustrate the valuation concept only and should not be regarded as valid figures.

The assumptions were:

1. The cost of rebuilding the oven and other improvements will be around US$1,200,000.

2. The total cost of glass per square meter, excluding depreciation, will be US$2.35 at the 40,000 sq. mt monthly production level, US$1.50 at the 70,000 square meters level, US$1.35 at the 95,0000 square meters level.

3. Export will absorbed 20% of the production and domestic sales 80%.

4. The average sales price will be US$2.70 per square meter.

5. Since depreciation is excluded from above costs, the difference tween sales price and cost represent cash flow.

6. Projected sales and cash flow over a 10-year period will be as shown below:

Year	Sales (Sq. Mts)	Cash Flow (US$)
1	480,000	168,000
2	840,000	1,008,000
3	840,000	1,008,000
4	1,140,000	1,539,000
5	1,140,000	1,539,000
6	840,000	1,008,000
7	1,140,000	1,539,000
8	1,140,000	1,539,000
9	1,140,000	1,539,000
10	1,140,000	1,539,000

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The total net cash flow must take into consideration the initial outlay of US$1,200,000 for a plant overhaul plus another overhaul after five years. The net cash flows projected over a 10-year period and their corresponding Net Present Value (NPV) discounted at 20% are determined as shown in the following table. See Case No. 1 to understand the financial concept involved in the NPV approach to evaluating the company.

Year	Cash Flow (US$)	Discount Factor (20%)	NPV (US$)
0	-1,200,000		-1,200,000
1	168,000	0.83	139,440
2	1,008,000	0.69	695,520
3	1,008,000	0.58	584,640
4	1,539,000	0.48	738,720
5	1,539,000	0.40	615,600
6	-192,000*		-192.000
7	1,539,000	0.28	430,920
8	1,539,000	0.23	353,970
9	1,539,000	0.19	292,410
10	1,539,000	0.16	246,240
			2,705,460

* The negative cash flow results from the reconstruction of the oven (which must be rebuilt every 5 years) costing US$1,200,000 less the income from production which has been reduced to 840,000 sq. mt. due to the down time during overhaul

Applying the same reasoning outlined in Case No. 1, a fair offering price from which negotiations between seller and buyer may start may be somewhere around 50% (US$1,350,000) of the net present value of all cash flows produced over a 10-year period. At that price, it would take over 4-1/2 years for an investor to recover his investment of US$2,550,000 (US$1,350,000 for the company, plus US$1,200,000 for the overhaul).

As may be seen, the economic value of FANVIPLAN is considerably lower than the US $4 to $7 million CORDEPAZ expects to receive upon selling the company. The liquidation value is estimated to be even lower, about US$1,035,000. This figure is based on 80% of the current net book value of land, buildings, furniture, tools and vehicles plus 100% of cash, receivables, and investments. The manufacturing equipment, consisting primarily of a glass oven, has no liquidation value.

Inasmuch as the most likely buyer for FANVIPLAN would be one of the neighboring country's glass manufacturers, the gap between the economic value of this enterprise and CORDEPAZ's expected sales price may be bridged through a debt/equity swap. Under this scheme, the investor would buy, at a deep discount, the external bonds of Bolivia held by foreign banks. The GOB would then exchange these bonds at its nominal value for equity of the SOE to be acquired by the investor. Since the bonds were purchased at a deep discount, the investor can afford to pay the full price demanded by CORDEPAZ and still end up with an economically viable investment.

Informal conversations between FANVIPLAN and a Peruvian glass manufacturer indicated some interest in a participation by the latter. The benefit of a sale to another glass manufacturer would be, of course, that the buyer would contribute technology as well as a private sector approach to management. The scheme envisioned by FANVIPLAN would be to raise fresh capital for rebuilding the oven through the sale of a new issue of preferred shares. Such shares would have a guaranteed dividend payable in cash out of the company's earnings or in stock currently owned by CORDEPAZ. This scheme is a modified version of a leveraged buy-out and is worth studying further.

Here again, it is necessary to point out the need for a thorough feasibility study by a professional management team to develop a strategic plan and a business plan from which the economic value of FANVIPLAN can be determined more exactly.

Project Manager - Job Description

The project manager will be a long-term consultant to the INTRAC with reporting responsibilities to USAID/Bolivia. His/her main duties and responsibilities include the following:

* To provide policy, financial, and technical advice on privatization activities to the Director of INTRAC. He/she will assist in: the development of a comprehensive privatization strategy for the GOB; the formulation of privatization action plans for the DDCs and the strategic SOEs; the review of valuation and sales procedures, and the monitoring and reporting of the results of privatization.

* To coordinate the provision of short-term consultants on key aspects of privatization (legal, financial, valuation of assets, sales negotiations, public education). He/She will work closely with the Deputy Director of the INTRAC in supervising and coordinating the technical assistance required to initiate privatization activities.

* To assist in the development of management and operating procedures for the INTRAC, including recommendations on data management, staff responsibilities, and reporting requirements. He/She will aid in the initial preparation of operating procedure manuals, and periodically review them to assure consistency with actual operating practices.

* To serve as liaison between the INTRAC and USAID/Bolivia. He/She will serve as the main communications channel between the INTRAC and USAID/Bolivia, and provide quarterly progress reports to the latter regarding the activities of the INTRAC

The project manager should be a senior professional with private sector management experience, an advanced degree in business or finance, fluency in Spanish, and excellent interpersonal skills. He/She must have a working knowledge of financial markets and mechanisms, valuation procedures, and public administration in Latin America. He/She must also have practical experience with privatization/divestiture activities in Latin America, including the capacity to develop strategies and action plans and supervise their implementation. Finally, he/she should be familiar with the operations and procedures of USAID and other international donors.

Public Affairs Specialist

A senior public affairs/relations professional will be required on a short-term consulting basis for up to twenty-four months. His/her main responsibility will be to assist the INTRAC in designing and implementing a public education/communications program to develop public understanding and support for INTRAC's activities and for privatization generally. He/she will also assist in the establishment and training of personnel of the INTRAC's public education office.

The public affairs specialist should have a Bachelor's Degree, a strong professional background in public relations/public affairs, and fluency in Spanish. He/she should possess a good working knowledge of various forms of communication/public education, including print, radio, television, and seminars. Previous experience in directing public relations/public education campaigns in Latin America would be useful.

Investment/Finance Specialists

Several senior investment/finance specialists are required to assist the LATRAC in brokering the sale of state-owned enterprises. Their main responsibilities will include: preparing a sales prospectus on the SOE; locating potential buyers, analyzing and selecting an appropriate financing mechanism for the acquisition; and negotiating the sale between the buyer and the GOB or DDC.

The investment/finance specialists should have previous high level investment/finance/banking experience. Good negotiating skills and familiarity with the business climate in Latin America would be required. Previous financial and/or industry (agribusiness, light manufacturing) in Latin America would be an asset.

Valuation Experts

Three-person teams of experts will be required -- in most cases -- to value the assets of SOEs and establish a fair selling price. The proposed members of the team and their responsibilities are:

Industry Specialists - Evaluation of the technical process of the plant, quality of production, and suitability of the work force. Identification of production bottlenecks, including operating procedures. Assessment of the condition of manufacturing equipment and machinery.

Marketing Specialists- Evaluation of market potential (domestic and foreign), market size, and market penetration. Assessment of competitors product and market penetration. Analysis of companies distribution system, sales promotion efforts, and pricing policies. consideration of product diversification possibilities.

Economic/Financial Analysts - Analysis of production costs, administrative and overhead costs, and potential for savings. Preparation of cash flow projections. Assessment of working and investment capital needs.

The valuation experts should be non-resident nationals of recognized professional standing. Advanced professional degrees in marketing, accounting, finance, and business administration, and/or substantial industry experience (especially in agribusiness and light industry) are required. Fluency in Spanish is required, and familiarity with Latin American business operations is desirable.