PD-AAU-459

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: 511-0598

4. BUREAU/OFFICE: LAC 05

5. PROJECT TITLE (maximum 40 characters): STRENGTHENING FINANCIAL MARKETS

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

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

A. Initial FY 87 B. Quarter 3 C. Final FY 89

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

A. FUNDING SOURCE	FIRST FY 87 B. FX	C. L/C	D. Total	LIFE OF PROJECT E. FX	F. L/C	G. Total
AID Appropriated Total	750	50	800	5,996	204	6,200
(Grant)	(750)	(50)	(800)	(5,996)	(204)	(6,200)
(Loan)	( )	( )	( )	( )	( )	( )
Other U.S. 1.						
Other U.S. 2.						
Host Country	9,700	300	10,000	26,220	2,423	28,643
Other Donor(s)						
TOTALS	10,450	350	10,800	32,216	2,627	34,843

9. SCHEDULE OF AID FUNDING ($000)

A. APPROPRIATION	B. PRIMARY PURPOSE CODE	C. PRIMARY TECH. CODE 1. Grant	C. 2. Loan	D. OBLIGATIONS TO DATE 1. Grant	D. 2. Loan	E. AMOUNT APPROVED THIS ACTION 1. Grant	E. 2. Loan	F. LIFE OF PROJECT 1. Grant	F. 2. Loan
(1) SDA	840	840		–	–	6,200	–	6,200	–
(2)									
(3)									
(4)									
TOTALS						6,200		6,200	

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

042 | 690 | 819 | 930

11. SECONDARY PURPOSE CODE

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

A. Code							
B. Amount							

13. PROJECT PURPOSE (maximum 480 characters)

To improve the effectiveness of Bolivia's private sector financial institutions and to increase private sector participation in financial sector policy formulation.

14. SCHEDULED EVALUATIONS

Interim MM 10 YY 88 | MM 10 YY 89 | Final MM 04 YY 91

15. SOURCE/ORIGIN OF GOODS AND SERVICES

[X] 000 [X] 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.

Steven G. Liapis
Controller

17. APPROVED BY

Signature

Title: George A. Wachtenheim, Acting Director, USAID/Bolivia

Date Signed: MM 04 DD 14 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)

STRENGTHENING FINANCIAL MARKETS
PROJECT PAPER
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06751

PROJECT AUTHORIZATION

Name of Country: Bolivia

Name of Project: Strengthening Financial Markets

Number of Project: 511-0598

1. Pursuant to Section 106 of the Foreign Assistance Act of 1961, as amended, I hereby authorize the Strengthening Financial Markets Project for Bolivia, involving planned obligations of not to exceed Six Million Two Hundred Thousand United States Dollars (US$6,200,000) 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 AID/OYB allotment process, to help in financing foreign exchange and local currency costs for the Project. The planned life of the Project is four years from the date of initial obligation.

2. The Project ("Project") consists of technical assistance and training to improve the effectiveness of Bolivia's private sector financial institutions and to increase private sector participation in financial sector policy formulation.

3. 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 and in accordance with the waiver included below. 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. Contracting Approvals

The following contracting actions are also approved:

i) A justification for less than full and open competition to contract services from the U.S. Federal Deposit Insurance Corporation (FDIC).

Approved ____________________

Disapproved ____________________

ii) Approval to sign Cooperative Agreements with the Instituto para el Desarrollo de Empresarios y Administradores (IDEA) and The Asociación de Bancos y Instituciones Financieras de Bolivia (ASOBAN) without competition to implement two components of the Project.

Approved ____________________

Disapproved ____________________

iii) A Nationality waiver allowing USAID/Bolivia to include Code 941 country contractors in the competitive contracting process for the provision of technical services to help establish the Financial Training Center and to strengthen the service capability of ASOBAN.

Approved ____________________

Disapproved ____________________

Approved ____________________

Disapproved ____________________

____
Dwight Ink
AA/LAC

Date: ____________________

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List of Abbreviations

A&A	Agribusiness and Artisanry Project
AA/LAC	Assistant Administrator for Latin America and the Caribbean
ACI	International Cooperative Alliance
ATM	Automated teller machine
ASOBAN	Asociacion de Bancos e Instituciones Financieras
BAB	Banco Agricola de Bolivia
BCB	Banco Central de Bolivia
BDIF	Bolivian Deposit Insurance Fund
Bs	Bolivianos (Bs 2 = US$ 1)
CACEN	Caja Central de Ahorro y Prestamo
CBD	Commerce Business Daily
CEP	Confederacion de Empresarios Privados
COLAC	Confederation of Savings and Loan Cooperatives
CRT	Cathode Ray Tube
EOP	End of Project Status
FDIC	Federal Deposit Insurance Corporation
FENACRE	Federacion Nacional de Cooperativas de Ahorro y Credito
FTC	Financial Training Center
FX	Foreign exchange
GDP	Gross Domestic Product
GOB	Government of Bolivia
IBEE	Instituto Boliviano de Estudios Económicos
ICI	Intermediate Credit Institution
IDB	Inter-American Development Bank
IDEA	Instituto para el Desarrollo de Empresarios e Administradores
IISE	Instituto de Investigaciones Socio-Economicos
ILDES	Instituto Latinoamericano de Estudios Socio-Economicos
IMF	International Monetary Fund
IRR	Internal Rate of Return
ISTI	International Science and Technology Institute
LAC/PS	Latin America and Caribbean Private Sector Office
LC	Local currency
LDC	Less Developed Country
LL	Lower Level
MIS	Management information system
ML	Middle level
n/a	Not available
NEC	New Economic Policy
PIO/T	Project Implementation Order / Technical Assistance
PL 480	Public Law 480 Program
p.m.	Person month(s)
PRD	Private Sector and Rural Development Office
ProAg	Project Agreement
SFM	Strengthening Financial Markets Project
SL	Senior level
$B	Pesos Bolivianos ($B 2 - $1)
TA	Technical assistance
Trng	Training
UDAPE	Unidad de Analisis de Politicas Economicas
WOCCU	World Council of Savings and Loan Cooperatives

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LIST OF TABLES

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I. Summary and Recommendations

A. Summary

As a result of the coherent and consistently applied economic policies of the Paz Estenssoro Government, Bolivia's economy has stabilized. The economic reactivation the Government has been seeking, however, is proceeding slower than desired.

One of the most significant hindrances to Bolivia's economic recovery and growth is its poorly functioning financial system. Despite the fact that the financial system is no longer hampered by inflation and ill-founded governmental attempts to interfere with market forces, Bolivia's financial institutions are not adequately fulfilling their basic function of mobilizing and allocating resources for productive economic activities. Unless the performance of the financial system improves, the country's prospects for private-sector-led economic growth will not improve.

Bolivia's financial system is currently suffering from four major problems. The first is the existence of poorly functioning private intermediate credit institutions (ICIs). As a result of the recent hyperinflationary period, the viability of Bolivia's commercial banks is precarious. Loan portfolios have shrunk, and the quality of many loans outstanding is questionable. Overhead costs are excessive in relation to current operations, and levels of paid-in capital are very inadequate. The poor condition of the banks in addition to the perceived risk inherent in the Bolivian economy (reflected in high interest rates on deposits) are responsible for the very high real interest rates on loans, which by themselves are detrimental to expanded economic activity. In addition, ICI personnel too often lack knowledge of rudimentary modern banking practices, and as a result, ICIs do not operate as effectively as they should.

The second problem area affecting the Bolivian financial system is the poor functioning of its public financial institutions. The Central Bank is currently in the midst of a complete reorganization which is seriously affecting its operations. Decisions remain to be made with regard to the proper role, if any, of Bolivia's four state-owned banks.

The third problem affecting the financial system is the lack of adequate financing for medium to long-term credits, whether provided from foreign sources or raised domestically.

Lastly, there is a need within the financial sector for better-informed policies which reflect the highest degree of consensus possible among public and private sector representatives and are based on sound economic analysis.

With the assistance of AID, the World Bank, the Inter-American Development Bank (IDB), and the IMF, the GOB has developed a strategy to address these financial sector problems. Each of these agencies has been asked to provide assistance with different components of an overall program to improve the financial system. Through the Strengthening Financial Markets Project, AID assistance will be focussed on improving the financial status and operations of private ICIs and on fostering private-sector-led policy analysis and research. The purpose of the Project is to improve the effectiveness of Bolivia's private sector financial institutions and to increase private sector participation in financial sector policy formulation. The Project's focus on institution building and policy reform is completely consistent with AID policy concerning financial sector assistance.

The Project will have three components: improvement of financial sector regulation; improvement of private sector ICI operations; and financial sector policy research and analysis.

The first component will support the creation of an independent Bolivian Deposit Insurance Fund (BDIF), whose purpose will be to strengthen weak ICIs in cooperation with the Bolivian Superintendency of Banks, and to insure the public's deposits in these institutions with the resultant increase in domestic depositor confidence in the local banking system.

The second component will include three activities. A Financial Training Center (FTC) will be established under the auspices of the Instituto para el Desarrollo de Empresarios y Administradores (IDEA), which will train ICI officers in all aspects of modern banking operations. The Project will also assist the Association of Banks and Financial Institutions of Bolivia (ASOBAN) to expand the services it offers to its members by supporting the development of a cooperative relationship with a successful banking association from another country. Lastly, under this component, assistance will be provided to help ICIs mobilize domestic deposits and to explore opportunities for the development of new capital market financial instruments.

The third component of the Project will sponsor seminars for the discussion of topical financial sector policy issues among private sector and public sector leaders and finance limited financial sector policy research with a view toward fostering better development, understanding, acceptance, and adoption of well-founded financial sector policies.

AID's contribution to the Project will total $6.2 million in Grant Funds. The GOB and the Bolivian private sector will contribute a total of $28.6 million to Project activities. The summary Project budget is given below:

	AID Grant	GOB	Private Sector	TOTALS
- Bolivian Deposit				
- Insurance Fund	1,368,600	687,500	26,840,600	28,896,700
- Financial Training				
- Center	1,441,500	-	544,000	1,985,500
- ASOBAN Services	393,200	-	312,700	705,900
- Savings Mobilization	722,900	-	70,000	792,900
- Policy Research and				
- Analysis	719,800	-	16,500	736,300
- Other Costs	1,554,000	13,100	159,000	1,726,100
- TOTALS	6,200,000	700,600	27,942,800	34,843,000

B. Recommendations

USAID/Bolivia hereby recommends that the Project be authorized by AA/LAC. In conjunction with the authorization, it is recommended that AA/LAC approve: 1) A justification for less than full and open competition that will allow AID to contract directly with the Federal Deposit Insurance Corporation (FDIC), without competition, to provide technical assistance for the establishment of the BDIF; 2) a waiver of nationality requirements from Code 000 to Code 941 for the provision of technical services to the FTC and ASOBAN; and 3) non-competitive negotiation of cooperative agreements with ASOBAN and IDEA for the implementation of two Project components. The justifications for these actions are contained in Section V.

C. Project Design Team

As noted by the DAEC when it approved the PID for this Project, AID has had relatively little experience with financial sector projects. To ensure that the best and most appropriate project was designed, USAID/Bolivia contracted a consultant team to assist USAID and Bolivian personnel with project design which included individuals with long experience in the Bolivian financial sector and/or pre-eminent experience in their fields of expertise.

The project design team was made up of the following people:

Consultants

Robert Shumway - Deputy to the Director, Federal Deposit Insurance Corporation.

Melville Brown - International Banking Consultant. Formerly Director of the Maryland State Savings and Loan Deposit Insurance Fund, and President or Division Manager in four banks.

Luis Fernando Tobón - Twenty years experience with Citibank including, most recently, Director of Training for Latin America and President of the Banco Internacional de Colombia, a Citibank subsidiary.

Marion Thomson - International Banking Consultant. Formerly Vice President of International Operations, Bank of Montreal.

Robert Vogel - Professor of Economics, University of Miami. Expert in financial markets who has worked in Bolivia frequently during the last six years.

Jerry Ladman - Professor of Economics, Arizona State University and Director of its Center for Latin American Studies. Expert in Rural Financial Markets who has worked frequently in Bolivia during the last ten years.

John Gadway - International Economics Consultant who has worked in Bolivia several times during the last two years. Fields of expertise include rural financial markets, informal financial markets, credit unions and rural savings mobilization.

Onofre Torres - International Banking Consultant. Formerly a top executive in several Latin American branches of Citibank. Has worked in Bolivia several times during the last four years investigating the banking system.

Donald Larsen - Professor of Agriculture Economics, Ohio State University. Has previously worked in Bolivia for the World Bank.

Arthur Warman - Team leader, International Science and Technology Institute, Inc.

Bolivians

Javier Nogales - President of the Central Bank of Bolivia.

Luis Arnal - World Bank Consultant currently assigned to the Central Bank of Bolivia to coordinate donor activities in the financial sector. Formerly Bolivian Representative to the IDB and Subsecretary in the Ministry of Finance.

DIGITEC (Consulting firm composed of experienced Bolivian bankers)
IDEA (Ing. Jorge E. Lonsdale, President, and staff)
ASOBAN (Board of Directors composed of general managers of members banks, and ASOBAN staff)

USAID

Robert J. Asselin, Jr., Chief, Office of Project Development and Implementation
David L. Jessee, Project Manager, USAID/PRD
Clark Joel, Chief Economist, USAID/Bolivia
T. David Johnston, Chief, Office of Private Sector and Rural Development Programs
Steven Liapis, Controller
Luis Montero, Financial Analyst, USAID/CONT
Gail Owens, Financial Analyst, USAID/PRD
Gustavo Vega, Banking Consultant/Financial Analyst, USAID/PRD

II. PROJECT BACKGROUND AND RATIONALE

A. Current Economic Conditions

The misguided and inconsistent economic policies of the Government of Hernán Siles Zuazo between 1982 and 1985 led to a chaotic economic situation by the time Victor Paz Estenssoro was sworn in on August 6, 1985. The incurrence of substantial fiscal deficits fueled by increased current expenditures, an inelastic revenue system and large operating deficits by state enterprises resulted in substantial Central Bank credit expansion and increases in the money supply. The disequilibrium was aggravated by ill-conceived attempts to control prices, interest rates and the official exchange rate.

On taking office, the Paz Government was faced with hyperinflation, a foreign exchange crisis substantially aggravated by the collapse of tin and petroleum prices, a growing debt service problem, a substantial budget deficit, and a real GDP that had declined each year since 1981. The following statistics illustrate the magnitude of the problem that confronted the new Government. The rate of increase of the consumer price index accelerated from 123 percent in 1982 to 276 percent in 1983, 1,281 percent in 1984 and 11,750 percent in 1985. The rate of increase of the budget deficit of the consolidated public sector (a key cause of the hyperinflation) increased from 353 percent in 1983 to 1,964 percent in 1984 and 3,500 percent in 1985. Total net credit extended by the Central Bank to the public sector increased from $b 16 billion in 1981 to $b 2,926 billion in 1984. Net domestic financing covered 81 percent of the overall public sector deficit in 1984. The annual rate of increase of bank credit expansion to the non-financial public sector accelerated from 287 percent in 1983 to 1,166 percent in 1984 and 17,029 percent in 1985. However, credit to the public sector was not the only cause of the increase in money supply as bank credit expansion to the private sector increased at comparable rates during 1984 and 1985. As a result, the supply of currency plus demand deposits (M1) increased at a rate of 1,780 percent in 1984 and 6,137 percent in 1985. M2 (M1 + savings and time deposits) increased at rates comparable to M1 over this period.

Predictably, substantial deficits appeared in the current account of the balance of payments. These rose from US$ 176 million in 1982 to about US$282 million in 1985. The overall balance of payments has been consistently in deficit since 1982, with the balance fluctuating between a negative US$103 million in 1984 and a negative US$ 363 million in 1982.

The Paz Estenssoro Government knew that it had to act quickly and boldly on the economic front to begin to restore public confidence and stabilize the economy. Few people, however, expected the sweeping economic measures enacted in October 1985 under Supreme Decree 21060. The Decree eliminated government controls on prices, interest rates and the official exchange rate; implemented a lower uniform tariff rate on all imports; froze public sector wages and provided for free negotiation of private sector salaries; and decentralized key state enterprises, as a first step in a major effort to reduce the public sector's role in the economy and to stimulate more private investment.

The Government's "New Economic Program" (N.E.P.) which was initiated with Decree 21060 has been highly successful in ending Bolivia's hyperinflation. The rate of increase in the consumer price index was brought down from 11,750 percent in 1985 to 66 percent in 1986 (December to December), and to only 4.5 percent during the last quarter of the year. The rate of increase in the budget deficit of the Central Government was brought down from 3,300 percent in 1985 to an estimated 72 percent in 1986. As a proportion of the GDP, the budget deficit of the consolidated public sector declined from 28 percent in 1984 to 12 percent in 1985, and is estimated at 4 percent for 1986 and 6 percent in 1987. The annual rate of bank credit expansion to the public sector which was 3,891 percent in 1985 became a negative figure in 1986, while the rate of credit expansion to the private sector declined from 4,249 percent to 129 percent. As a result, the rate of increase of the money supply (M1) declined from over 6,100 percent in 1985 to a projected 25 percent in 1986.

The main task that presently confronts the Bolivian authorities is to bring about the reactivation of the economy. The Central Bank's preliminary GDP projections show a decline of about 2.9 percent in real terms in 1986, which is a smaller decrease than in 1985 but still negative. While all indicators point to the fact that the Paz Government has succeeded in setting the basis to arrest and reverse the decline in economic activity, a number of factors have impeded an early recovery. These include a badly functioning financial system, the continued deficits incurred by state-owned enterprises, substantial difficulties faced by the mining industry, the multiplier effects of the sharp drop in export earnings, continuing uncertainty in the private sector regarding the future course of the Bolivian economy, and the slow adjustment of the private sector to the new, free-market-based economic environment established under the N.E.P.

Among the various problems impeding faster economic growth, the poorly functioning and weak financial system is perhaps the most critical. With a poorly functioning financial system, the process of mobilizing and allocating domestic and foreign reserves for productive economic activity in Bolivia is being carried out inefficiently, and business productivity and expansion are suffering. The GOB is counting on the financial sector to help propel the country's recovery by channelling donor-financed credit to the private sector for new investments in the short run, and by mobilizing and allocating more domestic resources for development in the longer run. If measures are not taken to deal with the severely weakened condition of Bolivia's private and public financial institutions, there is a clear possibility for a collapse of the financial system, which would severely compromise all chances for the success of the N.E.P. and the democratic reforms which have accompanied it.

B. The Bolivian Financial Sector

Bolivia's financial sector is made up of a number of public and private sector intermediate credit institutions (ICIs). They include the Central Bank (which is currently responsible for monetary matters, ICI regulation, management of the government's foreign exchange reserves and credit refinancing transactions), four state-owned banks (Vivienda, Minero, Agrícola, and Estado), 17 private commercial banks (13 Bolivian and 4 foreign), three specialized banks, a private savings and loan system with 13 member associations, and about 200 credit unions and cooperatives. These are complemented by five social security systems and sixteen insurance companies. Among the ICIs, the private domestic commercial banks are the most active in lending to both commercial and industrial concerns, and more recently have begun to lend to medium and large-scale farmers. Foreign commercial banks were previously active in these areas but have contracted their operations sharply over the last three years. The savings and loan System, which was severely damaged by the Siles Government's dedollarization policy, concentrates its lending on housing and consumer credit. Both it and Bolivia's cooperatives and credit unions are the most active private financial institutions in rural areas.

Of the four state banks, only the Banco Agrícola (BAB) and the Banco del Estado appear to have a chance to continue operating. The Banco de la Vivienda is bankrupt and can only continue to exist if the GOB decides to privatize it or to channel new foreign loans through it, neither of which appears likely. The Banco Minero's main function has been to facilitate mineral exports, and it has never really functioned as a bank. There is no need for it to continue operating. The World Bank recently recommended that the BAB and the Banco del Estado be merged because they possess branch facilities throughout the country which can serve rural financial markets largely ignored by private banks. This would require the assumption of each bank's poorly performing portfolio by the GOB Treasury and a major reorganization of both institutions. The GOB has still not decided whether to implement the recommended plan, but it is likely that the two banks will not be merged. The Central Bank recently transferred its responsibility for handling public sector accounts to the Banco del Estado, and has now asked the World Bank to re-examine the possibility of continuing to operate both banks separately and to make recommendations regarding the future of the Banco Minero and the Banco de la Vivienda.

The Central Bank is currently undergoing a major reorganization which involves a very significant cut in staff and a complete reshuffling of remaining personnel into fewer operating divisions. This process was initially hampered by personnel disputes and the failure, until just recently, to appoint senior managers within the Bank. The organizational changes have seriously affected the efficiency of the Bank's operations.

C. Current Problems Within the Bolivian Financial System

The chief problems within the Bolivian financial system are institutional in character. Private commercial banks are still suffering from the effects of the recent hyperinflation, and for all practical purposes many of them are technically bankrupt. Similarly, the Central Bank, Bolivia's central monetary authority and regulator of the financial system, and Bolivia's four state banks are currently undergoing profound changes and not carrying out their responsibilities well. Two additional problems affecting the financial sector are the inadequate availability of both domestic and international financing for working capital and new investments and a less than adequate understanding of financial sector policy issues among both private and public sector officials. These four problem areas are explained below.

1. Poorly Functioning Private Banks

A study of the current condition undertaken during the intensive review of most banks revealed that by any normal accounting criterion, most are technically bankrupt. The Bolivian banking system is undercapitalized, inefficient and poorly managed through a series of closely-held, interlocking, family-owned corporations. The system's failure to perform adequately its proper financial intermediation functions constitutes one of the most serious obstacles to Bolivia's economic recovery.*

The evolution of the banking system in the 1960s and 1970s was characterized by steady growth of about 7 percent per year and the emergence of a relatively large number of institutions, primarily engaged in financing commerce. The system's growth in the 1970s was generally satisfactory, as the emergence of medium and long-term credit lines signalled a gradual transition towards a more responsive and sophisticated system. This progressive trend came to an abrupt halt in the early 1980s, however, as the system was hit with a series of negative economic events including:

- two years of record-breaking hyperinflation;
- sharply lower economic activity (GDP contracted by 16 percent from 1981 through 1985);

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* The GOB is also depending on the banking system for the collection of newly instituted income and property taxes which are needed to lower the budget deficit.

- GOB attempts to contain inflation through direct price controls, ceilings and interest rates and maintenance of an overvalued exchange rate; and

- the 1982 "dedollarization" of dollar-denominated deposits and loans, whereby the Government ordered that all accounts be settled in Bolivian pesos at a specified rate.

The costs and benefits of dedollarization and hyperinflation were unevenly distributed. Depositors saw the purchasing power of their savings vanish, while many borrowers were able to repay their debts at a fraction of their original value. It is also believed that many of the bank's owners and directors profited during this period of crisis, using their banking institutions as vehicles to repay dollar debt held by their industrial concerns at a significant savings due to both de dollarization and the artificially subsidized exchange rate, to channel dollars abroad, to obtain loans used for speculative purposes, and to acquire fixed assets within Bolivia.

During this period, the financial system contracted abruptly, as depositors shifted resources into real assets or dollar currency. In December 1981, deposits in the financial system totalled US$725 million. By June 1985, the total had fallen to just US$68 million. By December 1986, total deposits in the commercial banks had again risen to US$290 million, of which 53 percent was denominated in dollars or bolivianos with maintenance of value guaranteed. Commercial bank loans followed a similar pattern, contracting from a level of US$452 million in 1981, to US$165 million in 1985 and recovering to over US$300 million by December 1986.

The Bolivian banking sector was severely affected by this period of extreme economic fluctuation but survived by passing most losses to the accounts of depositors through dedollarization and engaging in a defensive policy of investing in fixed assets (mostly real estate) which increased in nominal value through inflation.

At first glance, Bolivia's banks might appear to be well on the way to recovery. Deposits are expanding rapidly. Loan portfolios have expanded by a factor of three in 18 months. Moreover, real overhead costs have fallen as payrolls have been reduced by an average of 30 percent. On closer examination, however, it is evident that the condition of most banks is precarious. Most banks are undercapitalized. As inflation has subsided, banks are no longer able to book paper profits to offset real portfolio and operating losses. Most financial institutions are currently operating at a loss, due to a combination of excessive payrolls and operating expenses, heavy concentration in valuable but non-earning assets (real estate) and a large number of non-performing loans. High interest rates and the economy's continuing stagnation have caused a dramatic increase in the number of non-performing/past due loans of the banking system. The banks' deposit base is fragile and speculative, and the quality of management is often deficient. A close analysis of the condition of the Bolivian commercial banks as of December 31, 1986 reveals a number of structural and operational problems. These problems are analyzed in depth in Annex A. To summarize:

a. During the recent period of hyperinflation, loan portfolios shrank significantly, overhead costs as a percent of total operating costs and revenue expanded as incomes from loans shrank, and banks invested heavily in real estate as a hedge against inflation.

b. The Central Bank's failure to pay banks' foreign debt at the official exchange rate in accordance with the dedollarization decree has left the banking system with over US$60 million in debt which must be paid off in some way if the system is ever to recover from its current financial problems. In addition to no longer being able to pay off these debts from current earnings, Bolivia's banks no longer have access to foreign loans.

c. Revalued real estate now accounts for over 88 percent of the banking system's capital reserves. This unacceptably high ratio makes all banks very vulnerable during financially troubled periods. The stockholders' actual investment in a number of banks has already been lost several times over.

d. Operating costs currently average 13 percent of total earning assets for the system as a whole. This extraordinarily high ratio contributes directly to Bolivia's high interest rates (See Table 1). There is also evidence that some banks are using deposits to cover operating costs or increasing spreads to cover operating costs by engaging in "uncovered swaps" (financing high interest rate local currency loans with relatively lower interest rate dollar deposits).

e. Loan portfolio quality is very poor. Over 17 percent of the system's loans are classified as non-performing by the banks themselves, and it is likely the real proportion is higher. Banks are lending for very short terms (30 to 90 days) at high interest rates, rolling over loans when due (often capitalizing interest charges), and increasing effective interest rates by charging commissions for each roll-over. It is suspected that a dangerously high proportion of loans are made to borrowers connected with bank owners. Loan loss reserves are inadequate. Customers borrowing in dollars, or with a dollar maintenance-of-value clause, may not be able to repay their loans if the <u>boliviano</u> devalues.

f. Seventy percent of the recent growth in deposits has been in dollars or <u>bolivianos</u> with a dollar maintenance-of-value clause. These deposits are volatile because they are being "bought" with interest rates significantly higher than those paid for dollar deposits internationally. Several banks are engaged in exposed swap transactions to help finance high overhead costs, or conversely (financing dollar loans with <u>boliviano</u> deposits) betting on profitting from significant devaluation of the <u>boliviano</u>.

g. Compared with banks in neighboring countries, Bolivia's banks suffer from serious operational deficiencies. Although a few banks have begun to improve their operations by using technical assistance which was provided under the A&A Project, the financial sector in general is still weak in areas such as: credit analysis techniques; financial marketing; market segmentation; product development, market research,

Table 1

YEARLY INTEREST RATE ON 30-DAY LOANS AS OF 3/26/87 *

	Deposit Rates			Loan Rates		
Bank	$US	Bs**	Bs	Bs**	Bs	Bs
Mercantil	18	14	24	20	18.5	36
Santa Cruz	14	n/a	18	22	n/a	30
La Paz	15	n/a	24	24	n/a	30
Cochabamba	16	14	18	26	26	36
YEARLY INTEREST RATE ON 60 DAY LOANS AS OF 3/26/87						
Mercantil	18	15	n/a	20	18.5	36
Santa Cruz	17	n/a	18	24	n/a	36
La Paz	15	n/a	24	24	n/a	30
Cochabamba	16	n/a	18	26	26	36
YEARLY INTEREST RATE ON 90 DAY LOAN AS OF 3/26/87						
Mercantil	18	n/a	n/a	20	18.5	36
Santa Cruz	n/a	n/a	18	n/a	n/a	n/a
La Paz	n/a	n/a	24	n/a	n/a	n/a
Cochabamba	16	n/a	18	26	26	36

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* "n/a" means "not available"

** With dollar maintenance of value

product profitability mangement; and marketing strategy. Personnel management practices are rudimentary. Modern financial control procedures are not employed. Work processes are time-consuming and expensive. Bank expertise in simple trade finance procedures, foreign exchange transactions and investment banking is almost completely lacking. In short, there is a clear need for Bolivia's banks to train their personnel and modernize their operations if they are to survive as financial intermediaries.

2. Poorly Functioning Public Financial Institutions

The key financial sector functions of Bolivia's public sector, for which the Central Bank has been solely responsible, are monetary regulation, management of the government's foreign exchange reserves, bank regulation, the refinancing of private sector credits, and the management of governmental and state enterprise accounts. Because of problems within the Central Bank, none of these functions is currently being handled as well as it should.

The Central Bank should be providing the framework within which the financial sector operates. During the Siles years, the BCB was thoroughly politicized and, for all practical purposes, ceased to function. Its leftist labor union usurped policy-making authority from the Bank's Board and chief executive officers. When union leaders did not agree with GOB policies the Central Bank was told to implement, they simply closed the Bank. Staffs and payrolls were padded illegally. BCB officials refused to allow audits by the Bolivian Controller General. No monetary controls were imposed, and inflation soared. The politicization of the BCB was one of the principal causes of Bolivia's economic collapse.

Action to deal with the Central Bank's problems began with a major audit which the Controller General was finally able to carry out in 1986. The audit uncovered major operational deficiencies and internal fraud. When the Paz Government came into office, it moved swiftly to deal with the problems identified by the Controller General. A number of key executives/union leaders were thrown into jail, and a competent Board and President were installed.

The World Bank was then asked to make recommendations concerning the restructuring of the Central Bank. It recommended that the Bank be reorganized and concentrate its efforts on monetary management and the purchase and sale of foreign exchange, with a concurrent strengthening of the BCB's Economic Studies Department to support these activities. The World Bank recommended that the bank supervision function currently assigned to the BCB's Departamento de Fiscalización be strengthened and turned into an independent Superintendency of Banks, and similarly, that the BCB's credit refinancing function, currently assigned to the Departamento de Desarrollo, be strengthened and eventually isolated from other Central Bank functions.

As explained in the PID for this Project, the GOB is in the process of transforming the credit refinancing function of the Central Bank into a second story operation under which the Departamento de Desarrollo will no longer approve individual refinancing transactions, but will monitor ICI use of the Government's refinancing facilities. There is also a need to consolidate other GOB refinancing facilities with those of the Central Bank once the Central Bank refinancing operations are revamped. Consideration will eventually be given to the creation of an independent financial corporation to manage all GOB refinancing lines. The Inter-American Development Bank will provide assistance to the BCB in these areas.

While the reorganization of the Central Bank is proceeding more slowly than desired, it is moving forward, and World Bank assistance in the effort is already being provided.

For all practical purposes, there has been no regulation of the banking system during the last several years. Bank reporting to the Central Bank has been very inadequate, and until recently there has been no inspection or supervision of banking activities. Given the profound effect Bolivia's economic conditions have had on the banking system over the past several years, this situation is especially disturbing. Steps have just begun to be taken to reorganize and strengthen the Departamento de Fiscalización, with a view toward molding it into an independent Superintendency. Until a Superintendency can be created again (an act of Congress is required), it is planned that the Departamento de Fiscalización will improve its monitoring of the activities of Bolivia's financial institutions. In addition, audits financed by AID will be carried out under the responsibility of international auditing firms to obtain a more precise picture of the status of Bolivia's banks.

Bolivia's banking law also needs to be revised. The current law was written in 1928, and has been amended so often by decree that it no longer is coherent, nor can it provide a framework for regulation of the financial system. The private banks themselves are aware of the situation, and in an effort to begin the process of drafting a new law more in keeping with the situation in which the financial sector now finds itself, the Association of Bolivian Banks and Financial Institutions (ASOBAN) sponsored a successful workshop in early March which produced a schema for a new law. Action will now be taken jointly by the BCB and ASOBAN to draft a new law which is simple, comprehensive, and more appropriate to Bolivia's present situation based on the schema developed at the workshop. AID will continue to assist in this effort under the Agribusiness and Artisanry Project. A new law is scheduled to be presented to the Bolivian Congress when it reconvenes in August 1987.

3. Insufficient Availability of Medium and Long-Term Credit Financing

Due to the Siles Government's misguided interest rate policies, the refinancing lines previously set up by donors within the BCB for development credits have been largely decapitalized. Since commercial banks do not use their own deposit resources to finance term loans, additional external funds are needed in the short to medium run to finance the levels of fixed and working capital investment necessary to spur economic recovery. In the long run, Bolivia should rely less on external financing and more on internally mobilized savings, both by banks increasing their domestically mobilized deposits and through the development of new capital market instruments.

4. Inadequate Financial Sector Policy Development

The GOB's basic economic policies affecting financial market operations (interest rate flexibility, exchange rate flexibility, controls on credit to the public sector) are sound, and they should provide the basis for the financial sector to perform its proper economic role. However, detailed financial sector policies need to be developed in a systematic and analytically sound manner, and there is a clear need for better analysis of financial sector issues by both private sector and public sector officials so that, as time goes on, a fuller, better-informed dialogue concerning financial sector policy issues can take place which leads to wider acceptance and understanding of financial sector functions and standards. Currently, GOB policy measures are devised by the members of the GOB Economic Stabilization Council (composed of the Ministers of Finance, Planning, Commerce, and Foreign Affairs, and the BCB President) with staff support from the Unidad de Analisis de Políticas Económicas (UDAPE) and the help of outside consultants. Little consultation with the private sector has taken place, and this has led to private sector suspicion and criticism of certain measures being considered by the GOB.

UDAPE will continue to provide economic analyses and recommendations across a wide spectrum for key GOB policy-makers. The World Bank is also developing a balance of payments/financial sector policy loan which will require the GOB to take several financial sector policy measures prior to disbursement of balance of payments assistance. The measures are being analyzed and discussed with the GOB by World Bank consultants. AID and the World Bank collaborated closely in the development of the financial sector policy agenda. Taking these measures will be a significant step in the right direction.

It will also be healthy for the development of the financial sector for its private sector entities and Bolivian academic institutions to participate more fully in the analysis of policy issues and discussions of policy options leading to financial sector decisions. Examples of current financial sector issues which need further analysis and discussion, with private sector participation, include: the setting of deposit and lending rates for various financing needs in response to Central Bank monetary measures; terms and conditions for the management of credit refinancing lines; problems involved with the significant role of the U.S. dollar in the Bolivian economy; bank regulation practices; the drafting of a new banking law; the role of state-owned banks; development of rural financial markets; and capital market development. Other issues will surely arise as time goes on.

D. Recommendations for Dealing with Bolivia's Financial Sector Problems

Over the course of the last several months, with the assistance of outside experts financed by USAID, the World Bank and the IMF, the GOB has developed a strategy for improving Bolivia's financial system. It involves both short-term and long-term actions and will require assistance from several donor agencies to be coordinated by the Central Bank. The measures to be taken in the short term (during the next year) are as follows:

1. Bank Audits

Instructions for the annual year-end audits commissioned by all Bolivian banks, both public and private, were modified to place more emphasis on an examination of portfolio quality and recent bank operations. This audit is due April 30, 1987. It will be followed by a second audit, covering the six-month period ending June 30, 1987, commissioned by the Central Bank with partial AID financing and to be carried out by international auditing firms. The purpose of the second audit is to provide the GOB with accurate data on the status of all banks which it will use as a basis for fomulating instructions to individual banks from the BCB Departamento de Fiscalización for corrective actions and for making final decisions on the future of Bolivia's state-owned banks.

2. Creation of the Superintendencia de Bancos and a Deposit Insurance Corporation

Working cooperatively, these two autonomous organizations will implement various measures to strengthen and consolidate the country's private banks. The Superintendencia will devise, and ensure bank conformance with, bank regulations while the Deposit Insurance Corporation will be empowered to take a variety of measures to deal with bank solvency problems and insure the safety of the public's deposits in private financial institutions.

3. Revision of the Banking Law

A new banking law will be drafted with consultant assistance financed under the A&A Project and enacted by the Bolivian Congress to provide a framework for the regulation and growth of the country's financial sector.

4. Negotiation Between the BCB and Private Banks of Disputed Foreign Debt

A compromise of some sort will have to be negotiated to allow for the payment (or renegotiation) of outstanding private bank debt to foreign creditors. There are valid arguments on both the side of the GOB and that of the private banks which would support a negotiated settlement to the bank debt problem, which must be addressed if the Bolivian banking system is to regain financial stability and access to foreign credits.

5. Reorganization of the Central Bank

As noted above, the reorganization and strengthening of Bolivia's main financial institution, without which financial sector strengthening will not be possible, has begun with World Bank assistance.

6. Closing/Reorganization of Bolivia's State-Owned Banks

The Banco de la Vivienda and the Banco Minero should be closed, and the BAB and Banco del Estado should be reorganized. Decisions with regard to the future of these banks should be made by September 1987.

7. Provision of Credit Financing

Assistance in the short to medium term in reestablishing credit refinancing facilities will come from the IDB ($120 million agriculture and agribusiness loan) and USAID (PL480 Title III-financed local currency credits and the Market Town Capital Formation Project, in addition to continued use of refinancing facilities already established).

Measures designed to have a favorable impact on the financial sector in the medium to long term include:

a. Establishment of a Financial Training Center The Center will be established within the Instituto para el Desarrollo de Empresarios y Administradores (IDEA) to train ICI personnel in all aspects of modern banking.

b. Redesign and Improvement of the BCB's Credit Refinancing Functions As noted above, the IDB will take the lead in assisting with the reorganization of credit refinancing transactions, which will continue to be required in the foreseeable future.

c. Improvement of ASOBAN Services Currently, ASOBAN serves primarily a lobbying function for Bolivia's private financial institutions (banks and S&Ls). It will gradually be equipped to provide a variety of services to its members, all designed to improve their operations.

d. Improved Financial Sector Policy Analysis and Research UDAPE will continue its assistance to the GOB Economic Stabilization Council in the analysis of financial/economic policy options. The World Bank will help improve the BCB's Economic Studies Department. USAID will also assist private sector entities (the Catholic University, etc.) to sponsor seminars and research on topical financial sector issues, with a view toward engendering better understanding of, and agreement on, financial sector policies.

e. Savings Mobilization Programs As economic conditions improve and financial institutions take important initial steps to strengthen their own financial stability, the prospects for increased internal savings mobilization should improve. The Strengthening Financial Markets Project will provide assistance in this area.*

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* Assistance is already being provided to the Savings and Loan System under another AID project.

f. Creation of New Capital Market Instruments As financial and economic conditions improve, assistance will be provided by AID to investigate the feasibility of creating GOB treasury securities, corporate debt instruments and other capital market instruments.

E. Project Strategy

In February 1987, the Mission contracted the International Science and Technology Institute (ISTI) to carry out an extensive assessment of USAID's private sector assistance strategy. This study is available in LAC/PS. As a result of the study, USAID reformulated its private sector assistance 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.

Without a concerted effort to address Bolivia's serious financial sector problems, economic reactivation will be seriously hampered even with the most coherent policy framework. The SFM Project will form part of a comprehensive multi-donor effort to help the GOB and Bolivia's financial sector institutions address the full range of financial sector problems outlined in the prior section. USAID/Bolivia, World Bank, IMF and IDB representatives have met regularly with GOB officials, principally in the Central Bank, during the last several months. There is full agreement among the donors and the GOB on the key problems within the financial sector and what needs to be done to address them. The shared goal of each donor's assistance efforts will be to improve the Bolivian financial sector's financial intermediation performance. Each donor has selected components of the overall effort on which to concentrate. Parallel, rather than co-financed, activities will be financed by each donor, in a closely coordinated fashion. The implementation of the SFM Project will not require any specific actions to be undertaken under other donors' projects, but the full success of the GOB's plan to rehabilitate the financial sector will require all of the assistance the GOB has requested.

The SFM Project will focus on the improvement of private sector financial institutions and their participation in financial sector policy decisions.

The World Bank is planning two loan projects as part of its effort to improve the financial sector. The first, the "Financial Sector Structural Adjustment" Loan, will require as pre-conditions for disbursement a number of policy adjustments by GOB. The other, "Bolivian Public Financial Management Operations," will finance technical assistance for the reorganization of the BCB, improvement of its internal procedures and controls, reactivation of Superintendencia de Bancos, improvement of the BCB's Economic Studies Department, and reorganization of the BAB and the Banco del Estado.*

A new IDB loan, which was approved by the IDB Board on November 12 1986, will provide credit financing for agricultural production and agro-industry, as well as finance technical assistance for the reorganization of the Departamento de Desarrollo.

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* This loan will also provide assistance for the organization of the Ministry of Taxation and a complete revamping of the financial control procedures of the GOB. (USAID assistance is also being provided in the latter area.)

The IMF will continue to provide advice to the GOB in the areas of monetary and fiscal policy, and cooperate with other donors, as appropriate, in the provision of assistance in related areas, such as revision of the banking law, financial sector policy analysis and improvement of the BCB Economic Studies Department. This process has already begun with the signing of an agreement for a three-year arrangement under the Structural Adjustment Facility which calls for GOB action on several fronts, including the financial sector, and with a planned IMF staff review of a scheme for a new banking law prepared by ASOBAN.

Table 2 below shows the areas to be covered by USAID, the World Bank, the IDB and the IMF.

TABLE 2

DONOR ACTIVITIES IN THE FINANCIAL SECTOR

Component	AID	WB	IDB	IMF
Bank Audits	x			
Superintendency of Banks		x		
Deposit Insurance Corporation	x			
Banking Law	x			x
BCB Reorganization		x		
State Bank Reorganization		x		
Credit Financing	x		x	
Financial Training Center	x			
Overhaul of Credit Refinancing Facilities			x	
ASOBAN Services	x			
Financial Sector Policy Research and Analysis	x	x		x
Savings Mobilization	x			
New Financial Instruments	x			x

Coordination of assistance efforts will be the responsibility of the Central Bank. This process will be facilitated by quarterly financial sector assistance meetings chaired by the President of the Central Bank which will be attended by the USAID Director, the World Bank and IMF Resident Representatives, and appropriate project personnel (staff, consultants, and GOB officials).

F. Conformance with Host Country and AID Priorities

The SFM Project is in full conformance with both Bolivian and AID priorities. There is general recognition within the Bolivian private sector and by the Paz Government that market-based, private-sector-led recovery cannot occur in a timely fashion without a better functioning financial sector. The GOB sees improvement of financial sector operations as one of its highest economic priorities, and has requested AID, World Bank, IDB and IMF assistance in the effort.

The SFM Project fits well with in USAID/Bolivia's assistance strategy. It will directly support the Mission's prime program objective: promoting private-sector-led economic recovery. Economic recovery is key to the attainment of USAID/Bolivia's other two program objectives: sustaining democracy and assisting with coca control efforts. The SFM Project will also complement other AID-sponsored efforts under the Market Town Capital Formation, Industrial Transition, Housing Guarantee, and Policy Reform projects, as well as the PL 480 Title III Program.

The Project is in full conformance with AID policy directives, specifically those contained in the draft AID Policy Paper on Financial Markets Development. The Project conforms with basic AID policy on assistance to the financial sector, which has been summarized as follows: "A.I.D. supports LDC efforts to develop financial markets by assisting them to build strong, resilient, and durable financial institutions; encouraging them to adopt the policies conducive to the growth and viability of these institutions; and helping them to eliminate the deficiencies in the types of credit available that are impeding the growth of their private enterprises."*

In addition, the Project will be carried out in line with guidance on the importance of coordinating assistance efforts with other donors: "Missions should coordinate their efforts to help the LDCs solve their development finance problems with those of .... multilateral agencies and other bilateral donors so that our efforts are mutually reinforcing." **

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* Draft Policy Paper on Financial Markets Development, p. 6

** Ibid, p. 8

III. PROJECT DESCRIPTION

A. Goal and Purpose

The goal of this four-year Project will be to improve the performance of Bolivia's financial sector. The chief indicators of the achievement of the Project's goal will be:

- Improved financial sector policies
- Better regulated ICIs
- A better functioning Central Bank
- Better functioning ICIs
- An increase in the volume of domestic savings deposited in Bolivian financial institutions and invested in new financial instruments
- Increased term lending to private sector farms and other businesses

The purpose of the SFM Project will be to improve the effectiveness of Bolivia's private sector financial institutions, and to increase private sector participation in financial sector policy formulation. The chief indicators of the achievement of the Project's purpose will be: improved ICI loan analysis and monitoring, more ICI deposits, more efficient ICI operations, wider ICI operations, larger loan portfolios, closer adherence to bank regulations and sound banking practices, regular and accurate ICI audits, a functioning Deposit Insurance Fund, a stronger ASOBAN, a functioning Financial Training Center, and the existence of regular analysis and discussions of financial sector policy issues by public and private sector leaders.

B. Project Components

The SFM Project will have three components:

- Improvement of Financial Sector Regulation. Under this component, AID will assist with the establishment of the Bolivian Deposit Insurance Fund (BDIF), following completion of external audits of banks and revision of the banking law. Related World Bank assistance is being provided to reorganize the Central Bank and establish the Superintendencia de Bancos.

- Improvement of Private Sector ICI Operations. This will include establishment of a Financial Training Center, expansion of ASOBAN services, and savings mobilization efforts.

- Improvement of Financial Sector Policy Research and Analysis. This will include private-sector-led financial sector research and seminars, also involving public sector officials.

1. Improvement of Financial Sector Regulation ($1.4 million AID; $26.8 million Bolivia)

The objective of this Project component will be to improve the regulation of financial institutions operating in Bolivia so that they can more effectively and rationally serve the country's economy. The key activity under this component will be the establishment of the BDIF.

Funding will also be provided to help finance the cost of external audits of 21 private and public banks which will be carried out in June and July 1987 prior to the establishment of the BDIF and the Superintendencia de Bancos. The audits are estimated to cost $750,000, of which - subject to the availability of funds - AID will finance 75 percent, or $562,500. Partial funding has already been reserved for the audits under the Agribusiness and Artisanry Project in the amount of $320,000. An additional $187,500 will be required under this Project*. The audits will be contracted by the Central Bank with several international auditing companies. The Request for Proposals for these audits was issued in March, and contracts are scheduled to be signed in May.

a. Purposes of the BDIF

The establishment of a deposit insurance fund within a country's financial system is neither a new nor a unique concept. Many countries have such insurance schemes for their deposit-gathering institutions. It is recognized, however, that most financial systems which incorporate a deposit insurance fund are well-established, stable and well-regulated. In these systems, the deposit insurance fund acts as an additional support vehicle to reinforce depositors' confidence in the financial system.

In the case of the Bolivian financial system, as a result of the effects of recent economic policies, and an almost total lack of regulation, a serious, system-wide situation of poorly performing, and in some cases insolvent, financial institutions exists. Consequently, the creation of a Bolivian Deposit Insurance Fund will have as its primary objective the establishment of an independent, well-managed vehicle for the early intervention, support, and management of weak or failing financial institutions. The philosophy of the BDIF will be to take whatever financial or managerial actions are necessary, and at the earliest stage possible, consistent with avoiding unjustly rewarding the

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* No formal or informal commitment has been made to provide these additional funds. If they are not authorized, the Central Bank will finance the remaining cost of the audits.

bank's stockholders, to prevent the failure of member institutions, and thereby to avoid the more costly and detrimental ultimate solution of bank liquidations. The reassurance that such an insurance fund will provide to depositors is important to the long-term stability of the financial system and restoration of confidence by depositors in the system, but is considered at this stage to be a secondary benefit.

The BDIF will reinforce and support the efforts of the Superintendency of Banks to rehabilitate and maintain the Bolivian banking system in a safe and sound operating condition. The Fund will be able to employ a wider variety of measures to deal with ICI financial problems than will the Superintendency.. Whereas the focus of the Superintendency will be on bank "regulation", that of the Fund will be on bank "rehabilitation" and assistance. As described below, the BDIF and Superintendency of Banks, although organized as two separate and independent agencies, will, in fact, operate in close coordination. The GOB sees the establishment of both entities as critical to its overall financial sector restructuring program. There is also support among the private banks for these plans.

b. Organization of the BDIF

It is essential that the BDIF operate as an independent entity with a small, skilled and respected staff. The independence of this entity is of primary importance to avoid future politization or undue influence by the Administration, Congress, and the banks themselves. The small size is considered necessary to avoid the Fund's becoming too unwieldly or bureaucratic in its operations. The BDIF will be organized as a public corporation so as to have the flexibility of an independent corporation while simultaneously operating in the public interest. In this manner, the Fund will have the greatest latitude for operation while maintaining its necessarily close link with the Central Bank and the Superintendecy of Banks. It will be legally created under the new Bolivian banking law, if a law can be passed by September 1987 by the Bolivian Congress, or by Supreme Decree pending passage of a new banking law.

The Board of Directors of the BDIF will appoint the Fund Director and will act with the full authority of a normal corporate board of directors as regards the operations of the Fund.

The Board of Directors will consist of both public officials and private sector individuals, with public members always having an absolute voting majority. The Board will consist of at least five persons. The Chairman should be either the Superintendent or Assistant Superintendent of Banks. Two additional public members will come from the Board of the Central Bank. Members from the private sector will be appointed for a specific term and serve in an individual capacity. They will not include active officers from member financial institutions. It is imperative that the membership of the Board not deteriorate into an "insider trade association." Private sector membership should come from well-respected persons, preferably with prior financial experience.

The staff requirements of the BDIF reflect the financial, technical and managerial functions that the Fund will perform. The BDIF will require the following staff:

> Fund Director/Chief Executive Officer. The Fund Director must be a person of impeccable reputation and thoroughly knowledgeable and experienced in bank operations, bank regulation and supervision, financial accounting, and asset management.

- Controller. This person, along with an accounting assistant, will be needed to calculate assessments, send statements to banks, and make certain the statements are paid properly. The Controller will also be responsible for investing Fund reserves and maintaining corporate records.

- Financial Analysts. The initial organization of the BDIF will require the assistance of at least one senior financial analyst/asset manager and two to four additional financial analysts to be available for special projects and management assistance within member institutions. They must be well acquainted with the various procedures for intervening banks, which will require short-term training in other countries with established insurance funds.

- Legal Counsel. It is anticipated that the work of the BDIF will require a full-time corporate attorney.

- Administrative support. Initially, the Fund will require the administrative support of at least two secretaries.

c. <u>BDIF Authorities</u>

The BDIF will be empowered to undertake a wide range of activities in order to rehabilitate member institutions. It is necessary that the powers and authorities of the BDIF be broad so that the Fund can operate quickly and efficiently, unencumbered by the narrow boundaries currently hindering some actions by the Central Bank.

The BDIF will have authority to provide quick assistance and support in a variety of forms (e.g. purchase capital instruments; grant loans to, or place deposits with, institutions to support liquidity needs; issue guarantees or promissory notes; and directly purchase troubled loans) in order to intervene and support an institution in the most efficient and least costly manner.

The BDIF will have the authority to establish an assessment rate for insurance premiums within a reasonable range. The Fund will also have the authority to collect assessments from institutions which are in arrears.

The BDIF will have the authority to establish criteria for membership in the Fund, be able to approve or disapprove applications from new members, and have the authority to define "deposits" for the purpose of establishing deposit insurance limits within each financial institution. This latter definition is also important for the exact determination of the assessment level for each member institution and for the collection of annual insurance premiums.

The BDIF will be empowered to obtain any financial information from insured institutions that may be required. The BDIF will have access to all financial information, reports, external audits, and examinations conducted by the Superintendency of Banks. Additionally the BDIF will have the authority to hire external auditors at the expense of member institutions whenever deemed necessary. It is also considered important that the BDIF and the Superintendency of Banks have the joint authority to require financial institutions to disclose certain basic financial information periodically to the public.

The BDIF will have parallel authority, along with the Superintendency of Banks, to enforce established regulations, require financial institutions to conform to sound financial standards, and to issue cease and desist orders when deemed necessary. The BDIF also will have the authority to terminate membership in the Fund when appropriate. The authority of the BDIF should clearly establish that the Fund will always be the appointed receiver for a failed member financial institution.

The BDIF as an independent agency will have all rights and powers generally associated with a Bolivian corporation which will include the ability to invest all funds received, either through capital contributions, loans or insurance premiums, in whatever manner it deems most appropriate. As will be discussed below, the investment of the funds received by the BDIF must be in conservative and liquid investments.

d. Participation in BDIF

Initially, the Bolivian Deposit Insurance Fund will cover deposits in all privately owned Bolivian commercial banks. However, the Fund should be organized to be able to accept new member ICIs from other sectors of the Bolivian financial system in the future. There is considerable interest in the creation of such a Fund among both the savings and loan associations and the credit cooperatives within the country. However, both systems present unique problems as well as operating practices which distinguish them from banks. Special regulations and eligibility requirements will have to be designed to incorporate these financial institutions into the Fund.

The inclusion of the state-owned banks and foreign banks is also not considered appropriate at this time. The GOB is considering reorganizing, closing or privatizing a number of state-owned banks, and moreover, several currently do not accept deposits. When the GOB decides what to do with the state banks, some may be eligible for consideration for membership in the BDIF. The Bolivian branches of foreign banks are mostly inactive at this time, but could be considered for membership later.

It is most desirable that the deposit insurance function be consolidated and totally integrated within the financial system of Bolivia. There is no need, and it would be economically and administratively unwieldy, to have separate insurance funds for each segment of the financial system. It is envisioned that after the initial period of the Fund's operations (two to three years), new members from either the savings and loan associations or reorganized state banks could be admitted. Such expansion would require necessary adjustments in the policies and procedures of the Fund as well as increased staff.

e. Eligibility for Membership

Ideally, the BDIF would be created within a strong and stable financial system which would allow the Fund to establish firm prerequisites for admission. However, it is again noted that the Bolivian financial system is in a weakened condition with a variety of structural and organizational problems which affect most potential members to varying degrees. Consequently, it is difficult beforehand to establish hard and fast eligibility requirements for membership in the new deposit insurance scheme.

The initial catalyst for applying basic regulatory rules and eligibility requirements for admission into the BDIF will be the in-depth audits of the private banks to be completed by July of this year. The results of these audits will give a clear-cut indication of the depth and complexity of the problems within the Bolivian banking sector. From these, the Central Bank, through its strengthened Departamento de Fiscalización, will advise each bank of its major weaknesses and of the corrective actions that will be required.

Minimum eligibility requirements for membership in the BDIF will be at least those levels of management, capitalization, earnings performance, asset condition and correct accounting procedures required by the Superintendency of Banks. While it is not yet possible to fix specific criteria for each item, eligibility requirements will address the following basic areas:

. Capital The applicant institution must meet the minimum capital guidelines established by the Superintendency of Banks. Actual composition of the capital account as regards minimum levels of paid-in capital from shareholders will be determined.

. Financial condition The applicant institution's overall financial condition, taking into consideration such factors as asset quality, diversification of portfolio, loan performance, amount and valuation of fixed assets and asset/liability management, must be within the Superintendency's guidelines and considered satisfactory for the health of the Fund.

. Earnings The financial institution must be able to demonstrate the ability to operate in a sound and profitable manner. Actual profits or losses for preceding periods will be considered, as well as the ability of the bank to operate profitably in the future without major intervention or financial support from the Fund.

. Management The quality and overall depth and ability of an institution's management must be satisfactory to both the Superintendency and the Fund.

It is recognized that many of the problems confronting the Bolivian banking system will not be quickly or easily resolved. Many of the problems are structural in nature and will require time to be corrected, and then only with the full cooperation of the Central Bank through its monetary policies, and with the support of the Superintendency and the BDIF itself. Therefore, it is not considered practical to require that each bank completely resolve all its problems prior to admission to the Fund. Neither will it be possible for the coordinated effort to strengthen the banking system to be successful if any of the private banks remains outside the BDIF. Consequently, all of the private banks will be strongly "encouraged" to join the BDIF by the use of incentives and disincentives. These will include announcement by the Central Bank that banks not belonging will lose access to BCB refinancing lines and short-term liquidity loans. The GOB has also indicated its willingness to announce that it will only stand behind deposits in member institutions, if it is necessary to do so. Several bankers feel that for competitive reasons once a few banks join the Fund, all will wish to join.

Once a financial institution is a member of the BDIF, it will receive the supervision and support to be provided by the Fund. Member institutions will be required to move toward total compliance with the established performance criteria and will be allowed a reasonable time period to do so. If a member institution should fail to meet the minimum eligibility requirements and regulatory and performance criteria within a reasonable period, the Fund will begin intervention measures.

f. Bank Intervention and Support Mechanisms

A primary role of the Deposit Insurance Fund will be to provide financial and management support to troubled financial institutions. The role of the BDIF as an intervener of a member institution should not be considered totally a punitive action. If done early enough and accomplished professionally, BDIF involvement can be both corrective and preventive. There are a number of levels of involvement and degrees of intervention which the BDIF can employ, ranging from support for a liquidity problem to total liquidation of a failed bank.

It is usually the case that when a bank demonstrates persistent or recurring liquidity problems, these problems are actually symptomatic of a deeper problem of bank solvency. The lack of liquidity is often, in reality, the result of the poor quality of a loan portfolio and the high incidence of non-performing loans. Less often, liquidity problems are a result of a mismatch in the terms of a bank's liabilities and assets. In either case, failure to take corrective actions when such problems are first identified can severely jeopardize the capital of the institution.

Once problems of liquidity, capital adequacy or profitability in a member institution are identified, the Fund will have the capacity to take prompt corrective action through a variety of mechanisms. Emphasizing again that early support and intervention are the best policy, the Fund will be able to become involved in a troubled financial institution through the following steps.

The Fund could, depending on the problem identified, assist the financial institution through the purchase of non-performing assets, the placing of deposit funds for liquidity support or direct involvement of BDIF personnel in management decisions. The Fund will always keep in mind, however, that actions taken, or financial risks assumed, should be for the ultimate benefit of depositors and should not inordinately reward existing shareholders.

Depending on the severity of the problems identified, the BDIF could take stronger corrective actions and provide more financial assistance. If the Fund determines that a significant injection of new capital is required to properly address the problems identified and to rehabilitate a financial institution, it will have the authority to require existing shareholders to make such an investment. If this request is not obeyed, the Fund will have the power to cancel the institutions' membership in the Fund, to temporarily replace existing management, and/or to subordinate the position of existing shareholders to the financial investment of the Fund.

If corrective actions such as those outlined above have proven futile, the Fund will have the ability to attempt to merge or sell a failed financial institution to another member institution or to third party private investors, with the financial support for such a purchase available from Fund or Central Bank resources.

The Fund will have the ability to provide financial support to an acquiring bank or investor group by either purchasing non-acceptable and troubled loans or providing some form of long-term capital support for the new institution. Any such merger or sale transaction shall have as its primary goal the prompt reopening of the bank and complete access to funds by all depositors. The employment of this merger or acquisition technique will only be considered as long as its overall costs are found to be less than the actual liquidation of an institution.

g. Deposit Insurance Coverage

Deposit insurance funds set a coverage limit per depositor in order to limit their liability. This limit is set to protect the majority of depositors. Very large deposits are usually excluded, but all small and medium-sized deposits from the general public should be covered.

Only real deposits can be insured. For example, the Fund will not insure inter-bank loans or funds on deposit temporarily from refinancing entities. In order to determine coverage limits, it will be necessary to analyze the deposit structure in the institutions whose deposits are to be insured. Due to a lack of data on the structure of deposits in Bolivia's commercial banks, it has not yet been possible to determine what the deposit coverage limit should be. It is felt, however, that a limit of Bs20,000 per depositor should cover the majority of depositors.

Before the Fund begins operations, a thorough study of the deposit structure of commercial banks will be made, and an insurance limit will be set. This study will also enable the Fund to define "deposits" for the purpose of setting insurance premiums. It is important to realize that deposit insurance limits can be increased over time if increases are supportable by corresponding increases in the average deposit level within the system. However, once a limit is established, it will be politically impossible to lower it.

h. Insurance Premiums and Capitalization of the Fund

The Bolivian Deposit Insurance Fund will function as a self-insurance system and will be funded by its member financial institutions by means of semi-annual insurance premium payments calculated as a percentage of the members' total deposits. Initially, the Fund will receive a working capital loan of at least $500,000 from the Central Bank. This loan will provide necessary working capital and resources for the Fund until income from membership premiums and interest on investments allow the Fund to operate in a self-sustaining manner. It is important to realize that while the Fund will be able to finance its normal operating costs and will have sufficient reserves to undertake a variety of financial intervention techniques, it may not have sufficient resources to pay off all insurance claims to depositors in the case of a major bank failure or a series of failures during its initial years of operation. Consequently, the Central Bank, which will continue to carry the ultimate responsibility for the soundness of the financial system, has agreed either to absorb the cost of 50 percent of any bank intervention actions during the first three years — or, if necessary, the first five years — of the Funds existence,* or to provide a more substantial, long-term loan (e.g. $3,000,000) for initial capitalization.

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* If more than 50 percent of the cost of any liquidation is required during the Fund's early operations, the BCB will finance the portion above 50 percent on a loan basis until insurance premiums accumulate adequately to repay the loan.

The BDIF will also have access to additional working capital loan, as necessary, from the BCB, to carry out intervention actions in a timely manner.

The deposit insurance charge will be 2 percent of the projected year-end level of deposits covered. This fee will be payable semi-annually, beginning in June 1988 (six months after the Fund begins operating). The 2 percent premium will be maintained for as long as necessary and possible to capitalize the Fund and then reduced gradually. An initiation fee, averaging $10,000 per bank will also be charged when the Fund begins operating in December 1987. This fee will be subtracted from the June 1988 assessments.

It is essential that the BDIF invest its surplus cash in sound, liquid instruments. The Fund must preserve the value of its reserve funds while seeking a reasonable investment return. Since currently there does not exist any type of treasury instrument in Bolivia, and because it would not be proper to invest a large amount of insurance reserves in a member financial institution, the BDIF will have the authority to invest its reserves in US dollar instruments offshore, and will do so. The original loan from the Central Bank will be in dollars. The assessments from the member institutions will be received in either bolivianos or dollars. Local currency will be used first for operating expenses. Remaining funds will be converted to dollars and invested offshore.

i. EOPs and Project Inputs

The activities to be carried out under this component are intended to result in the establishment of a viable, functioning Bolivian Deposit Insurance Fund. The actions of the Fund will be essential to the strengthening of Bolivia's private financial institutions. A variety of measures will be taken to improve the financial status of these banks. Working together with the Superintendencia, the Fund will help ensure that sound banking practices are followed and that financial institutions' operations are of benefit to the business community and the general public. Lastly, the activities of the Fund will help increase public confidence in the financial system and the safety of deposits mobilized.

To establish the Fund, the following Project inputs will be provided:

Technical Assistance - 24 p.m. long-term, 24 p.m. short term ($1,032,100).
Bank Audits (21) - ($750,000) (75 percent AID; 25 percent BCB)
Capital Contributions- $26.0 million, to be financed from insurance fees charged to banks, and a $500,000 loan from the Central Bank.
Training - 6 short-term visits to FDIC and 3 trips to superintendencies, in Latin America ($54,000) (AID).
Commodities - Computers, furniture and office equipment ($40,000) (AID).
Operating Costs - ($1,300,000) (to be financed from insurance fees charged to banks).

USAID/Bolivia made a special effort to obtain the help of the Federal Deposit Insurance Corporation (FDIC) to investigate the feasibility and design the BDIF component of this Project. This was done because of the FDIC's pre-eminence world-wide in the field of deposit insurance and because the Mission desired to foster a collaborative relationship between the FDIC and the BDIF which could continue during, and after, Project implementation.

The FDIC is prepared to continue providing assistance to the Project, and USAID/Bolivia hereby proposes that a justification for less than full and open competition be approved in conjunction with the authorization of this Project to allow the contracting of technical assistance and training for this component from the FDIC without competition. The basis for the waiver of competition is unique capability. Services could conceivably be provided from a commercial company with access to ex-FDIC employees or a foreign deposit insurance agency. Very few firms would be able to provide ex-FDIC employees, however, and such an arrangement would not provide the inter-institutional relationship the BDIF will require. Under the other alternative, AID grant funds would have to be used to finance services from outside the U.S.

The FDIC will provide a long-term resident advisor (two years) and eight short-term advisors (3 months each) who will assist the BDIF in the areas of designing procedures for the Funds operations (incorporated in by-laws, manuals, etc.), training in bank intervention methods, management of acquired bank assets, assessment and management of insurance premium payments, management of the Fund's reserves, and bank inspection and reporting procedures. The FDIC will also arrange for six short-term visits by BDIF personnel to FDIC facilities in the United States or Puerto Rico for training in intervention mechanisms, financial analysis and insurance fund operations, and three trips to other Latin American countries to discuss bank regulation issues with banking officials.

Conterpart contributions will finance 25 percent of bank audit costs, and 100 percent of the BDIF's operating costs and BDIF capitalization.

B.

2. Improvement of Private Sector ICI Operations

This Project component will finance activities to help existing private sector intermediate credit institutions (commercial banks, credit unions and, to a lesser extent, savings and loan associations) to survive in the new Bolivian economic environment and better meet the private sector's financing needs. The three subcomponents to be implemented are (a) the establishment of a Financial Training Center, (b) the strengthening of ASOBAN, and (c) improvement of domestic savings mobilization.

a. Financial Training Center ($1.4 million AID; $544,000 Bolivia)

1) Objectives

The prevailing weaknesses in Bolivian financial institutions are recognized as having resulted from the inappropriate policies of the former Government and the destabilization resulting from these policies. However, the poor managerial practices of these institutions have also significantly affected their financial condition and performance. Poorly trained professional staff in the banks has meant that sound credit policies and procedures, modern marketing techniques, financial controls and effective management information systems are only sporadically employed in the Bolivian financial system.

To help ensure an effective and viable role for Bolivian financial institutions in the country's economic reactivation, this component will strengthen ICI managerial and technical capabilities. To this end, a Financial Training Center (FTC) will be established to provide training at three different mangement levels in credit analysis and management, marketing, management of human resources, financial control, management information systems, trade finance, and the like.

The FTC will be a semi-autonomous division of the Instituto para el Desarrollo de Empresarios y Administradores (IDEA) which USAID helped to establish under the auspices of the Bolivian Confederation of Private Businessmen (CEP) to provide private sector management training. A training advisory board for the FTC will be established to assist in overall direction of the Center, whose members will be drawn from ASOBAN.

The FTC will have the following three main objectives:

- identification of specific training needs of private financial sector institutions;
- design, development and delivery of short-term training courses and workshops; and
- selection, development and training of local instructors, thereby ensuring continued relevance of course design and delivery of training programs.

2) Course Content

As reported in the Technical Analysis Section of this Paper, an assessment of ICI personnel training needs carried out for this Project revealed that training is required in the following subject areas: credit assessment and management, financial services marketing, human resources management, financial control, trade finance, bank operations, treasury management, and strategic planning.

Over the three-year life of the subcomponent, the FTC will undertake a total of 68 seminars which are projected to train 1,300 participants from commercial banks and other ICIs operating in Bolivia. Seminars are to be offered in the following topics under each of the Center's main subject areas:

Table 3

Financial Training Center Curricula by Area of Training

Credit

- Credit Analysis and Management (Basic and Intermediate Courses)
- Problem Loans
- Advanced Credit Analysis and Management
- Rural Credit Delivery

Treasury

- Basic Treasury Operations
- Treasury Management
- Risk Management

Technology

- Basic Technology Concepts
- Managing Technological Change

Trade Finance

- Basic Trade Finance
- Intermediate Trade Finance

Marketing

- Sales Skills
- Marketing Concepts and Tactics
- Strategic Planning
- Competitive Strategy
- Rural Credit Delivery

Management and Human Resources

- Developing Management Skills
- Human Resources Workshop

Services Management

- Deposit Mobilization
- Services Management
- Operations Simulation Game
- Managing Productivity

Financial Control

- Basic Financial Control
- Financial Control and Analysis
- Management Information Systems

Seminars will be given at three management levels as follows:

Table 4

Curricula by Management Level

Senior Level Management (12 seminars - 180 participants)

- Advanced Credit Analysis and Management
- Strategic Planning (Competitive Strategy)
- Risk Management
- Management Information Systems
- Managing Technological Change
- Savings Mobilization

Middle Level Management (29 seminars - 580 participants)

- Intermediate Credit/Problem Loans
- Marketing Concepts and Tactics
- Treasury Management
- Human Resources Workshop
- Bank Operations
- Managing Productivity
- Intermediate Trade Finance
- Financial Control and Analysis
- Rural Credit Delivery

Operating Level Management (27 seminars - 540 participants)

- Basic Credit Analysis and Management
- Sales Skills
- Basic Treasury Operations
- Developing Management Skills
- Basic Technology Concepts
- Services Management
- Basic Trade Finance
- Basic Financial Control

The Senior Level is defined as the group comprising the upper level of management, including Presidents, Vice Presidents and Regional Managers. The Middle Level is comprised of experienced middle managers or those recently promoted to middle managment. This is a very important target group, as they are responsible for the implementation of bank policies and are in charge of the day-to-day operations of the financial institutions. The Operating Level comprises the banks' recently promoted supervisors as well as the heads of units or small departments.

3) Training Methods and Duration of Courses

A variety of training methods will be employed, including case studies, lectures, small group exercises, and game playing. Operational level employees will be given short talks, with extensive use of visual aids, and simplified case studies in view of their more limited educational backgrounds.

Since ICIs will not be inclined to allow their employees to be absent for long periods, and given the fact that Bolivian workers are not accustomed to receiving training in extended courses, all courses have been designed to be presented in three-to-five day seminars (except the basic credit training course, which will last ten days). The seminars will be narrowly focussed, as indicated above, and form part of a larger curricula addressing the Center's core subject areas.

Workshops will also be held to discuss topical issues such as deposit mobilization techniques, extending services to rural areas, the changing competitive environment, changes in bank regulations, and the like. These will serve to keep the banking community informed of changing financial sector issues.

4) Course Development and Delivery

During the first year of the FTC, it will be necessary to "import" already prepared seminars from abroad. In both the United States and Latin America, several banking and finance training centers exist which are capable of carrying out the training identified. These organizations will be responsible for the development of the seminars, their delivery, and the preparation of IDEA's local instructors and consultants so that they can teach the courses in the future.

USAID and IDEA will assure that the contract signed with the institution responsible for the delivery of the seminars and overall technical assistance to the FTC will contain a clause stating that teacher training sessions must be given as part of the contractor's responsibilities. IDEA should also acquire intellectual rights to course materials, so as to avoid problems with the use of such materials in the future by local instructors and consultants.

The FTC will also develop and adapt course materials to make them more appropriate to the Bolivian situation, as time goes on. A large percentage of the courses developed will be modifications of seminars already being used in other countries which are adaptable to the Bolivian context. During the second and third years of operation, most cases used in the seminars should be written based on experiences and real-life situations of Bolivia's financial institutions. The technical assistance contractor will also assist in this process.

Local instructors, who will work at the FTC part-time, will be recruited from local universities, Bolivian consulting firms, financial institutions, and IDEA itself.

5) Evaluation of Training Courses

All seminars and instructors will be evaluated at the end of each session by participants. Instructors will also evaluate all participants. The purpose of the evaluations will be to improve the quality of the training courses by identifying which training methods are most successful in achieving their objectives.

There is a wide range of possible evaluation techniques which can be used. The selection of the correct technique (or combination of techniques) will depend on the nature of the training objective, the design of the program, and the training methods. IDEA is in the process of redesigning its evaluation methods, after some negative results experienced with the first evaluation method chosen. It used a literal translation of a North American system, and students could not understand the questions and were confused. IDEA's new evaluation system is easier to understand, has fewer questions, and has been used successfully in local universities.

6) FTC Organization and IDEA Support

The FTC will be a semi-autonomous division within IDEA. The establishment of the FTC on a semi-autonomous basis will allow it to complement IDEA's ongoing training programs, draw upon IDEA's existing administrative capabilities and reduce its overall costs of operation.

The FTC will have an Academic Director who will report to the IDEA General Manager and cooperate with the Center's Training Advisory Board (see below). The Director will be responsible for the day-to-day operations of the Center. Specifically, he/she will: provide leadership to the FTC staff; monitor the training needs of Bolivian bankers (with the advice of the Training Advisory Board); oversee development of the course offerings of the Center; supervise the Center's technical assistance contractor; oversee the arrangement of training seminars and the hiring of local consultants for the training activities; supervise the development and preparation of local case studies; and establish and maintain close relationships with all Bolivian financial institutions and with similar bank training institutions in other countries.

One Academic Assistant, one secretary, and one clerk will be hired to carry out the activities of the FTC. The Academic Assistant will be responsible for all matters concerning teaching methodologies, course development, evaluation of instructors, course scheduling and student registration. He/she will also assist the Academic Director in the ongoing training needs analysis process and the development of case studies.

The FTC's Training Advisory Board will assist in the oversight of the FTC. Membership will be drawn from ASOBAN. Its role will be to assist IDEA's Board of Directors, the IDEA General Manager, and the staff of the FTC in designing training courses and workshops which are appropriate to the needs of the Bolivian financial community.

IDEA's Administrative Unit is already successfully operating, and it will provide all basic administrative support to the FTC. Courses will be marketed by the IDEA Marketing Coordination Unit. All accounting, purchasing and general administrative tasks will be handled by IDEA.

IDEA's facilities will be expanded very soon, providing enough space to accommodate the needs of the FTC. The new layout will contain three classrooms and four break-out rooms, as well as lounge facilities. Each classroom will be provided with all necessary equipment, such as screens, slide projectors, overhead projectors, flip charts, and chalkboards. There is no need to budget under the FTC component of the Project for teaching facilities, since these new facilities have already been funded. A special section for financial books and publications will be established in the IDEA library, and provisions have been made in the budget to acquire a modern collection of books and case studies.

7) Financing of the FTC

AID will finance the basic costs of setting up the Center and a declining percentage of its operating costs. Operating costs will be fully financed from course fees by the end of year 3.

AID will finance 100 percent of technical assistance to organize the FTC, FTC staff training costs, course royalty charges and initial commodities. Course delivery costs, which include technical assistance to teach seminars and prepare local instructors, FTC overhead costs, and course logistical and administrative costs, will be partially financed by AID during the life of the component given the high cost of foreign technical assistance which will be used to establish the Center's curricula and teach initial courses. AID will finance 75 percent of FTC operating costs during year 1, 50 percent in year 2 and 30 percent in year 3.

8) End of Project Status (EOPs)

At the end of the Project, the FTC will be fully developed and incorporated into IDEA as a functional self-financing training unit. Currently, there is only ad hoc training available to the financial sector, and, if ICIs are to have a full role in Bolivia's economic reactivation, a permanent training center is needed. During the three-year life of the component, 1,300 ICI professionals will be trained. The FTC will continue operations after its initial three-year period, but at a reduced pace, in order to meet continuing financial sector training needs. Its operations will result in a higher degree of efficiency in the financial community and a more timely response by the sector to the private sector's financial needs.

9) Inputs

To establish the FTC, the following inputs will be required:

- Technical Assistance (24 p.m. long-term, 12 p.m. short-term; $677,000 AID)
- Staff Training (9 training trips, short-term; $45,000 AID)
- Course Delivery Costs (includes TA and course administration and logistical costs; $1,044,600; AID 75% year 1, 50% year 2, 30% year 3)
- FTC Operating Costs (staff salaries and Center operating costs; $138,900; AID will finance declining percentages)
- Commodities (furniture, office equipment, library materials; $80,000 AID)

Technical assistance will be obtained from a U.S. or Latin American institution (bank or training center) already operating bank training courses. This institution will be asked to set up training courses using materials and curricula it has already developed. The contractor will also provide assistance in teacher training, curriculum development and course evaluation, and arrange for 9 short-term training trips for FTC staff and teachers to its home office training facilities.

b. Expansion of the Services of the Association of Banks and Financial Institutions of Bolivia (ASOBAN) ($393,200 AID; $312,700 Bolivia)

1) Status and Refocus

The development of an effective banking association is recognized as a necessary ingredient to a revitalized financial sector. ASOBAN was established in 1976 to represent the private sector financial community in Bolivia. Its membership is comprised of all Bolivian and foreign banks with operations in Bolivia, as well as the Caja Central de Ahorro y Préstamo (CACEN). To date, the primary role filled by ASOBAN, unlike its counterparts in the U.S. and Latin America, has been to represent the banking sector in lobbying endeavors and, to a much more limited extent, to gather banking industry data. During the intensive review, numerous bankers as well as the board members and executives of ASOBAN were questioned about the role of ASOBAN as a banking association. Overall, ASOBAN was criticized for very low levels of activity. With incipient reactivation of the economy occuring, the transformation of ASOBAN into a more pro-active banking association will enable it to assist its members to improve their operations.

The purpose of this subcomponent is to expand ASOBAN services in order to increase the Association's usefulness to the financial community.

2) Activities

This subcomponent will sponsor the development of six new ASOBAN services over the life of the Project in an effort to make it less of a lobbying organization and more of a professional trade association. While additional services could be developed, the six detailed below have been selected by ASOBAN members from a list of potential services suggested by a project consultant. Other potential services which might be developed later include bank security consulting and assistance with automated banking.

a) Central Information System

The objective of this activity is to create within ASOBAN a bank customer data base in a two-phase process. Phase I will consist of establishing a national record of cancelled demand deposit accounts. Phase II will consolidate information on loans extended by banks and determine the global indebtedness by credit sector for all kinds of loans. This will be done through the creation of a data base run by two new ASOBAN staff members and the acquisition of one microcomputer. The provision of information on deposits and lending will facilitate inter-bank exchanges of information and improve internal bank efficiencies. The central information system will be expanded to provide other types of information as appropriate.

b) Check-Clearing System

The objective of this activity will be to provide Bolivian commercial banks with a back-up system for inter-bank check clearing when the Central Bank is unable to provide that service. ASOBAN members feel this is needed because, although the Central Bank is beginning to function better, there is no guarantee that it will not close periodically in the future. When it has closed in the past, ASOBAN has had to handle check clearing through a manual, labor-intensive process. ASOBAN wants to perform this function in a more professional and systematic way. The activity will include establishment of schedules and processing procedures, and the development of internal controls. One professional will be added to ASOBAN's staff, and a microfilm reader will be provided for use with the microcomputer being provided as part of the central information system.

c) Economic Analysis

This activity's objective will be to provide ASOBAN and its members with timely, standardized financial and economic information. ASOBAN will consolidate and analyze banking industry information as well as economic trends in Bolivia. Currently, ASOBAN has one economist who was until recently the Central Bank's Chief of Economic Studies. Under this activity, an assistant economist will be retained. One microcomputer with an appropriate data base will be provided. Combined, the two economists will establish an Economics Unit within ASOBAN which will be responsible for preparing reports on the economy and banking trends. These reports will help the Board of Directors of ASOBAN better understand the status of the banking industry, support its lobbying efforts with government institutions, and prepare recommendations to strengthen the banking industry.

d) Legal Analysis

As in the case of economic information, legal information is often scarce and difficult for banks to obtain. The objective of this activity will be to establish a permanent Legal Unit in ASOBAN which will analyze legal regulations that affect the banking industry. This will provide ASOBAN and its members with the requisite support to analyze and act upon subjects related to banking law and banking regulations.

One lawyer will be retained as a permanent staff member of ASOBAN. A word processor station and software will be provided. The Legal Unit will develop position papers on banking regulations, serve as a communication channel between the Association and entities that interact with the financial sector, and assist members' own lawyers in analyzing labor and fiscal laws and regulations affecting the industry.

e) Personnel Selection

Given the high turnover of ICI staff, the need exists to develop a central clearing house on personnel. ASOBAN will assist in ICI employee selection, test potential employees and evaluate their training needs, and provide career counselling, as may be appropriate. A new ASOBAN unit will screen employee candidates, verifying employment and academic records, test them and provide member banks with confidential reports, as requested by ICIs. One half-time professional, who will also be responsible for managing the technical library, will be retained.

f) Technical Library

The reorganization and expansion of ASOBAN services requires developing a technical library for use by the various sections of the Association as well as its members. The objective is to create a business library to facilitate the Association's research activities and to help ASOBAN members keep abreast of and to research, financial industry topics. Materials will be provided to stock the library, and expansion over the life of the project is envisioned.

3) ASOBAN Restructuring

Currently, ASOBAN's Board of Directors represents the full spectrum of the banking community, and this will not change over the three-year life of the subcomponent. However, the staff of ASOBAN is quite small (four professionals) and does little more than support lobbying efforts and carry out some ad hoc analyses and studies. ASOBAN's staff will be organized into two new departments to enable ASOBAN to provide the services contemplated. A Technical Department will be established which will include a Legal Unit, an Economics Unit and a library. An Operations Department will be put in place to consist of the Central Information Unit, Personnel Selection Unit and the Internal Accounting Unit. Six additional staff members will be retained to operate the new units and the library.

The strategy of this subcomponent calls for the fostering of an ongoing, cooperative relationship between ASOBAN and a successful bankers association from the U.S. or another Latin American country. In addition to assisting ASOBAN develop its new services, such a relationship will expose

ASOBAN staff and members to the valuable services a professional bankers association can provide its members. It will also provide Bolivian ICIs with a means to develop banking contacts in another country which should be useful both to their own ICIs and to the financial sector as a whole.

4) End of Project Status (EOPs)

This subcomponent will result in a better functioning banking association. ASOBAN's membership will benefit from the expansion of the Association's activities. ASOBAN will broaden its role from that of a lobbying association, and should develop into a major force in the Bolivian financial community.

5) Inputs

The following inputs will be required to help establish ASOBAN's new sources:

- Short-term Technical Assistance (18 p.m.) from another banking association ($316,200 - AID).
- Six Training Trips ($30,000) to the cooperating association (AID)
- Computers and Library Materials ($47,000 - AID $5,000 ASOBAN).
- Operating costs of new services ($307,700, 100 percent financed by member banks).

ASOBAN members themselves will finance 100 percent of the cost of delivering new services. This will be done by increasing annual dues or on a fee-for-service basis. AID will finance the costs of developing the new services. For this purpose, 18 p.m. of technical assistance in the service areas specified above, and general assistance in the organization of bankers associations, will be provided by another U.S. or Bolivian banking association. That association will also arrange six trips by ASOBAN staff members to its headquarters during the course of the Project.

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c. Savings Mobilization ($722,900 AID; $70,000 Bolivia)

In order for the economy to fully recover and begin to grow again, it is necessary to increase the mobilization of domestic savings and allocate them to productive uses, and to develop financial instruments that will provide a vehicle for capturing additional savings.

During the last year, commercial banks have been the most significant mobilizers of new deposits. These deposits have come from the dollar currencies formerly held by the Bolivian public, some repatriated savings attracted by high interest rates, earnings from the narcotics trade, the liquidation of non-financial savings vehicles, and the informal economy. Despite the potential for mobilizing more deposits, deposit-gathering efforts focussed on commercial banks at this time are not advisable given the precarious situation of many banks and the additional potential liabilities for the BDIF and the GOB which would be created by increasing bank deposits in the short run (see Section II.B). In perhaps another year, after the anticipated "shake-down" in the private banking sector, deposit mobilization efforts for the banks could be more appropriate. In the short run, savings mobilization efforts will be possible in the rural financial sector, where little or no formal savings experience exists, and where financial institutions with limited experience in mobilizing deposits already operate. Savings cooperatives and mutuals are the most viable candidates.

Recognizing the constraints to savings mobilization existing in the Bolivian financial sector, this subcomponent is divided into three activities which will capitalize upon progress being achieved in the financial community and contribute to an increased level of domestic savings.

1) Capital Markets Development

a) Objectives

Central to deposit mobilization is the need to consider the development of financial instruments which can contribute in a broader sense to savings mobilization and allocation. The objective of this activity will be to broaden the awareness of the need for, and role of, savings mobilization through capital market instruments, and to exploit opportunities for developing new financial instruments in Bolivia.

b) Activities

To examine the possibilities for introducing and/or expanding financial instruments available to institutional and individual savers, technical assistance will be provided to carry out a capital markets assessment in Bolivia. This assessment will examine current sources of financing, types of financial instruments being used in the sector, prevailing uses for term deposits, and potential usage of new financial instruments. The latter will include study of the potential for a Bolsa de Valores (market for trading debt and equity instruments, inter-bank financial instruments, treasury bills, negotiable corporate debt instruments (short-term paper and corporate bonds), and mortgage-backed securities.

The assessment will be followed by six person-months of technical assistance to further examine and develop instruments identified as appropriate for Bolivia. It is envisioned that this short-term technical assistance will be provided over a three-year period so as to build upon changes in the financial sector resulting from this Project and other donor assistance.

2) Assistance for FENACRE

a) Objective

This activity is designed to increase the capacity of rural credit unions and cooperatives to mobilize deposits. It will focus on providing technical assistance and training to the National Federation of Credit Unions (FENACRE) and through it to the more than 200 affiliated credit unions and four integral cooperatives to which FENACRE provides credit, cooperative education, technical assistance, or financial services. FENACRE has been selected to receive this assistance, because it is a growing and potentially important private sector mobilizer of savings whose rural clients are not now well served by the rest of the financial system.

b) Activities

To support FENACRE and its affiliates in its rebuilding and redirecting efforts, A&A Project funds are being used in 1987 to contract short-term technical assistance to analyze FENACRE's new savings mobilization pilot project and recommend areas in which FENACRE might need additional assistance in the future. The information provided will be used to refine USAID's current plans for assistance to FENACRE under the Strengthening Financial Markets Project.

Under the Project, short-term technical assistance will be contracted to do a management audit of FENACRE which will analyze FENACRE's organizational and administrative systems and recommend modifications which will make FENACRE more efficient and help it to more effectively provide services to its member coops and affiliates. It is estimated that three person-months of short-term technical assistance will be required to carry out this analysis.

A market research study will be carried out to learn more about FENACRE members and to explore the potential for savings mobilization in urban and rural areas.

FENACRE personnel and managers from FENACRE's affiliates will be invited to participate in training courses offered by the Financial Training Center to improve the general educational level of FENACRE's employees. The Project will fund travel and per diem costs for key FENACRE managers to visit institutions similar to FENACRE in other countries. These trips will provide managers with an opportunity to exchange experiences with their counterparts from other countries and learn how savings and loan institutions in other countries are solving problems which are similar to FENACRE's problems, and how they are providing services to their members.

Technical assistance will be provided to FENACRE under the Project to help plan the expansion of initial deposit mobilization campaigns in Cochabamba to other cities, to prepare marketing strategies for the new campaigns, to design new savings mobilization techniques, and to design new financial instruments which would be needed to promote savings.

FENACRE's successes during the past 15 months with its pilot savings mobilization program have created a great deal of interest on the part of its affiliates, which would like to begin savings mobilization programs of their own. This interest has caused FENACRE to reassess its role as the head of a national system of savings and loan cooperatives and has resulted in a decision to emphasize and amplify FENACRE's role as a cooperative bank which centralizes cooperative funds, channels surplus funds from one cooperative to another, and provides financial services to the national system of savings and loan cooperatives. The Project will support this new initiative with technical assistance in the areas of financial management, financial service analysis, and cash management.

This technical assistance will be provided by a long-term (two-year) advisor and 18 p.m. of short-term experts in savings mobilization, credit union management, financial management and related areas involved in credit union management. Managerial assistance will focus on personnel management, control and auditory procedures, credit assessment, loan management and similar topics which will be identified in the future. Training trips to rural credit unions in other Latin American countries for nine people are also planned.

3) Savings Mobilization Seminars for Banks

a) Objective

Recognizing the importance commercial banks will have in deposit generation and placement following the near-term projected consolidation in the sector, the objective of these seminars will be to provide bankers with exposure to deposit mobilization techniques used in other countries, and the opportunity to jointly discuss how they might be applied in Bolivia in the future.

(b) Activities

Building upon the savings mobilization work undertaken to date under AID's A&A Project, a series of workshops on deposit mobilization and deposit services will be undertaken at the senior management level as part of the Financial Training Center's (FTC) course offerings. These workshops will be run by FTC instructors and cover the following areas:

- Strategic design and management of deposit gathering campaigns;

- How to organize and coordinate the various departments of a bank for effective deposit services;

- How to set reasonable goals, organize marketing efforts, and provide incentive compensation or recognition to those who achieve them;

- Targeting markets/customer groups and use of formal or informal market research techniques in deposit campaigns;

- Use of advertising, public relations techniques, such as sports team identification, improved logos, and pamphlets;

- Meeting customers' needs for more convenient and easily available banking services;

- Development of new deposit vehicles, such as special-purpose savings plans; and

- Interest rate policy and maturity structures, targeting currency requirements and coordination of depositors' and bank needs.

4) End of Project Status (EOPS)

The level of awareness, training and utilization of savings mobilization techniques will be more fully incorporated into the Bolivian financial community. The capital markets activities, at a minimum, will have examined the potential for new financial instruments. It is expected that with appropriate applications of the planned short-term technical assistance, new financial instruments will be developed. FENACRE and its credit unions will be restructured and recapitalized. Substantial growth in relative market share and absolute level of deposits will be achieved. Management's capability to identify problems and take advantage of opportunities for system growth and development will be improved. Savings mobilization concepts, procedures and opportunities will be fully integrated into the FTC program. Participants will benefit from the training provided. Commercial banks and other ICIs will undertake initiatives to increase institutional and individual deposits. Taken as a whole, it is expected that these activities will result in significant savings generations within the financial community.

5) Inputs

AID will finance 7.5 p.m. of technical assistance advisors for carrying out the capital markets assessment and follow-on assistance. AID will also finance a long-term advisor with financial management, cooperative or credit union experience to work with FENACRE over a two-year period, and nine training trips for FENACRE or capital market personnel. The long-term advisor and FENACRE will design, supervise and monitor an additional 18 p.m. of short-term technical assistance for FENACRE in the areas identified above. The total AID contribution to this subcomponent will be $722,900. FENACRE and the credit unions will bear all savings mobilization campaign ($70,000) and management improvement costs out of their ongoing annual operating budgets. Costs of carrying out savings mobilization training under the FTC are included in the FTC component.

3. Improvement of Financial Sector Policy Research and Analysis ($719,800 AID; $16,500 Bolivia)

a. Objective

The present period of intense discussion of the problems facing the financial system and possible solutions to these problems has been very fruitful. There is a strong consensus among those persons and institutions which have recently studied the Bolivian financial system concerning changes in policy required for the recovery, strengthening, and modernization of the system. To build on this progress, however, it will be necessary to improve the process of financial sector policy formulation. Financial sector research and informed policy discussion should be institutionalized, and the private sector should fully participate in such research and discussion in order that a fuller understanding and acceptance of policy measures on behalf of all sector participants can be achieved.

The objective of this component is to promote private sector participation in research and informed discussion in support of critical policy reforms. The activities to be carried out under this component will permit intelligent dialogue on financial sector issues; keeping in mind that fundamentally the GOB's and the private sector's objectives are the same - to achieve economic recovery.

b. Background

Because the financial system is in a state of crisis, it is imperative that a number of policy changes be implemented immediately. The World Bank and the GOB have reached tentative agreement concerning the implementation of initial policy measures, and most of them will be established as conditions precedent for the disbursement of funds under the World Bank's Balance of Payments/Structural Adjustment Loan. The most important measures are:

1. Market-determined real rates of interest must be maintained on deposit accounts (there has been pressure from some elements of the GOB to lower interest rates by decree).

2. Reserve requirements must not favor dollar accounts and should favor longer-term deposits.

3. The multi-currency situation is complex and must receive careful attention and study. (Most agree that in the longer run the system must move away from the dominance of the dollar.)

4. Public sector arrears to private suppliers must be reduced in a way that is consistent with the IMF stabilization program.

5. Increased externally funded credit programs must not disrupt domestic efforts to mobilize savings.

6. Existing banking regulations must be reviewed in order to permit the creation of adequate instruments and mechanisms to facilitate increased mobilization of longer-term resources.

7. To sort out the problems with the private commercial banks, the dedollarization payment issue must be resolved, external audits should be conducted, limits should be placed on the amount of a bank's portfolio lent to the bank's own holding group, bank supervision must be improved, and a deposit insurance fund should be established.

8. To sort out the problems with the public banks, key functions of the Central Bank must be strengthened and others devolved to other institutions. Serious consideration must be given to restructuring the Banco del Estado and the Banco Agrícola.

As noted elsewhere in this Paper, steps are already being taken to begin work on these measures.

c. Activities

The activities to be pursued under this component are aimed at promoting the participation of the private sector in the identification of topical policy issues, in the research of those issues, in the discussion of the issues by key persons in the sector, and in the formulation of follow-up recommendations and policy changes based on the research and discussions. The main activity to be sponsored under this component will be private-sector-organized seminars to exchange opinions and present analyses concerning financial sector issues. Limited financial sector research will also be sponsored, both to improve understanding of financial sector operations and as input to the seminars. As opposed to the FTC's training seminars which will instruct ICI officials in banking practices, the seminars to be carried out under this component will focus on short to medium-term financial sector policy issues.

Identification of topical policy issues will be the first step. Some of the issues identified by the GOB and World Bank will be included in order to develop a fuller understanding of those issues and a fuller consideration of policy alternatives by, and with, private sector representatives. Other issues which go beyond these will also be identified. This will be accomplished as the project proceeds through discussions with selected participants from the public and private sectors of the financial market system. A tentative list of seminar topics based on preliminary discussions is presented below.

Table 5

Improvement of Financial Sector Policy Research and Analysis

Seminar Topics

1987 A&A Seminars

"Bolivia's Emergence from Hyper-Inflation: Are High Interest Rates Unavoidable?"

"Initial Stages in the Creation of Formal Capital Markets."

"The Multi-Currency Issue: Costs and Benefits of Dollarization in Bolivia."

"Importance of Informal Finance in Bolivia: Lessons for Formal Financial Institutions."

1988 SFM Seminars

"Regulation and Supervision of Financial Institutions."

"Theory and Practice of Loan Delinquency and Loan Recovery."

"Term Lending for Development Purposes."

"Branching to Expand Financial Services into Rural Areas."

1989 SFM Seminars

"Deposit Mobilization."

"International Aspects of Bolivian Domestic Financial Markets."

"The Role of Public Sector Financial Institutions in Bolivia."

"Interest Rates in Bolivian Financial Markets."

1990 SFM Seminars

- "Increasing Access of Borrowers to Credit Services and Reducing Transaction Costs."
- "Capital Markets: Further Review of the Initial Stages of Their Creation."
- "Spreads and Efficiency of Financial Intermediaries."
- "Informal Finance."

Research will all be directed at seminar presentations, and the presentations themselves will all have to be very practical. The scope of the research will be very highly defined, and always judged by the criterion that it be directly applicable to the policy-making process. USAID/Bolivia will approve all research topics in advance of the initiation of studies.

Research will usually be carried out by researchers and students from both Bolivia and the United States. However, some research may be done by persons respected in their fields from other Latin American countries. The research procedures will include field surveys to collect primary data, case studies with key financial sector participants, and analysis of the data collected.

Papers will be written for presentation at the 12 seminars that are planned during the life of the Project. The audience invited to the seminars will include high-level government officials and key private sector leaders. The seminars will be planned so that all papers for presentation will be written and distributed to seminar participants in advance of the seminar.

The seminars will generally last two days and will tend to take one of two forms. Form A may include presentation of as many as five or six papers. After presentation of each paper, a designated discussant will present his or her written comments on that paper. This will be followed by a general discussion period lasting about an hour that should allow for ample dialogue among all participants. Form B will include presentation of two papers. After presentation of the papers, the presenters will provide a structured environment for logically thinking through the issue(s) with the active participation of the seminar attendees. When deemed appropriate, seminar proceedings will be published and distributed to all participants, and perhaps to a wider readership.

The seminars should, in many cases, lead to follow-up activities aimed at designing and implementing detailed policy reforms. When seminar recommendations merit follow-up action to formulate and implement a policy reform, assistance for that effort will be available under the Project.

The Project will also sponsor a series of occasional informal meetings of leaders in the financial sector. These will be aimed at discussing important issues of the moment, and they may be one mechanism for the follow-up work mentioned above. They could be either luncheon meetings or workshops.

An adjunct activity which will complement this component is support for the academic training of Bolivian researchers. It is important that a small group of Bolivians be trained as financial market researchers. The most appropriate training is the Master of Science degree in Economics with a major in Banking or Finance. This Project will not finance these studies, but it will seek out the best candidates and work with Mission scholarship programs to place them in U.S. universities.

d. Organization of Seminars and Research

A contract will be signed with a U.S. university or consulting firm for the implementation of this component. The contractor will work with local Bolivian institutions in organizing seminars and commissioning financial sector research. Initially, the contractor will work with the Catholic

University Institute for Socio-Economic Research (IISE) in La Paz. Later the contractor will attempt to establish cooperative relationships with the Private University of Santa Cruz, and at the San Simón University Faculty of Economics in Cochabamba. Other institutions which might cooperate in setting up seminars include the Latin American Institute for Socio-Economic Studies (ILDES), the Bolivian Institute for Business Studies (IBEE), IDEA, the Economic Studies Department of the Central Bank of Bolivia (BCB), and the Unidad de Analisis de Politicas Economicas (UDAPE).

The contractor for this component will subcontract with the local Bolivian entities identified above, as appropriate, for the joint organization of a seminar or to sponsor student or faculty research. The contractor will also be able to subcontract, on a very limited basis, with U.S. universities to sponsor short-term research by graduate students interested in working in Bolivia (four students for six months each during the life of the Project). Finally, the contractor will also be responsible for bringing U.S. and Latin American experts to Bolivia for seminar presentations.

The Project will normally cover the full costs of research and seminars. However, during the implementation of the Project, the contractor will look for opportunities for joint sponsorship with other interested Bolivian parties, especially with financial institutions, ASOBAN, and the GOB, with the idea of supporting the development of policy discussions which could continue after the Project ends.

e. End-of-Project Status (EOPs)

The most tangible outputs of this component will be the 12 seminars and the associated research. At least 12 important issues will have been investigated. Key decision-makers, including both private and public sector representatives, will be well-informed concerning those issues, and they will be given the opportunity to pursue recommended policy reforms. Finally, assuming that this process is well-managed and well-received, a number of financial sector policy reforms should be brought about.

f. Inputs

The inputs required to implement this Project component include:

- Preparation of Seminar Papers (24 p.m. U.S. experts, 36 p.m. Bolivian experts).

- Research (four U.S. students, nine Bolivian students, six months each).

- Contractor Backstopping (nine p.m. and logistical costs of seminars).

- Technical Assistance for Seminar Follow-up (12 p.m.).

- Commodities (very limited data processing machines and research materials for Bolivian universities).

All of the above inputs will be financed by AID ($719,800) except for $16,500 of seminar logistics and other costs to be financed by cooperating Bolivian institutions.

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C. Project Outputs and Inputs

1. Outputs

a. BDIF

- External bank audits (21)
- Operating BDIF (x)

b. FTC

- Operating FTC (x)
- ICI officers trained (1,300)
- FTC courses held (68)

c. ASOBAN

- New services established (6)

d. Savings Mobilization

- Capital markets study (1)
- Capital market instruments developed (1 to 5)
- Savings mobilization campaigns, FENACRE (3 to 5)

e. Policy Research and Analysis

- Seminars held (12)
- Financial sector topics researched (13)
- New policies implemented (3 to 12)

2. Inputs

		A I D ($000)	Host Country
a. Technical Assistance			
BDIF	48 p.m.	$1,032	-
FTC	36 p.m.	$677	-
ASOBAN	18 p.m.	$316	-
Savings Mobilization	49.5 p.m.	$711	-
Policy Research	12 p.m.	$107	-
b. Staff Training			
BDIF	15 trips	$54	-
FTC	9 trips	$45	-
ASOBAN	6 trips	$30	-
Savings Mobilization	9 trips	$12	-
c. Operating Costs			
BDIF		-	$1,327
FTC		$79	$60
ASOBAN Services		-	$308
Savings Mobilization		-	$70
d. Commodities			
BDIF furniture, office equipment		$40	-
FTC furniture, office equipment, library materials		$80	-
ASOBAN computers, library materials		$47	$5
Policy research materials, computers		$27	-

e. <u>Bank Audits</u>	$243*	188
f. <u>BDIF Capitalization</u>	-	$26,014
g. <u>FTC Course Costs</u>	$561	$484
h. <u>Seminar/Research Costs</u>	$585	$17
i. <u>Evaluations and Audits</u>	$130	-
j. <u>Project Coordinator</u> 36 p.m.	$324	-
k. <u>T.A. Chief of Party</u> 36 p.m.	$706	-
l. <u>Contingencies</u>	$394	$172
TOTALS	$6,200	$28,645

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* plus $320,000 under A&A Project

III. D. Project Beneficiaries

Although it is true that the most direct beneficiaries of the Project will be Bolivia's private sector ICIs themselves, the Bolivian public at large will be the real beneficiaries of the Project. More financing will be available to the public for investment and operating costs. The public will have access to a greater number of more secure savings vehicles. A wider number of clients will have access to the financial system. Financial services will be provided more efficiently and at a lower cost. Lastly and most importantly, a better functioning financial system will help stimulate economic growth, and greater investment and employment opportunities will be available to the public.

Bolivia's ICIs will become more financially stable as a result of the Project. Their potential for profitability will be enhanced by increased deposit mobilization, better trained employees, and operational assistance from ASOBAN. Finally, ICI personnel will have a stronger voice in financial sector policy formulation.

At an individual level, ICI officers, ASOBAN employees, seminar participants, and policy researchers and analysts will also benefit from the Project.

IV. Cost Estimate and Financial Plan

A. Project Budget

The total cost of activities to be financed under this four-year Project will be $34,843,400. The total AID contribution will be $6,200,000 in grant funds. As detailed below, counterpart contributions to the Project will total $28,643,400. Table 6 shows the detailed cost estimates. Table 7 shows anticipated yearly disbursements under the Project. Section IV.C. shows implementation and financing methods. Annex C details life-of-project funding for each project component as well as budget assumptions utilized in developing the Project costs.

B. Component Budgets

1. Improvement of Financial Sector Regulation/Creation of the BDIF

The total projected cost of this component is $28,896,700. The private sector will finance $26,840,600 in BDIF operating expenses and capitalization the Central Bank will finance a $500,000 loan for capitalization as well as $187,500 in bank audit costs. AID support for the component totals $1,368,600. AID funds will finance long- and short-term technical assistance, training, and commodity acquisitions.

2. Improvement of ICI Operations

a. Financial Training Center (FTC)

The total projected cost of the FTC component is $1,985,500 over a three-year period. Of this total, the private sector will pay $544,000 to help finance FTC operating and course delivery costs. AID support for the FTC totals $1,441,500. AID funds will finance long- and short-term technical assistance, a declining portion of operating and course delivery costs, FTC staff training and commodity acquisition costs.

b. Association of Banks and Financial Institutions of Bolivia (ASOBAN)

The total projected cost of this subcomponent is $705,900 over a three-year period. Of this total, ASOBAN will pay from membership fees, fees for services, and internal working capital a total of $312,700 for service delivery costs and commodities. AID support for ASOBAN totals $393,200. AID funds will finance short-term technical assistance, the acquisition of commodities and ASOBAN staff training costs.

c. Savings Mobilization

The total projected cost of this subcomponent is $792,900 over a three-year period. AID will finance long and short-term technical assistance for FENACRE, support for undertaking a capital markets study and additional short-term technical assistance, and limited short-term training trips for a total of $722,900. FENACRE will finance at least $70,000 in savings mobilization campaign costs.

3. Policy Research and Analysis

The total cost of this component will be $736,300 of which AID will finance all but $16,500 for seminars, research and commodities.

4. Other Costs

AID will finance project audits and evaluations for $130,000, a Project Coordinator for $324,000, and a T.A. Term Chief of Party for $706,300. Contingencies total $393,700 for AID and $172,100 for Bolivia.

LIFE OF PROJECT ESTIMATED COSTS AND FINANCIAL PLAN

	AID GRANT FX	AID GRANT LC	Total	HOST COUNTRY G.O.B. FX	G.O.B. LC	Total	PRIVATE SECTOR FX	PRIVATE SECTOR LC	Total	GRAND TOTAL
I. BOLIVIAN DEPOSIT INSURANCE FUND										
A. Technical Assistance	1,274,600		1,274,600	187,500		187,500				1,462,100
B. Training	54,000		54,000							54,000
C. Project Operating Costs								1,326,600	1,326,600	1,326,600
D. Commodities	30,000	10,000	40,000							40,000
E. Capitalization (BCB loan and member premiums)				500,000		500,000	25,514,000		25,514,000	26,014,000
Subtotal, Bolivian Deposit Insurance Fund	1,358,600	10,000	1,368,600	687,500		687,500	25,514,000	1,326,600	26,840,600	28,896,700
II. ICI IMPROVEMENT: FINANCIAL TRAINING CENTER										
A. Technical Assistance	677,000		677,000							677,000
B. Staff Training	45,000		45,000							45,000
C. Course Delivery Costs	458,500	102,100	560,600					484,000	484,000	1,044,600
D. FTC Operating Costs		78,900	78,900					60,000	60,000	138,900
E. Commodities	80,000		80,000							80,000
Subtotal, Financial Training Center	1,260,500	181,000	1,441,500					544,000	544,000	1,985,500
III. ICI IMPROVEMENT: ASOBAN SERVICES										
A. Technical Assistance	316,200		316,200							316,200
B. Training	30,000		30,000							30,000
C. Project Operating Costs								307,700	307,700	307,700
D. Commodities	47,000		47,000				5,000		5,000	52,000
Subtotal, ASOBAN Services	393,200		393,200				5,000	307,700	312,700	705,900

	AID GRANT FX	AID GRANT LC	Total	HOST COUNTRY G.O.B. FX	G.O.B. LC	G.O.B. Total	PRIVATE SECTOR FX	PRIVATE SECTOR LC	Total	GRAND TOTAL
IV. ICI IMPROVEMENT: SAVINGS MOBILIZATION										
A. Technical Assistance	710,900		710,900							710,900
B. Training	12,000		12,000							12,000
C. Promotional Campaigns								70,000	70,000	70,000
Subtotal, Savings Mobilization	722,900		722,900					70,000	70,000	792,900
V. IMPROVEMENT OF POLICY RESEARCH AND ANALYSIS										
A. Seminars and Research	692,800		692,800					16,500	16,500	709,300
B. Commodities	27,000		27,000							27,000
Subtotal, Improvement of Policy Research & Analysis	719,800		719,800					16,500	16,500	736,300
VI. OTHER COSTS										
A. Evaluations and Audits	130,000		130,000							130,000
B. Chief of Party, Institutional Contract, 3 yrs	706,300		706,300							706,300
C. U.S. Hire Personal Services Contract, 3 yrs	324,000		324,000							324,000
D. Contingencies (7%)	380,300	13,400	393,700	13,100		13,100	500	158,500	159,000	565,800
Subtotal, Other Costs	1,540,600	13,400	1,554,000	13,100		13,100	500	158,500	159,000	1,726,100
PROJECT TOTAL	5,995,600	204,400	6,200,000	700,600		700,600	25,519,500	2,423,300	27,942,800	34,843,400

DISBURSEMENT SCHEDULE

	YEAR 1 FX	YEAR 1 LC	YEAR 2 FX	YEAR 2 LC	YEAR 3 FX	YEAR 3 LC	YEAR 4 FX	YEAR 4 LC	TOTAL FX	TOTAL LC	GRAND TOTAL
I. BOLIVIAN DEPOSIT INSURANCE FUND											
A. Technical Assistance	825,600		395,500		120,500		120,500		1,462,100		1,462,100
B. Training	14,000		18,000		18,000		4,000		54,000		54,000
C. Project Operating Costs		290,200		305,200		343,500		387,700		1,326,600	1,326,600
D. Commodities	30,000	10,000							30,000	10,000	40,000
E. Capitalization Central Bank loan (member premiums)	6,436,700		6,233,000		6,521,700		6,822,600		26,014,000		26,014,000
Subtotal, Bolivian Deposit Insurance Fund	7,306,300	300,200	6,646,500	305,200	6,660,200	343,500	6,947,100	387,700	27,560,100	1,336,600	28,896,700
II. ICI IMPROVEMENT: FINANCIAL TRAINING CENTER											
A. Technical Assistance	303,400		303,400		70,200				677,000		677,000
B. Staff Training	15,000		15,000		15,000				45,000		45,000
C. Course Delivery Costs	357,500	229,400	80,300	212,800	20,700	143,900			458,500	586,100	1,044,600
D. FTC Operating Costs		44,700		46,300		47,900				138,900	138,900
E. Commodities	80,000								80,000		80,000
Subtotal, Financial Training Center	755,900	274,100	398,700	259,100	105,900	191,800			1,260,500	725,000	1,985,500
III. ICI IMPROVEMENT: ASOBAN SERVICES											
A. Technical Assistance	105,400		105,400		105,400				316,200		316,200
B. Training	10,000		10,000		10,000				30,000		30,000
C. Project Operating Costs		98,600		102,500		106,600				307,700	307,700
D. Commodities	52,000								52,000		52,000
Subtotal, ASOBAN Services	167,400	98,600	115,400	102,500	115,400	106,600			398,200	307,700	705,900

	YEAR 1 FX	YEAR 1 LC	YEAR 2 FX	YEAR 2 LC	YEAR 3 FX	YEAR 3 LC	YEAR 4 FX	YEAR 4 LC	TOTAL FX	TOTAL LC	GRAND TOTAL
IV. ICI IMPROVEMENT: SAVINGS MOBILIZATION											
A. Technical Assistance	381,700		257,200		72,000				710,900		710,900
B. Training	4,000		4,000		4,000				12,000		12,000
C. Promotional Campaign		24,000		24,000		22,000				70,000	70,000
Subtotal, Savings Mobilization	385,700	24,000	261,200	24,000	76,000	22,000			722,900	70,000	792,900
V. POLICY RESEARCH AND ANALYSIS											
A. Technical Assistance	231,600	5,500	230,600	5,500	230,600	5,500			692,800	16,500	709,300
B. Commodities	27,000								27,000		27,000
Subtotal, Policy Research and Analysis	258,600	5,500	230,600	5,500	230,600	5,500			719,800	16,500	736,300
VI. OTHER COSTS											
A. Evaluations and Audits			45,000		30,000		55,000		130,000		130,000
B. Chief of Party, Institutional Contract, 3 yrs	235,500		235,400		235,400				706,300		706,300
C. U.S. Hire Personal Services Contract, 3 yrs.	108,000		108,000		108,000				324,000		324,000
D. Contingencies (7%)	189,200	49,100	126,600	41,500	72,800	47,000	12,600	27,000	401,200	164,600	565,800
Subtotal, Other Costs	532,700	49,100	515,000	41,500	446,200	47,000	67,600	27,000	1,561,500	164,600	1,726,100
PROJECT TOTAL	9,406,600	751,500	8,167,400	737,800	7,634,300	716,400	7,014,700	414,700	32,223,000	2,620,400	34,843,400

C. Implementation and Financing Methods

Input	Implementation Method	Financing Method	Amounts ($000)
1. BDIF			
FDIC Contract for TA + Trng.	Direct AID Contract	Direct Payment	$1,086
Commodities	Direct AID Contracts	Direct Payment	40
Bank Audits	Host Country Contracts	Reimbursement	243
2. FTC			
TA+Trng+Course Provision	Direct Contract	Direct Payment	722
FTC Operating+Course Costs	Cooperative Agreement	Reimbursement	639
Commodities	Direct L/Com	Direct Payment	80
3. ASOBAN			
TA+Trng Contract	Direct AID Contract	Direct Payment	346
Commodities	Direct AID Contracts	Direct Payment	47
4. Savings Mobilization			
TA contract	Direct AID Contract	Direct Payment	711
Training	Direct AID Contract	Direct Payment	12
5. Policy Development			
Contract for Seminars and Research	Direct AID Contract	Direct Payment	586
Technical Assistance	Direct AID Contracts	Direct Payment	107
Commodities	Direct AID Contracts	Direct Payment	27
6. Other Costs			
TA Chief of Party	Direct AID Contract	Direct Payment	706
Project Coordinator	Direct AID Contract	Direct Payment	324
Evaluations and Audits	Direct AID Contracts	Direct Payment	130
7. Contingencies	-	-	394
			$6,200

N.B. 1. A preference will be given in the contracting process for signing one AID service contract for the FTC, ASOBAN, Savings Mobilization and Policy components.

2. Arrangements will be made with IDEA under which AID will pay all dollar course delivery costs to the U.S. contractor and share local course delivery costs with IDEA.

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V. IMPLEMENTATION PLAN

A. Negotiating Status

In-depth discussions have been held with the principal organizations which this Project will assist and broad areas of understanding have been established.

1. Improvement of Financial Sector Regulations. Mission representatives and technical consultants have conducted a series of in-depth discussions with the President of the Central Bank and his staff concerning various aspects of establishing the BDIF. The President of the Central Bank has, in turn, gained the concensus of the Economic Cabinet that the BDIF and the Superintendency of Banks must be established quickly. The Minister of Planning and Coordination in formally requesting AID assistance in this area, has confirmed the Economic Cabinet's desire to proceed. Discussions have also been held with key private sector bankers who have expressed agreement with the Government's plans for the creation of a Superintendency and the BDIF.

2. Improvement of Private Sector ICI Operations. Mission representatives and technical consultants have had in-depth discussions with both IDEA and ASOBAN, as well as with individual bank managers concerning the establishment of the FTC. All parties are enthusiastic and are convinced that it will contribute substantially to increasing the efficiency of the sector. IDEA's request for assistance is included in Annex D.

Mission discussions with the Technical Committee of ASOBAN covered a number of new or improved service that ASOBAN might provide its members. The Technical Committee, in consultation with the members, decided to expand and improve the ASOBAN services in the areas described elsewhere in this Paper. ASOBAN has formally requested AID assistance in this effort. (Annex D).

FENACRE recently requested Mission assistance in expanding its savings mobilization efforts. The Mission took the opportunity to discuss its concerns about various aspects of the FENACRE system. An agreement to assist FENACRE grew out of these discussions and is described elsewhere in this Paper. The President of the Central Bank has also indicated his interest in investigating the feasibility of creating new capital market financial instruments.

3. Financial Sector Policy Development

The Mission has held three meetings with the Catholic University Institute for Socio-Economic Studies. The co-directors have indicated that the Institute is interested in participating in the Project by carrying out local research in support of the seminars. The contractor assisting the Mission with this component will subcontract for this research.

Meetings have also been held with ILDES, IBEE, IDEA, UDAPE, ASOBAN and IESE to explore the interest of each in organizing and sponsoring one or more seminars. Each is interested in participating in the Project.

USAID plans to sign three obligating agreements for the Project: a ProAg with the GOB Ministry of Planning and Coordination for the BDIF, savings mobilization and policy research and analysis components; and two cooperative agreements with IDEA and ASOBAN for the FTC and ASOBAN improvement components, respectively.

B. Responsibilities

1. The BCB. The President of the Central Bank will chair a quarterly meeting which will coordinate activities of donors active in the financial sector. Attendees will include the Resident

Representatives of the World Bank, the IMF, and the IDB, the USAID/Bolivia Mission Director, and project personnel. The Central Bank will also coordinate work on the development of new capital market financial instruments and participate in policy seminars.

2. Local Institutions. Project activities will support the programs of several autonomous institutions, including the BDIF, IDEA, ASOBAN, FENACRE, and Catholic University. Each institution will have responsibility to manage the activities in which it will be involved, working closely with technical assistance advisors and USAID.

3. USAID: USAID will monitor all project activities and ensure coordination among all Project participants and with other donors.

C. USAID Monitoring Plan.

The overall management of this Project will be the responsibility of the Mission's Private Sector Office. An on-board U.S. Direct Hire employee will manage the Project. He will be assisted by a full-time American Project Coordinator, to be hired with Project funds. This person will have senior bank management experience.

The PSC Project Coordinator will have principal responsibility for day to day monitoring of the Project. He/she will be available full time for project implementation and monitoring tasks.

The Mission will work closely with its contractors in all aspects of project implementation. Regular monitoring meetings will be held with each institution involved with the Project. Within the Mission, regular Project Committee meetings will be held to monitor the progress of the Project. Quarterly reviews of the Project will be held with the Mission Director. The relationship of this Project to financial sector projects of other donors will be reviewed in quarterly meetings chaired by the President of the Central Bank.

D. Procurement Plan.

1. Services

As indicated previously, an AID direct contract will be negotiated with the FDIC, without competition, for the provision of technical assistance and training to the BDIF.

The FTC will require TA and training services from a U.S. or Latin American institution or firm with bank training capacity. ASOBAN will require services from another U.S. or Latin American banking association. Consulting services will be required from a U.S. firm for the provision of assistance under the savings mobilization.and policy components. This firm will be authorized to negotiate subcontracts during the course of the Project with Bolivian and U.S. institutions (including universities) for the provision of research and seminar analysis/participation services.

USAID will issue one RFP for all services, except those to be provided by the FDIC, expressing a preference for signing one contract with a U.S. firm which will subcontract with other firms, institutes or universities for the provision of services described in the RFP. If such an arrangement can be negotiated, the main contractor would be asked to provide a chief of party for three years. However, in order to obtain services from the most appropriate sources the RFP will also allow interested contractors to bid on separate components should they wish to do so. In this case, one contractor would be hired for the Savings Mobilization and Policy components and be asked to provide a Chief of Party for those two components for two years.

The following language is suggested for the Action Memorandum to be sent to AA/LAC to approve the SFM Project and necessary contracting actions.

"Problem Your approval is required for the subject justification/waivers in order that the USAID/Bolivia Mission may initiate procurement procedures under the Strengthening Financial Markets (SFM) Project. Even though some of these waivers could be approved by the Mission Director, USAID/Bolivia requested they all be approved by the AA/LAC at the time of Project authorization.

"1. Justification for Other than Full and Open Competition

USAID/Bolivia has the need to acquire the services of the U.S. Federal Deposit Insurance Corporation (FDIC). Approval to contract directly with the FDIC is required because of FDIC's unique capability to provide technical assistance to help Bolivia establish a Deposit Insurance Fund.

"You can approve entering into contract negotiations utilizing less than full and open competition based on FAR 6.302-1(b)(1) i.e. 'when there is a reasonable basis to conclude that the Agency's minimum needs can only be satisfied by unique supplier or services available from only one source or only one supplier with unique capabilities.' Notice of the availability of this contract and intention to sign it with the FDIC will be published in the CBD.

"2. Nationality Waiver

A nationality waiver is required to allow USAID/Bolivia to include Code 941 country contractors in the competitive contracting process for the provision of technical services to help establish the Financial Training Center and strengthen the services of ASOBAN. Latin American contractors should be allowed to compete for the provision of these services in the interest of Project efficacy.

"HB 1, Supplement B, Section 5.D.10(a)(1)(e), allows a waiver of nationality in the following instance:

'Such other circumstances as are determined to be critical to the achievement of project activities.'

"You have authority under Sec. 5.B.4.C. of Ch.5 of HB 1B to approve nationality waivers up to $5.0 million.

"3. Waiver of Competition for Cooperative Agreement (CA) with ASOBAN and IDEA

Per HB13, Section 1.B.2.E.3. the approval of the AA/LAC is required to allow USAID/Bolivia to invite only the Instituto para el Desarrollo de Empresarios y Administradores (IDEA) and the Asociación de Bancos e Instituciones Financieras de Bolivia (ASOBAN) to submit Cooperative Agreement proposals under the SFM Project.

"The participation of IDEA and ASOBAN in the implementation of two components of the project is vital to the success and continuity of the Project upon termination of AID assistance. Both Bolivian organizations have an adequate knowledge of the SFM project goals and both possess the institutional capability required to successfully carry out Project activities. IDEA was selected as the most appropriate Bolivian institution to establish the Financial Training Center. ASOBAN is Bolivia's banking association.

"Recommendation That you approve the subject waivers/justification in order that USAID/Bolivia may procure services as specified above."

2. Commodities

The cost of the commodities to be purchased with Project funds is modest (US$234,000) and the procurement of the commodities will be simple. The furniture (US$20,000) and computers (US$85,500) will be purchased directly by the Mission, either as local shelf items or from the U.S. Funds for computer software (US$9,500) and library and research materials (US$37,000) will be included in the institutional contract(s) and will be purchased by the contractor(s).

E. Evaluations and Audits

An impact evaluation of the A&A Project is planned for the last quarter of CY 88. Since three of the SFM Project activities are continuations of the A&A Project activities, the results of the A&A evaluation will be useful to the SFM Project.

Two SFM mid-term evaluations and an impact evaluation are presently planned. The A&A impact evaluation and the first SFM mid-term evaluation will probably be carried out together.

The mid-term evaluations will assess progress towards the accomplishment of the overall Project purpose and suggest mid-term refinement, as necessary. They will be focused on answering specific project implementation questions. The impact evaluation will measure the attainment of the purpose indicators (EOPS) and other quantifiable objective measures.

The Mission will look for opportunities to carry out joint evaluations with the World Bank and the IDB which look at the impact of each donor's project on the financial system.

Bi-annual audits will be conducted of the entities involved in each of the Project's components

F. Schedule of Activities.

A schedule of critical events for each Component is presented below.

1. Contracting and Evaluation Events for All Components

-Draft terms of reference, PIO/Ts, RFPs, and CBD notices, for contracts	05/87
-Sign ProAg(s) and cooperative agreements with cooperating organizations	06/87
-Sign PIO/Ts for contracts	06/87
-Send cable to CBD for notices for contracts (RCO)	07/87
-Issue RFP for Contracts (RCO)	07/87
-Sign Contract with FDIC	07/87
-Long term FDIC TA starts	08/87
-Sign other Contract(s)	09/87
-Other long term TA persons start work	10/87
-Do first evaluation	09-10/88
-Do second evaluation	09-10/89
-Do first audit	11/89
-Do second audit	11/91
-Do impact evaluation	11-12/91

2. Improvement of Fiancial Sector Regulation: Key Events

-Initiate Central Bank reorganization	03/87
-Begin World Bank TA for establishment of Superintendency of Banks	03/87
-Begin Central Bank audits of 21 banks (Initial A&A funding)	05/87
-Draft of BDIF operating procedures (A&A funding, FDIC)	05/87
-Sign ProAg with Minister of Planning and Coordination	06/87
-Do in-depth profile of deposit base	06/87
-Select BDIF head and staff	06/87
-Sign contract with FDIC, start short term FDIC TA	07/87
-Create/select BDIF Board of Directors	07/87
-Present draft of new banking law, acceptable to GOB and ASOBAN (A&A funds)	07/87
-Send draft law to IMF for review	07/87
-Long term FDIC TA arrives	08/87
-Congress considers new banking law	08/87
-Legally incorporate BDIF and start operations	09/87
-Publish external audit reports of individual banks(A&A)	09/87
-Start in-depth study of audit findings	09/87
-IDB starts TA to Central Bank Development Department	10/87
-Determine BDIF membership	12/87
-Start BDIF bank interventions, as required	01/88
-Start AID financed training	01/88
-Do 1st evaluation	09-10/88
-Do second evaluation	09-10/89
-Do impact evaluation	04/91

3. <u>Improvement of Private Sector ICI Operations - Financial Training Center: Key Events</u>

-Sign ProAg or letter of understanding with IDEA	06/87
-Hire local IDEA/FTC personnel	07/87
-ASOBAN appoints ad hoc academic advisory board	08/87
-Begin planning of FTC structure and curriculum	08/87
-Begin development of data file on sources of banking seminars, local and foreign consultants and instructors to serve as FTC short-term teachers	08/87
-Start plans for Library	09/87
-Have first meeting of academic advisory board and formally install it, present and discuss initial curricula ideas	09/87
-Determine specific accounting and MIS requirement for FTC	09/87
-Determine initial course schedule	09/87
-Survey market for dates, places	09/87
-Contract signed	10/87
-Long term TA arrives	10/87
-Based on terms of contract, determine pricing of seminars, fix dates and places and start promotional campaign	10/87
-Deliver two seminars (1 middle Level - 1 lower Level)	11/87
-Start needs analysis process (on-going), validate results of initial needs analysis	11/87
-Conduct first "train the trainer" seminar for IDEA instructors and other local instructors and consultants	11/87
-Deliver first senior level seminar	12/87
-Start planning of first financial workshop	12/87
-Deliver three seminars (1SL-1ML-1LL)	02/88
-Deliver three seminars (1SL-1ML-1LL)	03/88
-Deliver three seminars (2ML-1LL)	04/88
-Conduct first financial workshop on savings movilization	04/88

-Conduct three seminars (1ML-2LL)	05/88
-Start preparation of second financial workshop	05/88
-Conduct three seminars (1S-1M-1L)	05/88
-Conduct three seminars (2ML-1LL)	06/88
-Continue preparation of second financial workshop	06/88
-Deliver two seminars (1ML-1LL)	06/88
-Conduct second financial workshop	06/88
-Do first evaluation	09-10/88
-Deliver 8 seminars (2SL-3SM-3LL)	3rd qtr/88
-Conduct 1 financial workshop	3rd qtr/88
-Deliver 6 seminars (2SL-2ML-2LL)	4th qtr/88
-Conduct 1 financial workshop	4th qtr/88
-Deliver 6 seminars (1SL-3ML-2LL)	1st qtr/89
-Conduct 1 financial workshop	1st qtr/89
-Do second evaluation	09-10/89
-Deliver 6 seminars (1SL-2ML-3LL)	2nd qtr/89
-Conduct 1 financial seminar	2nd qtr/89
-Deliver 1 senior level seminar, 4 middle level seminars, and 3 lower level seminars. Delivery of seminars to be done mainly by local consutlants, previously trained as instructors by the FTC	2nd sem/89
-Conduct 2 financial workshops	2nd sem/89
-Deliver 2 senior level seminars, 4 middle level seminars, and 4 lower level seminars	1st sem/90
-Conduct 2 financial workshops	1st sem/90
-Achieve full self-sufficiency for course development and course delivery	1st sem/90
-Do impact evaluation	11-12/91

4. <u>Improvement of Private Sector ICI Operations: Improvement of the Services of ASOBAN</u>

-Sign ProAg or letter of understanding with ASOBAN	06/87
-Start hiring of new ASOBAN staff	06/87
-Start research for obtaining books and materials for library, materials for the Staff Selection Unit	07/87
-Start procurement of equipment and computers	07/87
-Define functions/responsibilities of Economics and Legal Unit	07/87
-Begin detailed planning of new services and functions	08/87
-Determine functional specifications for different data bases and check clearing	08/87
-Establish agreements with banks on procedures, regulations, deadlines, of check clearing function	08/87
-Place orders for books and materials for library as well as for Staff Selection Unit	08/87
-Contract development of required software as per functional specifications, Phase I	09/87
-Produce first professional reports from Economics and Legal Unit	09/87
-Visit Banking Associations in Santiago and Buenos Aires	09/87
-Staff Selecton Unit to begin operations	09/87
-Open Library for internal consultation	10/87
-Inititate testing of software for central information	10/87
-Test software for data base of bank's staff	10/87
-Open Library for external consultation	11/87
-Initiate testing of software for check clearing	11/87
-Complete operational procedures of check clearing function	11/87
-Complete operational procedures of central information function, Phase I	11/87
-Initiate operations of Central Information Unit on a pilot basis, Phase I	12/87

-Launch first publication of book/article of local authors	12/87
-Start use of data base with banks' staff	12/87
-Initiate operations of Check Clearing Unit on a pilot basis	01/88
-Start operations of Central Information Unit, Phase I	02/88
-Contract development of required software for Central Information (Phase II) as per functional specifications	02/88
-Start operations of Check Clearing Unit	03/88
-Produce second series of reports from Economics and Legal Unit	03/88
-Test software for Central Information, Phase II	04/88
-Complete operational procedures of Central Information Functions, Phase II	04/88
-Pilot test operations of Central Information, Phase II	05/88
-Plan activities for second year	06/88
-Search market for acquisition of new books, manuals, and publications for library	3rd qtr/88
-Start operations of Central Information, Phase II	3rd qtr/88
-Do 1st evaluation	09-10/88
-Place order for new books and materials for Library	4th qtr/88
-Publish thrid series of reports from Economics and Legal Unit	4th qtr/88
-Visit Banking Associations in Colombia and Mexico	1st qtr/89
-Analyse with banks, enhancements for Central Information Unit, Phase III	1st qtr/89
-Publish forth series of reports from the Economics and Legal Units	2nd qtr/89
-Contract software changes and modifications for data bases to include new files	2nd qtr/89
-Plan activities for third year	2nd qtr/89
-Finish enhacements for Central Information Unit, Phase III 2nd sem/89	

-Determine with affiliates upgrading of check clearing function	2nd sem/89
-Acquire new material for Library	2nd sem/89
-Publish fith series of reports from the Economics and Legal Units	2nd sem/89
-Do second evaluation	09-10/89
-Attend FELABAN annual conference	1st qtr/90
-Analyze potential new services	1st qtr/90
-Publish sixth series of reports from the Economics and Legal Units	1st qtr/90
-Conduct end-of-project third party evaluation	1st qtr/90
-Do impact evaluation	11-12/91

5. Improvement of Private Sector ICI Operations: Savings Mobilization and Capital Markets Development

a. Savings Mobilization Activities

-Sign letter of understanding with FENACRE	07/87
-Long term TA starts work with FENACRE	10/87
-Plan savings mobilization courses/workshops with IDEA/FTC	11/87
-Plan management audit of FENACRE by contractor	11/87
-Savings mobilization workshops in various cities begin	01/88
-Begin FENACRE short term TA	01/88
-Start management audit	01/88
-Start market reserch studies	03/87
-Prepare first marketing strategy for individual credit union	06/87
-Do first evaluation	09-10/88
-Do second evaluation	09-10/89
-Completion of long term TA	10/89

-Do impact evaluation	11-12/91

b. <u>Financial and Capital Market Development Activities</u>

-Financial market assessment and selection of activities to be supported	11-12/87
-Short term technical assistance started	02/88

6. <u>Improvement of Financial Sector Policy Development</u>

-Sign ProAg with Minister of Planning and Coordination	06/87
-Discuss with interested parties re seminar topics	07/87
-Sign Contract	09/87
-Sign sub-contract with IESE for first research	10/87
-Initiate baseline study of policies and attitudes	10/87
-Sign first sub-contract with expatriat researchers	10/87
-Sign first sub-contract for US masters thesis work	12/87
-Plan for informal luncheons/workshops	12/87
-Hold first luncheon	01/88
-Review final draft of all research for first seminar	01/88
-Issue invitations, finalize all logistics for first seminar	01/88
-Hold first seminar	02/88
-Schedule first follow up activities	02/88

-An indefinite number of informal luncheons/seminars each year
-Four sets of research and four seminars each year
-Follow up activities, as needed

-Do first evaluation	09-10/88

-Do second evaluation	09-10/89
-Do impact evaluation	11-12/91

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VI. PROJECT ANALYSES

A. Technical Analyses

1. Bolivian Deposit Insurance Fund

The Project Development Team examined six main issues regarding the establishment of the BDIF: alternative strategies concerning whether and when to establish the Fund; the BDIF's relationship to the Superintendency; mandatory versus voluntary membership; Fund capitalization, insurance coverage limits and whether to insure the maintenance of value of dollar deposits; and the powers of the GOB in intervening banks.

a. Alternatives/Timing

Given the realities of the Bolivian financial system as it exists today, the small number of banks in the country, and the *de facto* position of the Central Bank as "lender of last resort" and guarantor of all deposits, there appears to be only two alternatives to the establishment of a separate deposit insurance fund. One alternative would be to maintain the status quo and have the Central Bank or the Superintendency of Banks handle all future bank interventions without the support of a separate fund. A second alternative would be to plan to create a deposit insurance fund but only after the banking system stabilizes. Either alternative would be more expensive because 100 percent of deposits would be guaranteed by the Central Bank until a deposit insurance fund were created, whereas the Fund will insure only eligible deposits and each depositor only up to a specific amount. In addition, under either alternative the entire burden of any bank liquidation would fall on the Central Bank or the Superintendency, whereas the Fund will receive substantial income from the assessments of its members to help finance bank intervention measures or a bank liquidation.

It is conceivable that the Central Bank or Superintendency could bring the cost of this alternative closer to that of an independent Fund by formally announcing limited insurance of deposits, similar to the BDIF, and collecting assessments directly from the financial institutions. Even if this were done, the BDIF would still have a distinct advantage in terms of both cost and efficiency. This is so because an independent Fund dedicated to the early intervention and support of troubled institutions will be able to intervene and assist banks in a more timely, professional, efficient and less costly way than the Central Bank or the Superintendency. The Fund will be able to take a variety of actions appropriate to a specific bank's problems as early as it deems necessary. In this way, banks' problems can be addressed earlier and more appropriately than would be the case should the Superintendency be forced to wait until a situation got so bad that a full intervention and liquidation were necessary. It should be recalled again that the Fund's focus will be on assisting banks to resolve liquidity problems while the Superintendency's will be on bank regulation. Experience in other countries has shown that, without the discipline of an independent Fund, attempts by government authorities to intervene banks with serious problems are often handled inefficiently because of political pressures, bureaucratic inefficiency and lack of skilled personnel.

The creation of the BDIF will complement and complete other actions being taken in 1987 to deal with Bolivia's financial sector crisis: external audits, revision of the banking law, strengthening of the BCB and creation of a Superintendency of Banks. It is recommended that the BDIF be organized on September 1 and that the private banks be strongly encouraged to join by December 31. The banks will not be required to fully meet the eligibility criteria before joining but will have to show a good-faith effort to work toward meeting the criteria. After December 31, the BDIF will work with the banks as they take appropriate corrective actions.

An alternative way of dealing with the problems of the private banks would be to require that the banks totally resolve their problems and fully meet the entrance standards before joining the BDIF. This procedure might have the advantage of more strongly motivating the banks to take corrective actions so they would be allowed to join the BDIF. However, there are disadvantages which make this alternative undesirable. First, it would leave some banks outside the BDIF for relatively long periods of time. If such uninsured banks failed and had to be liquidated, the Central Bank would probably be forced to protect all of the depositors, which would be more costly than dealing with a failed bank which is a member of the BDIF. Second, under this scenario, the Central Bank or the Superintendency might have to intervene a number of banks without the benefit of the expertise of the BDIF.

b. Relationship to the Superintendency. The BDIF will be more effective as a separate entity than as part of either the Superintendency or the Central Bank. Its independence is important because:

- The development and maintenance of the expertise required to properly intervene banks must have top priority. If the BDIF were part of another agency, its objectives would, at best, be diluted by becoming part of the broader objectives of the other agency. At worst, the BDIF's objectives would be subordinated to the objectives of the other agency. Over a period of time, the BDIF could possibly find that it was not receiving the resources necessary to function properly.

- The BDIF needs to be isolated as much as possible from political influences. An independent BDIF whose sole role is to intervene banks would be less susceptible to political influence than a BDIF which was a department of the Superintendency or the Central Bank.

- An independent BDIF can be designed to have the powers needed to act quickly and decisively to intervene a bank efficiently. It would be more difficult for the BDIF to exercise such powers properly if it were part of another agency where its activities would be subject to the oversight of managers who might have other priorities.

- Lastly, although broadly speaking both the Superintendency and the Fund will have regulatory powers, the wider scope of the Fund's intervention methods, and its readiness to act as soon as problems are detected, will often lead a bank's management to request, and cooperate with, Fund assistance measures, whereas the Superintendency will inevitably be perceived as the banking system's ultimate authority and disciplinarian.

Close cooperation between the BDIF and the Superintendency should be reasonably assured by:

- Having the Superintendent or the Deputy Superintendent be a member of the Board of Directors of the BDIF, and possibly its Chairman.

- Requiring that the BDIF have access to all of the Superintendency's examination reports, audit reports, and correspondence relating to the financial condition of the members banks, and vice versa.

- Establishing procedures whereby staff members of both the BDIF and the Superintendency will participate in all meetings with bankers relating to supervisory or intervention issues.

c. <u>Mandatory vs. Voluntary Membership in BDIF.</u> Given the small number of banks in the Bolivian financial system, the <u>de facto</u> responsibility the Central Bank has for 100 percent of the deposits in all banks in the system and the major function of the BDIF as regulator within the financial system, it is essential to the success of the BDIF that it have the membership of all the private banks in the system.

To gain the initial membership of all private banks which wish to continue operating, as well as to be consistent with the Government's desire to have a deregulated, market-oriented financial system, it is believed that membership in the BDIF should at least appear to be voluntary. Although most bankers surveyed indicated a desire to join a deposit insurance fund, which they saw as a necessary addition to the financial system, and although others felt competitive pressures would force them to join the Fund, given the realities of the current problems within the Bolivian banking system, it is not realistic to assume that all banks will, in fact, volunteer to subject themselves to a new form of regulation and increased expenses without strong incentives.

A decision by any of the larger banks to not join the Fund would create three serious problems for the Central Bank and the Fund which might better be avoided. First, banks which do not join the Fund will not contribute to the Fund's operating costs and reserves. The Fund needs assessments from all the banks for all deposits to make it financially viable. Second, it would be most difficult politically to allow depositors in a failed, uninsured institution to actually lose their funds. Third, the legal authorities and staff expertise of the BDIF would not be available for assistance to intervene any non-member financial institutions.

Consequently, the GOB has agreed to put in place as strong a set of incentives as necessary to "encourage" banks to become members of the BDIF. These could include:

- Limiting to BDIF members the ability to borrow from the Central Bank.
- Limiting to BDIF members the ability to obtain refinancing for development loans.
- Limiting to BDIF members the ability to participate in any future Central Bank inter-bank market for excess liquidity.

The strongest position that the Central Bank will take, if necessary, regarding membership in the insurance fund will be to make a public statement that the Central Bank does not support, or guarantee, any depositor's position in any Bolivian bank which is not a member of the BDIF.

d. Fund Capitalization. There is no reliable way to calculate the appropriate reserves that a deposit insurance fund should maintain to be able to handle potential losses which might occur in intervening its member banks. The actuarial rules that are used by other types of insurance companies simply do not apply in the case of financial institutions. The amount of money needed to intervene a bank varies in each case, depending upon the size, condition, management situation and intervening method used. In some cases, initial cash infusions by the BDIF may in fact be repaid in a relatively short time. In other cases, cash outlays by the BDIF can be kept to a minimum by the use of notes and guarantees. On the other hand, other cases may call for sizable cash outlays which are not recovered for long periods of time, and sometimes not in their entirety.

In the United States, the net worth of the FDIC equals about 0.007 of the total deposits of its member banks. However, the FDIC is a mature fund, having been in existence for over 50 years. Its risk is spread over approximately 14,500 banks. In addition, the U.S. banking system, while experiencing serious problems in the agriculture and energy sectors, is essentially sound.

It is particularly difficult in Bolivia to establish a target level for the Bolivian Deposit Insurance Fund because:

- The exact condition of the private banks will not be known until the results of the in-depth, external audit by the Central Bank are received in August of this year. Substantial outlays by the BDIF might well be required to intervene a number of banks immediately after establishing the BDIF.

- The banking system in Bolivia is growing at a rapid pace, particularly in the area of gathering new deposits. This increases the potential risks to the new Fund and makes it doubly important that the Fund's reserves reach a high level as quickly as possible.

Because of these uncertainties, no specific level of insurance reserves for the Fund can be recommended at this time. Rather, the goal should be to accumulate reserves rapidly. After the banking situation and the Fund itself have stabilized, the desired level of insurance reserves in relation to total deposits of member institutions can be established.

The cash projections presented in the Financial Analysis section of this report show that the Fund will grow fairly rapidly in relation to projected total bank deposits. The 2 percent initial assessment rate for the member banks is large in relation to rates paid in other countries such as the U.S. and Spain, but given the large interest rate spreads in Bolivia, the rate is considered acceptable. It can be phased down as local interest spreads approach international levels. The projected size of the Fund looks large when compared to the FDIC. However, the cash flow projection does not contain any estimated outlays incurred to intervene banks even though it is almost certain that such outlays will occur. As stated earlier, such outlays are very difficult to estimate. Inasmuch as the Central Bank will pay 50 percent of the Fund's costs of any bank intervention actions during at least its first three years, or provide it will be a sizeable initial capitalization loan, the impact of such losses on the Fund's reserves will not be as great.

e. Deposit Insurance Coverage. The BDIF will provide insurance to depositors which will guarantee recovery of funds deposited in any failed financial institution which is a member of the Fund. Necessarily, this insurance shall have a maximum limit for coverage on a per depositor basis, otherwise such a system would imply a limitless guarantee and could only be provided as a direct commitment from the Central Bank.

Normally, insurance limits within the various deposit insurance systems currently in effect around the world are set at levels which will provide full coverage for the majority of depositors of the particular banking system. In the U.S., this limit has risen over the years to its current level of $100,000 per depositor. In the case of Bolivia, a number of factors complicate the establishment of an exact insurance limit at this time.

1) The Central Bank currently lacks detailed information from the banks regarding actual make-up of the deposit base. In order to accurately determine an insurance limit which covers the majority of depositors, a market review of the actual number of depositors in each bank with their corresponding aggregate deposit balances for various deposit levels should be prepared.

2) Determination of an insurance limit in Bolivia is complicated by the concentration of short-term deposits within the banking system, and the fact that almost 70 percent of the total deposit base consists of dollar, or dollar-equivalent, deposits.

3) There is a perceived expectation among the depositors that all dollar deposits are guaranteed to be withdrawable in dollars. This situation complicates the creation of a deposit insurance scheme, because if this factor is incorporated into the Fund it would effectively change from pure deposit insurance into an exchange rate guarantee fund as well.

Based upon the data that has been gathered to date, and taking into consideration income levels in Bolivia, it is believed that an initial deposit insurance limit could be established at Bs20,000 (US$10,000), whether deposits are in dollars or bolivianos. Before the Fund begins operations, a thorough study of the deposit structure of commercial banks will be made, and an insurance limit will be set. This study will also enable the Fund to define "deposits" for the purpose of extending insurance. It is important to realize that deposit insurance limits can be increased over time if such increases reflect corresponding increases in the average deposit level within the system. However, once a limit is established, it will be politically impossible to lower it.

The boliviano equivalents of dollar deposits, up to the Bs20,000 ceiling, will be determined at the time of deposit, and only that amount will be covered by the insurance. Payments will be made in bolivianos only, and only the amount deposited at the exchange rate prevailing at the time the deposits are made, plus accrued interest, will be paid to depositors.

Given the high percentage of dollar and dollar maintenance of value bolivianos currently deposited in banks, consideration was given to the possibility of insuring the maintenance of value of such deposits (either by paying out dollar deposits in dollars in case of a bank failure or paying out the dollar value of dollar or dollar-tied boliviano deposits at the rate of exchange in effect on the day of the insurance payment). The financial system and the economy are currently heavily dollarized as a result of the prolonged chaos created by the previous Government, despite the fact that the N.E.P. has succeeded admirably in stabilizing the economy for over a year. Dollar depositors are currently attracted to (and from within) Bolivia by the extraordinarily high deposit interest rates available here - up to 10 points above international levels. This added interest, along with the Bolivian bank's (not the GOB's) guarantee that deposits will be returned in dollars, compensates, in the mind of depositors, for the risk inherent in depositing funds in Bolivia. These deposits are "hot", however, and could leave Bolivia as fast as they arrived if risk perceptions change. The high interest rates paid on them also are a factor in the country's currently extremely high real interest rates on loans.

A policy of insuring the maintenance of value of dollar deposits could have several disadvantages. First, it would put an additional risk burden on the BDIF which will already have a sufficient challenge maintaining its financial viability just protecting deposits as envisaged, even with its reserves invested in dollar instruments.

Second, such a policy could make more permanent the market's current bias toward dollar deposits. In the long run, as confidence in the economy increases, it would be both natural and desirable for the Bolivian financial system to deal much less in dollars for domestic transactions.

Third, the insurance fee for exchange rate coverage would, most likely, have to be high (e.g. an additional 2 percent to 4 percent). This additional charge could not be fully passed on to borrowers and, most likely, would result in less net interest paid to depositors. A lower net spread could induce some depositors to move their dollars elsewhere if they were to perceive that the continuing country risk outweighed their reduced interest rate gain in Bolivia. Furthermore, the cost of the deposits to the banks would remain high, a factor which would continue to impede the reduction of Bolivian interest rates to more normal international levels.

Due to these factors, it has been decided that the BDIF will not initially attempt to insure deposits for exchange rate risk. However, some GOB authorities and bankers feel that the possibility of attempting to set up a separate insurance fund under the BDIF to insure against exchange rate risk should be explored. The reserves for such insurance could be kept separately from the Fund's normal reserves, and if depleted, direct BCB payments might be made to depositors rather than endanger the Fund's normal insurance program. It has been agreed to study the pros and cons of offering additional insurance coverage as soon as practicable. In the event that additional analysis shows that dollar deposit can and should be covered by the Fund, dollar deposits will be incorporated into the Fund at that time.

f. GOB Intervention Powers. The financial sector in Bolivia has serious problems in the areas of inadequate government supervision, the weakened condition of the banks, and structural weaknesses in the economy. The SFM Project and other donor efforts will address these inter-related problems on a coordinated basis. Each individual component of the Project is difficult in its own right. Moreoever, the success of the overall Project depends on the successful completion of the individual components in a fairly short period of time.

With respect to the Bolivian Deposit Insurance Fund, there are a number of good reasons for supporting its creation, including the fact that it is strongly endorsed by the Government. However, there are also potential barriers to its successful operation. These barriers have been satisfactorily addressed by the design features of the Fund, or will be addressed by the successful initiation of other components of the SFM Project.

There is one very important issue that cannot be dealt with by any of the usual methods and yet has serious implications for the success of this component. That issue is the ability of the Government to decisively and efficiently intervene banks with serious problems. The issue has been highlighted by the recent Central Bank intervention of Banco de Crédito Oruro.

The Central Bank became aware in February 1987 that the Banco de Crédito Oruro was insolvent and that management probably was engaging in fraudulent activities on a large scale. On March 20, the Central Bank declared an intervention of the Bank, but it took almost three weeks to gain access to it. Bank management, initially opposed the intervention on legal grounds. Then a majority of the Board of the Banco de Crédito Oruro suspended its Chairman and the Chief Executive Officer, ordered that criminal charges against these two persons be filed, and commissioned an audit to document responsibilities for the bank's illegal activities.

On the positive side, the banks have learned that this Government, unlike previous administrations, will not tolerate unsound banking practices. In fact, banks are now solidly behind a laudable plan to revise the banking law so they will have clear rules with which to deal. On the other hand, the fact remains that as of mid April the Central Bank still had not been able to force the Banco de Crédito Oruro to let it begin the full intervention process, and this clearly is unacceptable. The Government, and banking authorities, must be able to move quickly to address problems and protect the public's interest. The Banco de Crédito Oruro situation has allowed the GOB to demonstrate its political will to clean up the banking system, and that has had a salutory effect in and of itself. But unless Government authorities are able to translate decisions into actions, it will be very difficult to take the actions necessary to improve Bolivia's financial system in the future. The Government must maintain its firm policies with respect to the financial sector and ensure that the new banking law, or supreme decree, gives the Government and all banking authorities, sufficient powers. If, in fact, the Government cannot, for either administrative, legal or political reasons, effectively intervene a financial institution, the creation of a deposit insurance scheme would not be worthwhile.

In conclusion, the creation of a Bolivian Deposit Insurance Fund as a part of the overall Strengthening of Financial Markets Project is recommended if the conditions precedent are met and the issues raised by the intervention of the Banco de Crédito Oruro are satisfactorily resolved.

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2. Financial Training Center

This section will address three topics: ICI personnel training requirements, sources of training expertise, and training course content.

a. ICI Personnel Training Requirements

Training programs should be designed to respond to specific needs, not merely to react to a problem. Taking this into consideration, an intensive analysis of the training needs of Bolivian bankers was conducted as part of the Project development process. Presidents, vice presidents, and managers of 12 major, medium, and small banks were interviewed in a structured fashion during the intensive review. Simultaneously, observations of their operational practices and procedures were made.

The structured interviews covered such subjects as problems encountered, bank operations, improvements that could be made in the banks, customer service practices, and felt needs for acquiring additional skills or knowledge. Overall, the results of these analyses revealed the crises these financial institutions are going through and the need to address training needs as soon as possible.

The following are the major deficiencies noted, classified by banking areas:

i) Credit

In the opinion of most executives interviewed, the credit function is one of the most important aspects within the management of the banks that requires urgent and special attention.

One of the main reasons for the poor quality of the banks' portfolios is the lack of structured credit processes within financial institutions. Fundamental aspects of a credit process, such as target market definitions, credit policies and procedures, risk assessment, and thorough financial statement analysis are inadequate in most cases. There is an urgent need for strong financial analysis skills and industry knowledge. Given the excessive bad loan volumes in Bolivian banks, credit officers from all banking institutions must also be thoroughly familiar with remedial measures to protect the assets of their financial institutions.

There seem to be very few professional credit officers employed in each bank, and senior full-time credit officers are virtually non-existent. Given the scarcity of professionals in the financial market, there is a high turnover among banks. The problem is compounded because the formation of account and credit officers is done through on-the-job-training, and rotation and promotional opportunities are based on seniority rather than merit.

ii) Marketing

Financial marketing is one of the most important tools in today's highly competitive banking environment. It is a function that is frequently ignored, as well as misunderstood. Most Bolivian banking executives do not differentiate between marketing and sales. Some define marketing as their efforts in advertising. Most Bolivian financial institutions lack the ability to analyze market situations, as well as the ability to formulate and implement marketing strategies.

Product development and product management are not widely understood in the Bolivian financial industry, and only a few banking products exist with virtually no differentiation among them. The concept of product profitability is not commonly held and many bankers do not know whether an individual product is profitable or not. Market research is rare and often carried out by advertising agencies, with little supervision from bankers due to their lack of knowledge of how to undertake market research.

The sales process, although far from being adequate, is probably the one marketing area that attracts the most attention from bank executives. Efforts are being made in some institutions to develop sales skills among account officers. It is obvious that there are too few bank employees facing the customer and too many in the back office.

All bankers interviewed agreed with the need to address these marketing issues and considered that professional seminars on modern marketing techniques would help in the revitalization process of the Bolivian banking system.

iii) Management and Human Resources

This area presents serious deficiencies in the opinion of the executives interviewed. Supervisory skills are weak among mid-level executives. For example, delegation, problem analysis and decision making are skills that need attention in most financial institutions. Career planning is non-existent, and opportunities for advancement are rather limited.

vi) Financial Control and Management Information Systems

Serious weakness in these fields were identified both during interviews and also through the analysis of reports from banks. Most financial reports are prepared with great delays, and no critical reviews are conducted once reports are received. Although most institutions have incorporated a budget process as part of their planning activities, they are modified throughout the year, rather than incorporated into quarterly forecasts.

Management information systems that incorporate concepts such as the existence of profit centers, cost centers, allocations of overhead expenses, account profitability reports, product profitability reports, unit costs, etc. have not been implemented in most Bolivian banks. These concepts would enable banks to determine and measure the performance of individual units, performance of customers and account officers, and the profitability of individual products.

v) Trade Finance

Due to the isolation of Bolivia from the financial markets of the world and the economic crisis of the past few years, trade volume has declined. The know-how to handle trade transactions within financial institutions has almost disappeared. Banks, in response to the improving economy, urgently need to revamp their international trade departments. Trade finance personnel need to know how to use letters of credit (import and export), make collections, and use non-conventional international trade financing methods (barter, counterbarter, etc.).

vi) Services Management (Operations)

Although few of the executives interviewed mentioned this area as one of special concern, observation of operational processes, both front-end and back-end, revealed significant deficiencies. There is a clear need to rationalize most operational processes, improve work flows and automate labor-intensive tasks. Despite the fact that most banks have installed computers, many processes are done manually, and service is slow. The development of electronic banking oriented towards customers (ATMs, cash management systems, CRTs in customers' offices, etc.) is quite retarded in Bolivia. Further automation is needed, but more important than this is the need to prepare bank personnel to manage technological change.

vii) Treasury (assets and liability) Management

Although not mentioned at all by any of the executives interviewed, enormous opportunities could be tapped if Bolivian financial institutions upgraded their knowledge in the field of assets and liabilities management. Most activities executed at this time relate only to the managing of a bank's financial position and spot foreign exchange transactions. The concept of a treasury function as a profit center does not exist, despite the multiple possibilities offered by the liberalization of the foreign exchange market.

viii) Investment Bank/Capital Market Products

These types of products are not present on the menus of Bolivian financial institutions. Opportunities exist in the market for the use of merger and acquisition instruments, debt equity swaps, and other financial instruments. With the anticipated approval of a stock exchange in La Paz, opportunities will be even greater. Bolivian bankers, particularly senior managers, must begin thinking about more complex banking activities so they can begin to profit from new financial opportunities as they arise.

ix) Strategic Planning

The need for strategic planning was recognized by some bankers when asked about it. Most financial institutions are in desperate need of a strategic plan. Strategic objectives are not defined in many cases and seldom incorporated in bank planning.

b. Sources of Training Expertise

Training programs specially geared to meet the needs of banks' executives are not currently offered in Bolivia. Bolivian university programs were not analyzed in depth, but in most countries there exists a gap between the programs offered by the universities and the educational requirements of the financial institutions. Due to this fact, banks and other financial entities have developed their own training programs and facilities. While the IDEA and IBBE programs are of excellent quality, they have not been designed to respond to the specific needs of Bolivian bankers. With the exception of several seminars on managerial and supervisory practices, the IDEA and IBEE courses are not readily adaptable for use as part of the curricula of the FTC.

Given the need for employee training, some banks have sent their senior or fast-rising officers overseas for training, but this is expensive. The FTC is designed to provide comprehensive training to key professional bank employees which can have a synergistic effect on bank operations. To provide such training, the FTC will require outside assistance. Such assistance is available from the following institutions:

o Citibank, NA

Citibank operates bank training centers in Sao Paulo, Brazil; Buenos Aires, Argentina; and Pompano Beach, Florida.

o Banco Internacional de Colombia

BINT operates a bank training center in Bogota, Colombia.

o Escuela de Administración y Finanzas

EAFTI, based in Medellin, Colombia, offers specialized banking seminars.

o Instituto de Estudios Bancarios, Chile

Based in Santiago, this Institute offers several specialized banking seminars.

- Sistema Inc., Puerto Rico

  Based in San Juan, Puerto Rico, this corporation specializes in productivity, corporate planning, and branch rationalization seminars.

c. Training Course Content

Based on the training needs assessment, training will be carried out in the following areas:

Credit assessment and management, marketing, management of human resources, financial controls management information systems, trade finance, services management (operations), treasury management, and strategic planning.

The design of course offerings and training formats will be flexible and relevant to the needs identified. Course materials and corresponding teaching methodologies will be formulated for the three target groups identified earlier (senior, middle, operational), each addressing its own needs. With limited exceptions, all seminars will be for a three- to four-day period and repeated at least once per year. A total of 68 seminars will be held over the life of the Project. A description of the seminars to be given follows.

i) Senior Level Management Seminars

This curriculum will include seminars for senior executives, vice presidents, presidents and directors of the financial institutions. The core curriculum will consist of seminars in advanced credit management, strategic planning, risk management, management information systems, and managing technology. The following seminars will be aimed at this target group:

*<u>Advanced Credit Analysis and Management Seminars</u>

This seminar will include topics such as: macroeconomic indicators, country risk assessment, country risk management, industry analysis, corporate finance theory and practice, portfolio management, early problem recognition, remedial management, and liquidation analysis.

*<u>Strategic Planning Seminars (Competitive Strategy)</u>

This seminar will prepare senior executives with management responsibilities to develop strategic plans and to assess the risks of choosing/implementing a given strategy. The course will help senior executives define their businesses in terms of products and market segments, and translate industry and bank analyses into competitive business strategies which address such issues as overall cost leadership, product differentiation, and marketing focus.

*<u>Risk Management Seminars</u>

This course will familiarize participants with the inherent risks in treasury management, focusing on non-conventional foreign exchange and money market procedures.

*<u>Savings Mobilization</u>

See discussion in Section III.B.2.c.

*Managing Technology and Management Information Systems Seminars

This course will provide familiarity with technical concepts and their resulting impact on business.

ii) Middle Level Management Seminars

Middle Level management seminars will be aimed at heads of departments and divisions in financial institutions. The curriculum will include seminars in areas such as: intermediate credit management, problem loans, marketing concepts and tactics, treasury management, human resources management, operations simulations, managing productivity, intermediate trade finance, and financial control/analysis. The following are the seminars contemplated for this target group:

*Intermediate Credit

Participants will reinforce basic credit knowledge utilizing a practical case study approach, role playing, negotiations, and intensive group work.

*Problem Loans

This seminar will help develop the necessary skills and remedial knowledge to protect the bank's assets in situations where many borrowers are experiencing problems.

*Marketing Concepts

This seminar will address the banks' increasing needs in the area of marketing/product management. It will prepare participants to make accurate strategic decisions regarding the administration of their bank's products.

*Treasury Management

The "Bourse" (a simulation game) will provide a solid understanding of treasury concepts, transactions, management and related risks.

*Human Resources Workshop

Participants will upgrade their skills in personnel management.

*Bank Operations Simulation Game

This course provides managers with the necessary tools and technical knowledge to ensure that the operational costs of running a unit/branch/group are kept to a minimum.

*Managing Productivity

Participants will sharpen their managerial skills, emphasizing productivity improvement measures through the use of quantitative approaches to problem solving.

*Intermediate Trade Finance

This course will provide middle level managers with the ability to identify trade-related revenue opportunities as well as to structure and market trade-related services.

*Financial Control and Analysis

This course will develop and sharpen the skills needed for assessment of business conditions. The course will also help improve the quality of financial information used within banks.

Rural Credit Delivery

Participants will analyze the importance of expanding bank services to rural areas and methods for working in rural areas.

iii) Operating Level Management Seminars

This curriculum will include seminars for first line supervisors (experienced as well as recently promoted) and heads of small units or departments of financial institutions. The core curriculum will consist of seminars in such topics as basic credit, sales skills, basic treasury management, developing management skills, basic technological concepts, services management, basic trade finance, and basic financial control.

*Basic Credit Analyses and Management

The objective of this seminar is to teach basic credit analysis and management principles. It will include instruction in analytical and marketing skills necessary to function as credit trainees, analysts, and junior account officers.

*Sales Skills

This course will provide participants with the skills and tools necessary to improve interpersonal relationships by demonstrating effective fundamental skills for calling on clients.

*Basic Treasury Operations

This course will help participants understand fundamental treasury management concepts through a series of lectures and exercises.

*Developing Management Skills

Participants will learn the basic and fundamental skills needed to manage people and tasks. The program will focus on supervisor - subordinate relationships.

*Basic Technology Concepts

This course will provide participants with knowledge of technological advancements in the modern banking systems which will allow them to improve their planning and use of computer systems in Bolivian banking institutions.

*Services Management

This course will provide participants with basic knowledge of bank accounting, operating and auditing procedures.

*Basic Trade Finance

This seminar will provide participants with the fundamental concepts of trade finance instruments. This will include import and export letters of credit, collections, export assistance programs and the like.

*Basic Financial Control

This course will provide an introduction to the accounting, financial and regulatory controls that govern Bolivia's financial institutions.

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3. <u>Savings Mobilization:</u> <u>Current Potential and Recommended Interventions</u>

The factors which affect deposit growth include:

- General conditions such as discretionary income, depositors' liquidity needs, convenience and access to savings, and whether there is a tradition of holding savings in the form of financial instruments.

- Exchange rates, interest rate and tax policies which protect the value of principal and provide a reasonable return.

- Confidence in the government.

- Confidence in financial institutions and instruments.

In Bolivia, discretionary income is currently relatively low in real terms; however, there is room for deposit growth as a result of two key facts. First, most depositors withdrew their funds during the recent hyperinflationary period and some of those funds can be recuperated by financial institutions. Second, a high proportion of savings are traditionally kept in currency rather than deposited in financial institutions, especially in rural areas.

Bolivian exchange and interest rate policies are currently far more favorable to savings mobilization than those in most countries. The obvious basic problem is that of confidence in the Government. Given the long history of political instability and the profound impact of the 1982 dedollarization, it is surprising that the Bolivian savings rate has recovered as rapidly as it has. It is hard to overstate the confidence problem at the individual and institutional levels created by dedollarization. Restoring confidence under these circumstances requires time, steady macroeconomic performance, and political stability. As noted elsewhere in this Paper, there is also a potential problem in the public's confidence in the banks themselves, should one or more suddenly fail.

During the last several months, the commercial banks have been the most significant mobilizers of new deposits. These deposits have come from dollars formerly held by the Bolivian public, some repatriated savings attracted by high interest rates, earnings from the narcotics trade, the liquidation of non-financial savings vehicles, and the informal economy. Despite the potential for mobilizing more deposits, deposit gathering efforts focussed on commercial banks are not advisable at this time given the precarious situation of many banks and the additional potential liabilities for the BDIF and the GOB which would be created by increasing bank deposits in the short run. In perhaps another year, after the anticipated "shake-down" in the private banking sector, deposit mobilization efforts with banks would be more appropriate. In the short run, savings mobilization efforts will be more appropriate in the informal and rural financial sectors, where little or no formal savings experience exists, and where financial institutions with limited experience in mobilizing deposits already are operating. Savings cooperatives and Savings and Loan Associations are the most viable candidates.

Interventions which should be considered for enhancing savings mobilization in such organizations include:

- institutional strengthening of selected cooperatives or mutual societies;

- development of savings campaigns which popularize and equate savings mobilization with carefully studied and pre-tested themes;
- creation of financial instruments which better meet the needs of individual savers; and
- encouraging or directing savings institutions to make deposits and withdrawal services more available to savers despite the short-term costs.

Such assistance will be focussed on FENACRE.

In the medium term, savings mobilization should not be focussed exclusively on deposit mobilization. If economic stability continues, conditions will exist which will make it opportune to develop new capital market instruments. The most obvious need at present is for short-term treasury bills which could be used by the GOB to help finance its budget deficit and would be helpful to banks as vehicles in which to invest excess liquid reserves. The potential also exists for the development of markets for the trading of other types of debt paper, and this will be explored as the Project proceeds.

Deposit mobilization assistance for commercial banks, when appropriate, should take the form of workshops organized by the FTC for any banks interested in sending attendees, rather than assistance to individual banks, which would raise competitive issues and should, in the final analysis, be financed by the individual banks themselves from their own resources.

4. Improvement of Financial Policy Research and Analysis

A series of research activities and seminars for high level Government policy makers and key individuals from private sector financial institutions has been determined to be the most effective method for improving financial sector policies in Bolivia. The present section discusses briefly the 12 research and seminar topics that, based on preliminary discussions with key individuals, have been tentatively selected and the reasons for selecting them. The most effective timing and phasing of these seminars is also discussed, with four seminars tentatively scheduled for each year over the three year life of the Project. In planning for these seminars, an attempt will be made to strike a balance between two basic types of seminar topics: (1) those that focus on what tend to be pure policy issues and (2) those that focus somewhat more on technical issues of particular interest to managers of financial institutions.

Year 1, Topic 1: Regulation and Supervision of Financial Institutions

By the beginning of year one, considerable effort will have been devoted to reforming the regulation and supervision of financial institutions in Bolivia. These efforts include revision of the banking laws, establishment of a more professional and independent unit to supervise financial institutions, thorough external audits of major financial institutions as a crucial input to improved supervision, and the establishment of a deposit guarantee fund with the purpose of not only guaranteeing deposits, but also assisting problem institutions. It will, thus, be appropriate to evaluate what has been accomplished, and this can be done through brief reviews and analyses by Bolivian and foreign experts to be presented at a seminar for key policy makers and key individuals from financial institutions, both public and private.

Year 1, Topic 2: Theory and Practice of Loan Delinquency and Loan Recovery.

Loan delinquency has been found to be a serious problem for many Bolivian financial institutions--perhaps even more serious than appears because of the widespread practice of refinancing overdue loans. Research on various aspects of this problem is likely to be highly useful. Such research will provide better information regarding: overdue loans, refinancing practices, and loan recovery methods. New theories of why borrowers repay or fail to repay loans have been developed elsewhere, and these should be of particular interest to managers of financial institutions interested in improving loan recovery.

Year 1, Topic 3: Term Lending for Development Purposes.

Essentially, all term lending in Bolivia is based on funds provided by international donor agencies. Thus, one important area of research for this seminar is the issue of promoting term transformation or longer term deposit mobilization by financial intermediaries. Another area is the appropriate role of the Central Bank's Development Department in channeling funds from external donors--an issue that has generated considerable controversy in recent years. Another controversial area that might also be dealt with under this topic is whether or not it is appropriate to have interest rates on such loans below those on short-term commercial loans. Because of the importance of these long-standing controversies, along with the importance of promoting term lending, this topic is one to be dealt with relatively early in the Project.

Year 1, Topic 4: Branching to Expand Financial Services into Rural Areas.

To the extent that financial services are provided at all in remote rural areas of Bolivia, they are provided by the Banco Agrícola, credit unions and informal sources. It is, thus, important to examine possible profit opportunities for banks interested in opening more branches in rural areas providing a wide range of services to a wider range of customers. Most banks are currently reducing the number of their employees and branches, but by the time of this seminar, it is expected that some will be ready to enter an expansion phase. It will also be useful for this seminar to have some inputs from research on deposit mobilization by credit unions -- also making late in the first year an appropriate time for this seminar. The seminar should be of great interest to bank managers interested in the possibility of profitable deposit mobilization and lending activities in rural areas.

Year 2, Topic 1: Deposit Mobilization.

By the beginning of the second year the situation of the private banks should be clearer and work on Deposit Mobilization should be high on the agenda. This topic will draw together as many different elements as possible: policy research, technical assistance and training for financial intermediaries and development of new financial instruments.

Year 2, Topic 2: International Aspects of Bolivian Domestic Financial Markets.

The multi-currency issue and the dollarization of the Bolivian economy will have been discussed in 1987 in an A & A Project seminar. Hence, a second seminar in this very important area seems most appropriate to begin in the second year of the new Project. At this point, research will have been carried out on a wider range of international issues pertaining to Bolivian domestic financial markets such as the importance of capital flows and the appropriateness of exchange rate policies for trade flows and capital flows. Because of the controversial nature of many of these issues, both for economic analysis and in the Bolivian context, it will be important to have the research and seminar presentations undertaken by high level experts in this area, and also to have the papers for presentation reviewed carefully ahead of time by appropriate parties.

Year 2, Topic 3: The Role of Public Sector Financial Institutions in Bolivia.

Earlier work in Bolivia will have focused on restructuring certain public sector financial institutions, and the second year of this Project should be an appropriate time for reviewing whatever progress has been made. In addition, what is considered to be the appropriate role for public sector financial institutions has important implications for the role and behavior of private sector institutions. This topic should, therefore, be important to Government policy makers and to individuals from both public and private sector financial institutions-- some fairly heated discussions may be expected because of the conflicting interests involved.

Year 2, Topic 4: Interest Rates in Bolivian Financial Markets.

Interest rates are always a central topic for research and discussion in the area of financial markets. In the case of Bolivia, there are two major issues to be considered: (1) the extent to which the Government has maintained its policy of generally free interest rates; and (2) the extent to which the very high real interest rates, typical of the early stages of a successful stabilization program, have come down and their prospects for the future. It appears that the middle of the Project would be an appropriate time to focus directly on these issues.

Year 3.

The topics for year three are not listed in any particular order because this is sufficiently far in the future that it would not be appropriate to be more specific with respect to timing. The topics are also more illustrative than firm due to the desire to maintain flexibility.

Year 3, Topic 1: Increasing Access of Borrowers to Credit Services and Reducing Transaction Costs.

Formal financial institutions in Bolivia currently reach few marginal borrowers such as micro-enterprises or small farmers, and this is clearly an important topic to address in terms of both policy and practice. This seminar is scheduled relatively late in the Project to allow adequate field research to be carried out, especially with respect to the transaction costs involved in reaching different types of borrowers, and how one type of financial institution can learn from another in terms of reducing these transaction costs. Experience in USAID projects involving agriculture, housing and micro-enterprises lending will provide useful inputs for this seminar.

Year 3, Topic 2: Capital Markets: Further Review of the Initial Stages of Their Creation.

This seminar will follow the research and seminar held on capital markets during the A&A Project. Its precise development will depend on the results from the earlier seminar and the progress made in actually developing capital markets in Bolivia.

Year 3, Topic 3: Spreads and Efficiency of Financial Intermediaries.

This seminar will survey the research done and the current status (in year 3) of the financial intermediaries themselves with respect to their spreads and efficiency of operations. It will also touch again on the central issue of interest rates. Like the other seminars in year 3, it will tend to summarize what has been accomplished during the life of the Project.

Year 3, Topic 4: Informal Finance.

This seminar will follow the research and seminar on informal finance done under the A&A Project. Because of the great importance of informal finance in Bolivia, considerable research effort will be devoted to this topic during the course of the Project. Moreover, because of the necessity for considerable field work, the gestation period for this research may be longer than for other topics. For these reasons, this should probably be among the last in the series of seminars.

In the design and implementation of all research and seminars, there should be close coordination with other areas of the Project. In addition, as close collaboration as possible should be maintained with USAID projects dealing with agriculture, housing and micro-enterprise financing. With respect to policy issues, it will also be important to maintain very close coordination with the World Bank and other donors involved on the financial sector.

B. Administrative Analyses

1. Bolivian Deposit Insurance Fund

In designing the BDIF organization, it was decided to keep its staff small in view of the relatively limited availability of basically qualified financial personnel in Bolivia and the desire to keep the Fund's operational costs down.

Considering the limited number of insured institutions, a small staff should be adequate to handle the normal operating functions of the Fund. However, when it becomes necessary to intervene a bank, additional personnel will have to be contracted or secunded. It is expected that the permanent BDIF staff members will act as managers, directing the efforts of a sizable number of temporary persons. The temporary people would come from the Superintendency, the Central Bank and from the ranks of attorneys and accountants in the private sector. A series of short-term consultants from the FDIC are expected to provide assistance to BDIF staff members during the formative and early operational stages of the Fund.

The identification and hiring of an experienced person as the Fund Director/Chief Executive Officer will be difficult but is a very important task. The credibility and success of the BDIF will be greatly dependent upon the proper selection of this key manager. The GOB has tentatively selected a candidate with significant international banking experience. The help of a senior consultant to be financed through AID technical assistance is also of primary importance, particularly during the organizational and initial operational phases of the Fund.

Technical assistance and training, coordinated by the FDIC, have been programmed to develop the capabilities of Fund's staff. In addition to a long-term advisor, a total of twenty-four person-months of short-term technical assistance is budgeted. Approximately eight three-month assignments are projected, beginning with one in May 1987 to provide assistance in drafting organizational documents, by-laws and operating procedures. Others will provide assistance in such areas as: intervening banks; managing assets acquired from intervened banks; establishing and managing the assessment procedures; establishing proper cash management procedures; and establishing procedures for collecting and analyzing information about the condition of the banks intervened.

Two training trips (2 people) are programmed to Washington, D.C. for three weeks each, in years 1, 2 and 3. This will allow BDIF staff members to work directly with their counterparts at the FDIC and learn in such areas as intervention mechanisms, financial analysis and general operational procedures. Three trips to various seminars, meetings and training sessions within Latin America are also planned over the four year period. It is envisioned that the subject of these meetings will be common operational problems.

2. Financial Training Center

The FTC will be a semi-autonomous unit within the Institute for Development of Businessmen and Administrators (IDEA). IDEA was founded in 1985 under the auspices of the Confederation of Bolivian Private Businessmen (CEP) as a non-profit private entity organized by an association of companies and respected Bolivian business people. Initial operations were supervised by a board appointed by the CEP. The first general assembly of IDEA took place in March 1986, at which time a permanent Board of Directors was formally elected.

Membership in IDEA represents a cross section of the Bolivian private sector and is organized into three categories. The founding members are represented by the CEP and two private Bolivian businessmen. The private business community is represented by dues-paying active members classified in three categories based upon size, type of firm, and level of contribution. Lastly, there are limited honorary memberships which are awarded by the Board of Directors based on contributions to the private sector as a whole.

Since its inception, IDEA has assumed a leadership role in private sector training. Assistance to it is provided under the Management Training Project (511-0580). Courses are offered for senior executives, mid-level managers, small-scale businessmen and clerical staff. While training courses were only initiated in July 1985, by September 1986 (slightly more than one year later) twenty-one courses had been given to over 1,000 participants with classes given in La Paz, Cochabamba, Sucre and Oruro. As of December 31, 1986, a total of 42 courses had been given covering more than 700 hours of classroom instruction. Due to the rapid progress achieved by IDEA, the Management Training Project was amended in September, 1986, to provide additional funding to expand IDEA course offerings and its regional focus.

The IDEA General Assembly is composed of all active dues-paying members and represents a wide cross-section of the Bolivian private sector. A five-member Board of Directors selected by the CEP (one member) and the General Assembly (4 members) oversees staff recruitment, contracting of the foreign and local experts needed to conduct training courses, and all training activities. The General Manager oversees day-to-day operations and is responsible for training coordination, in consultation with the Board of Directors and the staff of the organization.

Under the Project, a Training Advisory Board will be established to assist in the oversight of the FTC. Its membership will be drawn from ASOBAN. Its role will be to assist IDEA's Board of Directors, General Manager, and the staff of the FTC in selecting training appropriate to the needs of the Bolivian financial community. The staffing of the FTC and its relation to the rest of IDEA has been explained in Section III.B.2.b.

IDEA's success to date is a testimony to the competence and drive of the private sector businessmen who run it. This success also is the best evidence available that the private sector feels a keen need for business training. This need is especially acute in the financial sector and is the reason why the FTC's comprehensive course offerings will be established. IDEA has proven that it can design and deliver good training seminars. It has had to do this with less than adequate technical assistance to date under the Management Training Project. IDEA is ready and able to undertake the challenge of establishing the FTC.

0365L

3. Association of Banks and Financial Institutions of Bolivia (ASOBAN)

a. Membership and Organization

Contrary to what one might expect, ASOBAN was created by a Supreme Decree in 1976 as a private non-profit organization to represent the private sector financial community in Bolivia. All Bolivian private domestic banks as well as all international banks with representation in Bolivia are required to be members. The latter category currently includes Citibank and Argentinian, Brazilian and Peruvian commercial bank branches. While ASOBAN is open to non-bank financial institutions, the only non-bank member is the Caja Central de Ahorro y Préstamo.

Membership in ASOBAN is dominated by the Bolivian commercial banks, with foreign bank participation limited to *ad hoc* representation. The Membership yearly elects a nine-person Board of Directors, eight of which are drawn from the founding members of the Association; the ninth Director is selected from among the banks which have been established since ASOBAN was created. The Board of Directors provides overall policy guidance and direction to the Association. Each board member serves two years, and elections are staggered so that four or five of the nine members change every year. Annual work plans are developed under Board supervision and depend, in part, on the commitment of individual Board members. The level of activity of ASOBAN varies considerably from year to year.

The Board of Directors develops an annual budget with which to carry out its work plan. This budget is financed by membership dues. Although the method of calculating dues varies from year to year, current practice is to establish levels of contribution based on the size of a bank's assets. The budget for the fiscal year June 1, 1986 to May 31, 1987 is US$130,000.

The Board of Directors elects a President, First Vice-President, Second Vice President and a Secretary. The President is the legal representative of ASOBAN and spokesperson for the Board of Directors. The President is responsible for overall direction of the Association's activities. The First Vice President serves as Controller of the Association. The Second Vice President acts as coordinator for the various commissions which are established based upon the yearly work plans. The Secretary is responsible for the execution and implementation of directives, instructions and resolutions coming from the Assembly, the Board, and the President.

ASOBAN's staff is quite small, consisting of an Executive Secretary, Administrative Director, an Economist, an accountant and four clerical employees. The staff is charged with carrying out the work plan devised by the Board of Directors.

b. Current Activities

One of the principal goals of ASOBAN is to foster a spirit of cooperation and unity among its members and, to a more limited extent, the whole private financial community. Through its assemblies and annual activities, it attempts to help the commercial banking community form a consensus on various issues of concern and to present its views to the Bolivian government and the public. In recent years with the impact of dedollarization and hyperinflation, this lobbying and public relations function has been all the more important. Two examples of recent accomplishments are: 1) success in persuading the Central Bank to change its method of calculating reserve requirements; and 2) in cooperation with IDEA, sponsorship of a two-day seminar on the development of a new banking law, which was very successful in increasing the banking community's understanding of the philosophy and structure of a good banking law and in galvanizing the banking sector's support for the revision of Bolivia's antiquated and overly complex law.

ASOBAN has also helped the government. For instance, recently ASOBAN and the Ministry of Taxation devised a system whereby domestic tax payments can be paid through the banking system. Formerly, all taxes were paid directly to the Bolivian internal revenue agency, which was highly inefficient.

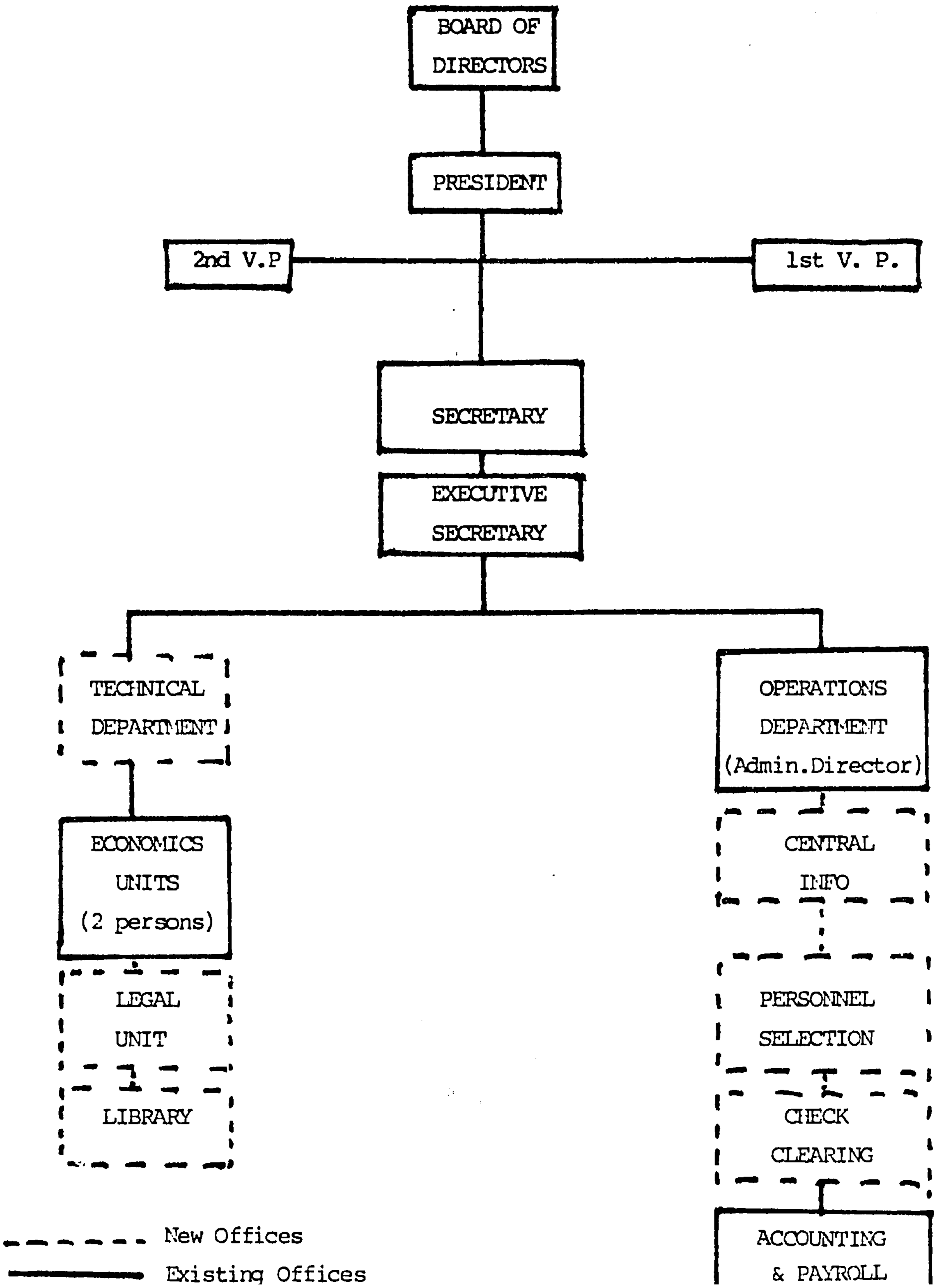
As a result of numerous labor disputes within the Central Bank which have often led to unanticipated closings, ASOBAN has also developed a rudimentary check-clearing service for its members' use when the Central Bank is closed. Other services for members include generating composite statistics on loan interest rates and deposit levels, and serving as an arbitrator for disputes among its members.

c. New Activities and Suggested Organizational Changes

Despite the sporadic successes listed above, ASOBAN has always been primarily a lobbying organization and extremely unimaginative and passive when it has come to providing other services to its members. In Bolivia's new economic environment, there is a good opportunity to make ASOBAN into an organization which serves and assists its' members better; these members have indicated an interest in making this happen.

Rather than attempt to modify ASOBAN's staff organization in a vacuum, it has been decided to concentrate efforts under this component of the Project on the design of new services. Organizational changes will be required to deliver services, but they will be made as the services are designed and implemented. A recommended revised organizational structure for ASOBAN is shown in the following exhibit.

ASOBAN


BOARD OF DIRECTORS
PRESIDENT
2nd V.P
1st V. P.
SECRETARY
EXECUTIVE SECRETARY
TECHNICAL DEPARTMENT
ECONOMICS UNITS (2 persons)
LEGAL UNIT
LIBRARY
OPERATIONS DEPARTMENT (Admin.Director)
CENTRAL INFO
PERSONNEL SELECTION
CHECK CLEARING
ACCOUNTING & PAYROLL
New Offices
Existing Offices

Rather than overload the present ASOBAN staff with technical assistance (i.e. by providing a full-time advisor), it has been determined that it would be preferable to have ASOBAN establish a cooperative relationship with another country's well-functioning bankers' association. The other association will provide short-term experts to design and install new services, sponsor visits by ASOBAN staff and members to its own seminars and with its own members, and serve as a technical resource to ASOBAN and its members.

As ASOBAN gradually develops new services, and a new mentality as a result of its relationship with a sister banking association, it is intended that it will gradually become more and more useful and beneficial to its members.

344L

4. National Federation of Savings and Loan Cooperatives (FENACRE)

a. Legal Status and Activities

FENACRE is the country's largest cooperative organization. This private institution was legally constituted on February 16, 1962 by Resolution No.001 of the National Directorate for Cooperatives and is subject to legal supervision by the National Institute for Cooperatives. By Supreme Decree No.19331 signed December 1982, FENACRE was recognized as an Intermediate Credit Institution and authorized to channel Central Bank of Bolivia (BCB) credit resources.

FENACRE's principal function is to serve as a conduit for financial resources and assistance to two hundred and fifteen savings and loan cooperative affiliates in order to accelerate their development and the improvement of the socio-economic condition of their members through urban and rural productive activities. The specific activities of FENACRE are the following: (1) promote the organization of savings and loan cooperatives; (2) provide technical assistance to cooperatives; (3) develop uniform administrative and accounting systems for cooperatives; (4) promote educational programs and publish educational materials; (5) supervise member cooperative compliance with cooperative laws and regulations; (6) obtain life and fidelity bond insurance for cooperative members and officials; and (7) represent and assist cooperatives in their dealings with government entities.

FENACRE is a founding member of the Latin American Confederation of Savings and Loan Cooperatives (COLAC), and is affiliated with the World Council of Savings and Loan Cooperatives (WOCCU) and the International Cooperative Alliance (A.C.I.).

b. Membership and Financial Soundness

The 1986 Annual Report indicates that during the last twenty-five years, FENACRE has built a National System of Cooperatives which is composed of six departmental federations, 215 cooperatives and 240,000 members. Of this membership, approximately 120,000 members (50%) are rural dwellers, and 140,000 have active accounts in a FENACRE affiliate. As of December 31, 1986, the savings of cooperative members totalled $3.6 million, and the cooperative loan portfolio was $8.9 million. The reserves and capital of FENACRE total $3.6 million, and the institution is today undergoing a rebuilding process after having survived the hyperinflationary and dedollarization problems of the recent past.

c. Organization and Personnel

FENACRE has a General Manger who is governed and supervised by an Administrative Council similar in function to a board of directors. FENACRE has three divisions: Lending Operations, Administrative, and Business and Cooperative Services. FENACRE's current organization chart is presented below. The main office of FENACRE is located in Cochabamba and has 65 employees. There are regional offices in La Paz (8 employees) and Santa Cruz (8 employees), Sucre, Trinidad and Oruro (2 employees each), and Tarija (one employee). FENACRE affiliates employ more than six hundred professional managers, accountants, and other administrative personnel.

d. Capacity to Carry Out Rural Programs

FENACRE has utilized loan and grant funds from several AID and COLAC sources during the past twenty-five years to expand agricultural, agro-industrial, and artisanry lending activities through its cooperatives. For the past five years, FENACRE has channeled PL 480

Title III Agricultural Credit Funds to Integral Cooperatives located in four different agricultural areas of Bolivia. The amount of PL-480 Title III funds increased from $1 million in 1981 to $5 million in 1986. FENACRE's Lending Operations Office includes a Studies and Projects Department which provides sub-project preparation assistance to cooperatives and businesses that are seeking credit from FENACRE or one of its affiliates. FENACRE's Business and Services Office provides technical assistance to member cooperatives in areas such as: cooperative education; credit administration; financial management; and management information systems.

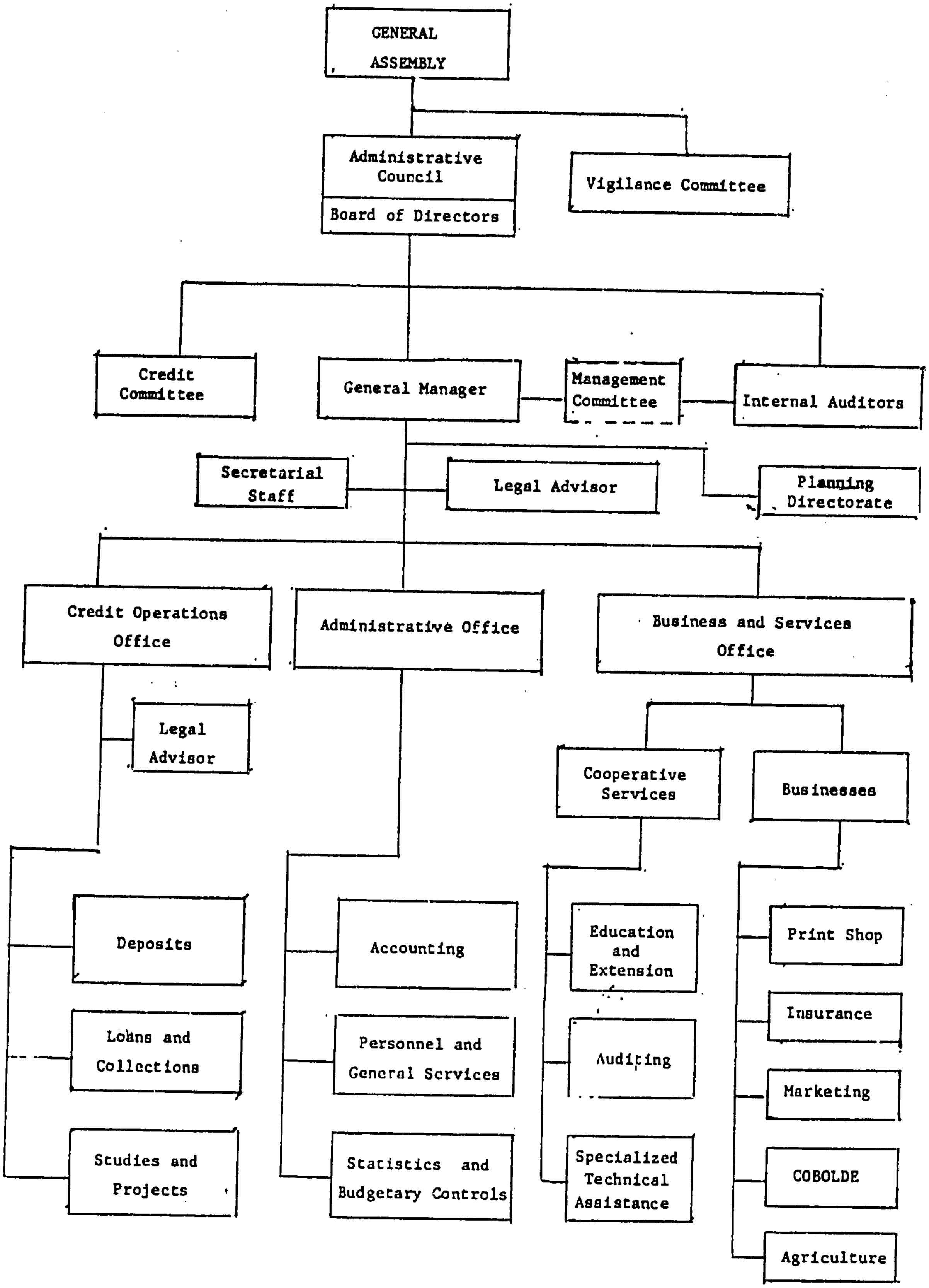
e. Savings Mobilization Experience

In December, 1985 FENACRE launched a pilot savings mobilization program in Cochabamba which has generated considerable interest among FENACRE affiliates throughout the rest of the country. This pilot project has mobilized over $1.1 million of savings to date. These savings have been used to provide small business loans to 269 small commercial and industrial firms in Cochabamba which were not able to obtain credit through normal banking channels.

f. Participation in the Project

Long and short term technical assistance will be provided to assist FENACRE with a management audit of its organizational and administrative systems. This audit will provide FENACRE with recommendations to make it operate more efficiently, and will help FENACRE provide more effective services to its member coops and affiliates. Short term technical assistance will also be provided to help FENACRE carry out market research studies to find out more about the savings and credit needs of its clients in Cochabamba, and throughout the country. Additionally, assistance will be provided to affiliated coops that are interested in preparing savings mobilization strategies and/or savings mobilization programs in their regions.

CHART ORGANIGRAM FOR FENACRE



5. <u>Catholic University Institute for Socio-Economic Studies (IISE)</u>

The Institute was selected to undertake the initial research effort as a continuation of its work under the A&A Project. Founded in 1973, the Institute is an official entity of the Catholic University. It is organized as a legal entity and is empowered to enter into agreements and sign contracts. The Institute is directed by two senior faculty members and active researchers: Dr. Juan Antonio Morales, an economist; and Dr. Salvador Romero, a sociologist. At any one time, there are usually three or four other faculty members actively working with the Institute on research. The Institute has an established record of undertaking contract research, including projects for such organizations as the IDB and the Andean Pact. There are presently no other academic research institutes in Bolivia that can boast this record.

The affiliation of the Institute with the Catholic University is advantageous from three major perspectives. First, it has access to high quality researchers. The Institute can draw upon most of the country's best academic economists, who are members of the Catholic University faculty. It can also contract non-faculty. The University is known for the high quality of training of its undergraduates. Many of the advanced undergraduate students would be excellent candidates to work as research assistants on the Project, and many of these students have prior work experience with the Institute, for example in survey work. Second, the Institute charges only a small negociated overhead fee, usually only ten percent or less of costs. The University provides the office space for the Institute and covers the salaries of the principal associates. The Institute operates on a pay-for-work basis, and any profits are turned over to the University. Third, as a result of the participation of the Institute in the Project, the Institute and the University should develop greater and more extensive capacity for research in financial sector matters. The Project will serve an important role in building this important dimension of the University.

C. Financial Analysis

This section deals with four subjects: an explanation of the criteria for the sharing costs of each relevant Project component with the private sector, the pace at which the BDIF will accumulate reserves to deal with bank intervention actions; the financial viability of the FTC; and the cost of ASOBAN's new services.

1. Cost Sharing Criteria. This Project, as all which AID helps to finance, is intended to bring about changes which will benefit the recipient country socio-economically. The potential to bring about the changes required to achieve the EOP status exists in the institutions which this Project will assist, and these institutions, left to their own devices, might well promote those changes with only their own resources, some day. The reason AID provides assistance for any project, however, is that resources, whether technical or financial, and the organization are currently lacking to assure that desired changes will occur in an orderly and timely fashion. Since project resources are always limited, AID should try to promote the changes and benefits sought in the least costly and most equitable fashion possible, and in a manner that will help ensure that the institutions involved and the changes brought about can sustain themselves after project assistance ends.

These obvious principles for AID financing of developmental activities should not vary depending upon whether private sector or public sector institutions are involved in any particular project. AID helps finance project costs, whether incurred by the private sector or the public sector, because the Agency perceives that it is worthwhile doing so to help achieve socio-economic (or political) objectives. Decisions regarding how much AID finances have to be made balancing the desire to attain those goals with the ability and willingness of the institutions with which it is cooperating to share the project's costs, and the desire to see project activities continue without AID financing after projects end.

AID's purpose in deciding to finance part of the costs of the proposed activities under the SFM Project is solely to bring about desired changes in Bolivia's financial sector. The fact that it has been decided to work primarily with private sector institutions reflects the Mission's conviction that those institutions will be the most efficient and effective agents for change, and recognizes the preponderance of private sector institutions active in Bolivia's financial sector.

It should be recalled that AID has regularly helped finance the developmental or operational costs of activities managed by both private and public sector financial institutions in the past; viz. state-owned agricultural banks, savings and loan systems and cooperatives. AID has an obligation when dealing with private sector institutions to attempt to finance only those costs necessary to obtain project objectives, taking affordability and sustainability of project activities into account. This does it mean, however, that because AID has decided to work with private institutions they must finance 100 percent of all project costs.

In the case of the SFM Project, taking into consideration the urgency of the desired financial sector changes, the weakened financed condition of Bolivia's banks and equity considerations, USAID/Bolivia has divided Project costs using the general criteria that AID should finance the TA and institution-building costs associated with developing activities whereas the private sector should pay the operational costs of the activities themselves. Thus, AID will finance the costs of TA, training, commodities, and audits (75 percent) required to set up the BDIF, while the commercial banks, or their depositors, will finance the operating costs and the capitalization of the Fund. To establish the FTC, AID will finance the TA, staff training, commodities, and a declining portion of FTC operating and course delivery costs, required for the first three years. Course fees will cover all FTC costs from the fourth year on. The reason for financing operational costs during the

FTC's early years is the initially high cost of foreign services necessary to develop, and initially present, courses.

Similarly, AID will finance the TA, commodities, and training required to set up new ASOBAN services and improve the existing services of that organization, and ASOBAN members will pay 100 percent of the costs of new staff and other operating costs of the new services. AID will finance 100 percent of the TA and training costs involved in investigating new capital market instruments and expanding FENACRE services mobilization programs, but none of the operational costs of those programs. Finally, in view of the longer term objectives sought by the policy research and analysis component, and the meagre resources of the Bolivian institutions involved, AID is prepared to finance practically the full costs of the policy research and seminars.

2. <u>BDIF Reserves</u>. The income and ordinary operating expenses of the Fund, over a four-year period beginning in December 1987, are shown in Table 6. The cash flow projections presented for the Fund do not incorporate any use of reserves for actual expenditures which would be incurred for the financial support of member institutions. Although it is recognized that such financial support is a basic rationale for creation of the BDIF, actual expenditures and their net cost and timing cannot be projected with any degree of accuracy. The purpose of the cash flows is to show how fast the Fund will accumulate capital with which to finance intervention activities.

These partial cash flow projections reflect a number of important assumptions:

- The insurance premium charged is 2 percent per year.

- Insurance premiums from the member institutions are paid as a percentage of the total deposit base of each bank. This cash flow is based on the membership of the private commercial banks with a total deposit base as of December 31, 1986, of approximately $286 million. The deposit base of the system is very conservatively projected to increase at 5 percent per cent per annum. Consequently the initial deposit base as of December 31, 1987, is projected to be $300 million.

- The average interest rate paid on reserves invested is assumed to be 7 percent.

- Salary and benefit expenses are projected to increase by 15 percent per year for the years 1989 through 1991. This reflects a modest growth in staff levels.

3. FTC Cash Flow. Table 7 shows the revenues, direct course-related expenses, and operating expenses of the Financial Training Center of the three years of Project assistance.

There are two sources of revenue for the FTC: course revenues from participants (paid by their respective ICIs) and the AID contribution. Both together are calculated to cover slightly more than actual projected expenses in order to provide a cushion in the event of unforeseen expenses, and to allow for a small positive cash balance at the end of the third year. As seen in the cash flow projections, the annual operating deficit of the FTC decreases over the life of the Project, from $286,000 to $39,433. With the AID contribution in the third year, the FTC breaks even in its first year of independent operation.

TABLE 6
BOLIVIAN DEPOSIT INSURANCE FUND
PROFORMA CASH FLOW
(US$)

	DEC 31,86	DEC 31,1987	JAN 1,1988 JUN 30, 88	JULY 1,88 DEC 31,88	JAN 1,89 JUN 30,89	JULY 1,89 DEC 31,89	JAN 1,90 JUN 30,90	JULY 1,90 DEC 31,90	JAN 1,91 JUN 30,91	JULY 1,91 DEC 31,91
Beginning Cash Balance		0	670,000	3,568,706	6,706,614	10,036,816	13,032,991	16,772,531	20,713,451	24,885,034
INCOME										
BCB loan		500,000	0	0	0	0	0	0	0	0
Member premiums (1)		170,000	2,833,000	3,078,075	3,155,027	3,233,903	3,314,750	3,397,619	3,482,559	3,569,623
Investment (2)			120,681	230,875	347,217	452,471	582,488	720,153	865,876	1,019,258
Total Income		670,000	2,953,681	3,308,950	3,502,243	3,686,373	3,897,238	4,117,771	4,348,435	4,588,881
EXPENSES										
Salaries			16,900	102,500	102,500	117,875	117,875	135,556	135,556	155,890
Annual Benefits			1,408	8,542	8,542	9,823	9,823	11,296	11,296	12,991
Pent			1,250	7,500	7,500	7,500	7,500	7,500	7,500	7,500
Data processing			833	5,000	5,000	5,000	5,000	5,000	5,000	5,000
G&A			833	5,000	5,000	5,000	5,000	5,000	5,000	5,000
Legal services			1,250	7,500	7,500	7,500	7,500	7,500	7,500	7,500
Travel			0	2,500	3,500	5,000	5,000	5,000	5,000	5,000
Int. expense BCB loan (3)			32,500	32,500	32,500	32,500	0	0	0	0
Total Expenses		0	54,975	171,042	172,042	190,198	157,698	176,852	176,852	198,881
BCB loan amortization		0	0	0	0	500,000	0	0	0	0
Ending Cash Balance		670,000	3,568,706	6,706,614	10,036,816	13,032,991	16,772,531	20,713,451	24,885,034	29,275,034
DEPOSIT BASE	286,000,000	300,300,000	307,807,500	315,502,688	323,390,255	331,475,011	339,761,886	348,255,933	356,962,332	365,886,390

(1) Annual payments paid on semi-annual basis beginning June 1988 at 2.0 percent of deposit base per year. Assumes deposit base of bank system increases by 5 percent per year.

(2) Assumes 7 percent per year return on investments.

(3) Deposit fund receives loan (capital infusion) from BCB.
Interest payable at 13 percent per year.
Regular interest accrual payable at $32,500 semi-annually in arrears.

Table 7

CASH FLOW FOR THE FINANCIAL TRAINING CENTER COMPONENT

COURSE REVENUE	YEAR 1 Number offerings	YEAR 1 Participants	YEAR 1 Cost per Part. ($)	YEAR 1 Revenue	YEAR 2 Number offerings	YEAR 2 Participants	YEAR 2 Cost per Part. ($)	YEAR 2 Revenue	YEAR 3 Number offerings	YEAR 3 Participants	YEAR 3 Cost per Part. ($)	YEAR 3 Revenue	YEAR 4 Number offerings	YEAR 4 Participants	YEAR 4 Cost per Part. ($)	YEAR 4 Revenue
Senior Level	5	15	500	37,500	4	15	500	30,000	3	15	500	22,500	3	15	500	22,500
Mid-Level	10	20	400	80,000	11	20	400	88,000	8	20	400	64,000	8	20	400	64,000
Lower-Level	10	20	300	60,000	10	20	300	60,000	7	20	300	42,000	7	20	300	42,000
Total Revenues	25	55		177,500	25	55		178,000	16	55		128,500	18	55		128,500

EXPENSES	YEAR 1 Number Offerings	YEAR 1 Cost per Course	YEAR 1 Costs	YEAR 2 Number Offerings	YEAR 2 Cost per Course	YEAR 2 Costs	YEAR 3 Number Offerings	YEAR 3 Cost per Course	YEAR 3 Costs	YEAR 4 Number Offerings	YEAR 4 Cost per Course	YEAR 4 Costs
Direct Courses												
Senior Level	5	20,000	100,000	4	10,100	40,400	3	5,400	16,200	3	5,400	16,200
Mid-Level	10	15,000	150,000	11	7,280	80,080	8	4,380	35,040	8	4,380	35,040
Lower-Level	10	10,000	100,000	10	4,020	40,200	7	2,520	17,640	7	2,520	17,640
Sub-total Courses	25		350,000	25		160,680	18		68,880	18		68,880

FTC Operating Expenses	YEAR 1	YEAR 2	YEAR 3	YEAR 4
Staff Salaries	38,350	39,884	41,479	43,139
Other	6,400	6,400	6,400	6,400
Sub-total	44,750	46,284	47,879	49,539

IDEA overhead	YEAR 1 Numbers of Hours	YEAR 1 Cost per Hour	YEAR 1 Cost	YEAR 2 Numbers of Hours	YEAR 2 Cost per Hour	YEAR 2 Cost	YEAR 3 Numbers of Hours	YEAR 3 Cost per Hour	YEAR 3 Cost	YEAR 4 Numbers of Hours	YEAR 4 Cost per Hour	YEAR 4 Cost
Senior Level	120	34.10	4,092	120	34.10026	4,092	72	34.10	2,455	72	34.10	2,455
Mid-Level	400	34.10	13,640	400	34.10026	13,640	320	34.10	10,912	320	34.10	10,912
Lower-Level	480	34.10	16,368	480	34.10026	16,368	360	34.10	12,276	360	34.10	12,276
Sub-total	1,000		34,100	1,000		34,100	752		25,643	752		25,643

OTHER	YEAR 1 Number Particip.	YEAR 1 Cost Particip.	YEAR 1 Cost	YEAR 2 Number Particip.	YEAR 2 Cost Particip.	YEAR 2 Cost	YEAR 3 Number Particip.	YEAR 3 Cost Particip.	YEAR 3 Cost	YEAR 4 Number Particip.	YEAR 4 Cost Particip.	YEAR 4 Cost
Senior Level	75	74	5,550	60	74	4,440	45	74	3,330	45	74	3,330
Mid-Level	200	74	14,800	220	74	16,280	160	74	11,840	160	74	11,840
Lower-Level	200	74	14,800	200	74	14,800	140	74	10,360	140	74	10,360
Sub-total	475		35,150	480		35,520	345		25,530	345		25,530
Total Expenses			464,000			276,584			167,933			169,592
Revenues minus Expenses			(286,500)			(98,584)			(39,433)			(41,092)
AID CONTRIBUTION			314,438			115,150			36,021			0
NET CASH			27,937			44,503			41,092			(0)

Expenses for the FTC are divided into two categories: course-related expenses, and FTC overhead expenses. Course-related expenses include the direct cost to the FTC of the courses themselves, miscellaneous course expenses such as photocopying, and the portion of IDEA overhead which accrues to the FTC. FTC overhead expenses include FTC staff payroll and operating expenses. The percentages of these expenses financed by AID are as follows:

	Year 1	Year 2	Year 3
Course-Related Expenses	75%	50%	30%
FTC Overhead Expenses	100%	60%	40%

4. ASOBAN Costs of Services. The incremental cost of new services ASOBAN will develop as shown below. These services will be financed out of annual fees to members by increasing them slightly, or on a fee-for-service basis (charging the users of the services).

ASOBAN SERVICES: COST OF SERVICES (US$)

Service	Year 1	Year 2	Year 3	Total
I. Information Center				
a. Manager	19,080	9,843	20,637	59,560
b. Programmer	12,720	13,228	13,757	39,705
II. Economics Unit				
Economist	19,080	19,843	20,637	59,56
III. Check Clearing				
1 Professional	12,720	13,228	13,757	39,705
IV. Legal Unit				
Lawyer	19,080	19,843	20,637	59,560
V. Personnel Selection				
1/2 Professional	7,950	8,268	8,599	24,817
VI. Library				
1/2 Professional	7,950	8,268	8,599	24,817
Total	98,580	102,521	106,623	307,724

Note: Unit costs are calculated to include 94 percent for salary and 4 percent for operational support such as stationary, mail, supplies, insurance, etc. Example, Year 1 staff lawyer salary is $18,000 and $1,080 is for operational support. For Years 2 and 3, an inflation rate of 4 percent has been calculated.

D. Economic Analysis

In this Section, we shall present and analyze available data to (a) identify the major historical causes of the difficulties presently confronting the private deposit banks; and (b) shed light on the dimension of the banks' current financial condition. We shall then explore two alternatives to the proposed project. 1/

1. Historical Causes of the Problem

a. Perhaps the major cause of the financial difficulties faced by Bolivian private banks is the sharp decline in the real value of both bank deposits and loans between 1981 and 1985. Table 8 illustrates the situation for demand, time, and dollar deposits; Table 9 shows it for bank loans. Note the following:

1) The real value of peso deposits, including both demand and time deposits (but excluding dollar deposits), declined from $b 16.7 million (in constant 1966 pesos) in 1981 to $b 8.57 million in 1983 and to only $b 3.0 million in 1984. A very modest recovery to $b 4.1 million occurred in 1986, (See Table 8).

2) US dollar deposits followed the same pattern, but the swings were even larger than for peso deposits, mainly as a result of

1/ A benefit-cost or IRR analysis is not considered advisable in the case of this project owing to the impossibility of developing a meaningful quantification of the potential benefits of this typical institution-building proposal. Estimating the quantitative impact on bank loans, deposits and profitability of the diverse project elements such as training of bank personnel, improved supervision of bank operations, deposit insurance and bank law reform would obviously involve some highly arbitrary and controversial judgments. We consider it preferable, therefore, to provide actual data establishing the precarious position of the banks to prove the need for urgent remedial action; and to discuss some major alternatives to the proposed project.

dedollarization. US dollar deposits declined from $134 million in 1981 to only $7 million in 1982 and $1.2 million in 1984. However, between December of 1984 and October 30, 1986, the value of total dollar deposits had recovered to $120 million (see Table 8). Total deposits (demand, time and US$ deposits), declined from US$508 million in 1981 to only US$ 46 million in 1984, then recovered to $228 million by October 30, 1986 (Table 8). Thus, while total deposits (including US dollars) have staged a remarkable recovery in 1986, they are still only 45% of the 1981 level.

b. The real value of bank loans granted to the private sector follows the same pattern. In US dollar terms (i.e. Bolivianos converted into dollars at the parallel market exchange rate), total bank loans granted to the private sector declined from US$566 million in 1981 to only US$107 million in 1984; then recovered to US$239 million in 1985 and to US$414 million in 1986, still 27 percent below the 1981 level.2/ (See Table 9). This helps explain the increase in overhead costs as a proportion of total loans granted.

c. The earnings of the banking system were affected very adversely by the lag of interest rates in relation to the rate of inflation during the period 1982-85. As shown in Table 10, the banks' interest rate on loans in 1981 was still positive — i.e. 30% versus an annual inflation rate of 25%. In 1982, the average real interest rate turned sharply negative: the nominal interest rate was 38% while inflation had accelerated to nearly 300%. The situation was at its worst in 1985, with average interest rates (on loans) at 231% while the inflation rate reached 8,170% (Table 10). The lag of interest rates in relation to the increase in the general price level is a contributing

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2/ Note that total loans granted by the financial system to the private sector exceed total bank deposits in all years. The difference is due to Central Bank credits and financing from international donors and foreign banks.

factor behind the precarious position of the national banking system, though it should be noted that banks were able to mitigate its adverse impact in their P&L statements by (a) securing credit lines from the Central Bank; (b) adding commissions and official charges to their interest rates; (c) making loans for only very short periods; and (d) investing heavily in real estate. Their losses were largely at the expense of their depositors.

During the stabilization period (from mid to late 1985 onward) interest rates continued to lag behind the rate of inflation. Today, however, the lag is reversed. During 1986 the rate of inflation fell precipitously, but interest rates declined much more slowly. As a result, interest rates in 1986 were significantly higher than the rate of inflation—i.e. 124% vs. 66% (Table 10). This lag had a significant negative impact on the level of economic activity as most "productive"3/ enterprises did not earn returns high enough to enable them to pay the prevailing interest rates.

d. The decline in overall economic activity during the 1982-86 period was another significant contributor to the difficulties of the banking system. This decline was due to a combination of factors, including the decline in the prices of the country's main exports (natural gas and tin), the burden on the balance of payments resulting from the country's enormous foreign debt, and, most importantly, the hyperinflation and various ill-advised economic policies pursued by previous governments. During the five-year period 1982-86, real GDP growth declined by 14% in real terms. Private investment declined by as much as 74%. Particularly hard hit were manufacturing (down by 36%) and mining (down by 63%. See Table 11). This decline in economic activity has contributed to the inability of many concerns to repay bank loans contracted in late 1985 and 1986.

3/ Enterprises engaged in manufacturing, agriculture and construction.

e. Paradoxically, the Government's successful stabilization program appears to have contributed further to the difficulties of the banking system. As the price level stabilized, the frantic demand for bank loans fueled by speculation experienced a sharp drop. The banks' overhead expenses which had declined significantly in real terms over the period 1982-85 (largely owing to the lag of wages and salaries behind the rate of increase in the general price level) suddenly shot up, particularly in their relation to the real value of the banking system's deposit base and to the total volume of loans granted. To make matters worse, banks had substantially expanded staff and facilities during the period of inflation and were thus caught with excessive overhead during the lean period that followed.

f. Lack of proper supervision and deficiencies in the management area resulted in a significant number of unsound loans, many utilized for speculative purposes. While most bank loans could easily be repaid during the period of hyperinflation, many resulted, after stabilization, in a substantial number of loans could not be repaid and had to be classified as "non-performing loans" (discussed further below).

The factors discussed above are believed to be the major causes of the difficulties the banking sector is currently confronting. A comment is in order on the subject of de-dollarization, which is often listed among the factors that contributed to the banking system's current difficulties. The net impact of de-dollarization on the financial position of the banking system is not clear. It is true that the banking system was hurt by the sharp decline in the real value of total deposits which was aggravated by the de-dollarization process, by the repayment in pesos of the dollar loans it had granted and by the cut-off from foreign credits as foreign banks (which did not accept repayment in pesos at a highly overvalued exchange rate) refused to extend new loans. On the other hand, the banks benefited from their ability to liquidate the dollar deposits of their customers with overvalued pesos, and from their ability to purchase dollars from the Central Bank at the official rate. Thus, with various factors working in opposite directions, it is not at all clear that the banks were hurt by de-dollarization.

Table 8

DEPOSITS IN THE BANKING SYSTEM

	1981	1982	1983	1984	1985	1986(1)
TOTAL $b. DEPOSITS (Mill.$b) (Nominal terms)	15,442	58,202	140,428	1,104,408	82,158,935	209,939,000
Demand Deposits	6,301	17,658	50,368	424,607	24,859,114	55,078,000
Time Deposits	9,141	40,544	90,060	679,801	57,299,821	154,861,000
TOTAL $b. DEPOSITS (Mill.$b) (Real terms)(2)	16.73	15.21	8.57	2.96	2.66	4.10
Demand Deposits	6.83	4.62	3.07	1.14	0.81	1.07
Time Deposits	9.90	10.60	5.49	1.82	1.86	3.02
TOTAL $us. DEPOSITS (Mill.$us)	133.82	7.31	1.79	1.16	21.62	119.91
Time Deposits	133.82	7.31	1.79	1.16	21.62	119.91
TOTAL DEPOSITS (Mill.$us)	508.17	212.94	114.69	46.21	69.50	228.40
$b. Demand Deposits(3)	152.75	62.39	40.49	17.32	14.49	28.46
$b. Time Deposits(3)	221.60	143.24	72.40	27.73	33.39	80.03
$us. Time Deposits	133.82	7.31	1.79	1.16	21.62	119.91

(1) To October 1986
(2) Deflated by the CPI for the month of December
(3) Adjusted by the parallel exchange rate for the month of December.

SOURCE: Estadisticas Monetarias y Financieras, BCB.

Table 9

PUBLIC AND PRIVATE CREDIT OF THE FINANCIAL SYSTEM: 1981-1986 (Balance Outstanding)	1981	1982	1983	1984	1985	1986(1)
inal Terms (Mill.$b)						
dit to the Public Sector (2)	43,297	241,541	725,583	13,115,122	2,443,624,611	2,580,554,232
dit to the Private Sector	23,358	91,192	191,788	2,624,024	409,714,472	800,673,723
l Terms (Mill.$b)(3)						
dit to the Public Sector (2)	46.9	63.1	44.3	35.1	79.2	50.6
dit to the Private Sector	25.3	23.8	11.7	7.0	13.3	15.7
lar Terms (Mill.$us) (4)						
dit to the Public Sector	1,050	853	583	535	1,424	1,334
dit to the Private Sector	566	322	154	107	239	414

As of October 1986.
On a gross basis - i.e. without deducting government deposits whose value was distorted by the devaluation.
Deflated by the CPI of December or October of the respective year.
Adjusted by the parallel exchange rate of the end of the year.

RCE: Estadisticas Monetarias y Financieras No.34, BCB.

Table 10

RATE OF INFLATION AND NOMINAL INTEREST RATES(1) (1981-1986)					
	$b.		$us.		Rate of Inflation (12 mos.) %
	Pasive(2) %	Active %	Pasive(2) %	Active %	
1981	23.00	30.00	20.00		25.12
1982	32.00	38.00			296.55
1983	45.00	62.00			328.49
1984	140.00	150.00			2177.23
1985	110.00	231.10	11.20	16.80	8170.52
1986	67.58	123.65	14.10	21.93	65.96
March	132.67	234.25	12.00	20.25	163.92
June	64.00	118.67	14.67	22.00	35.28
September	41.33	83.67	14.67	22.00	18.80
December(3)	32.30	58.01	15.08	23.46	4.48

(1) The rate of inflation and the interest rates are annualized.
(2) Time Deposits.
(3) Fourth quarter data includes January 1987 figures

SOURCE: Estadisticas Monetarias y Financieras No.32 and 34, BCB; INE.

TABLE 11

GROSS DOMESTIC PRODUCT BY ECONOMIC ACTIVITY
(Mill.1980 $b)

ECONOMIC ACTIVITY	1981	1982	1983	1984(p)	1985(e)	1986(e)
A. INDUSTRIES	105,644	102,573	94,363	93,233	91,421	88,625
Agriculture	22,350	23,878	17,507	20,782	21,417	21,006
Mining	12,133	10,635	10,889	8,565	6,852	4,454
Petroleum	7,157	7,704	7,219	7,037	6,899	6,629
Manufacturing	16,664	14,344	13,387	11,814	10,729	10,622
Construction	4,025	3,928	3,751	3,500	3,591	3,562
Electricity Gas & Water	919	923	919	931	936	945
Commerce	14,360	13,599	13,055	12,924	13,195	13,393
Transportation & Communications	8,196	7,770	7,931	7,988	8,067	8,163
Financial Institutions	6,324	6,413	6,490	6,555	6,686	6,853
Housing Property	10,119	10,149	10,169	10,179	10,189	10,199
Other Services	4,877	4,731	4,565	4,492	4,425	4,403
Imputed Bank Services	(1,480)	(1,501)	(1,519)	(1,534)	(1,565)	(1,604)
B. PRIVATE SERVICES	687	666	646	633	622	616
C. PUBLIC SERVICES	13,291	13,504	13,909	13,965	13,686	13,234
GDP AT PROD. PRICES	119,622	116,743	108,918	107,831	105,729	102,475
Plus Indirect Taxes	3,753	3,162	3,132	3,223	3,384	3,502
GDP AT CONS. PRICES	123,375	119,905	112,050	111,054	109,113	105,977
GDP % GROWTH RATE	0.3%	-2.8%	-6.6%	-0.9%	-1.7%	-2.9%
PRIVATE INVESTMENT	4,678	5,786	2,094	1,759	1,225	1,225
% Growth Rate		23.7%	-63.8%	-16.0%	-30.4%	0.0%

p= preliminary
e= estimate

SOURCE: Boletin Estadistico No. 258, BCB and Statistical Appendix, IMF.

What is clear, however, is the net effect of de-dollarization on the banking system's debt to their foreign creditor banks. Since the Central Bank refused -- or was not able -- to convert the peso repayments of the national banks into dollars at the highly overvalued exchange rate that prevailed at that time, the national banks are left with an unpaid debt to foreign banks of some US$ 67 million. This has resulted in their inability to get fresh credit from abroad as well as in a huge reduction in net worth as reported on their balance sheets. The banks clearly cannot repay this debt at the current exchange rate. This problem remains unresolved to date.

2. Indicators of current financial difficulties

A detailed analysis of the current weakness of the Bolivian national banking system was undertaken by the consultant for the Project Design Team 4/. In interpreting the data presented below, account should be taken of the fact that the Central Bank's ability to collect and process accurate data on the current situation of the banks is extremely weak. There are no reliable audits of private banks, and the Central Bank simply accepts the financial data provided by the banks without knowing its accuracy or completeness. The de-dollarization process (that took place in 1982) further complicates the banks' financial picture as it provides ample opportunity for concealment of speculalive profits or losses. Still, the data presented below (analyzed in greater detail in Annex A) constitute the only available quantitative information available to USAID at this time.

The following indicators are particularly revealing with regard to the present condition of the commercial banks:

4/ The International Science and Technology Institution (ISTI). The data in this Section was presented in their paper entitled "The Bolivian Banking System," attached as Annex A.

a. The high ratio of non-performing loans: Non-performing loans (i.e. loans on which interest and principal are not being paid) on December 31, 1986, amounted to US$28 million and constituted 14% of all loans granted by the national banks. The proportion of non-performing loans granted by foreign banks was 66%. For the banking system as a whole, the proportion of non-performing loans was 25% (See Table 12).

Table 12

Non-Performing Loans - December 1986
(millions of dollars)

	Total Loans	Non-Performing Loans Amount	Non-Performing Loans Percent
Private Banks	198.4	28.1	14
Foreign Banks	11.9	7.9	66
Special Function Banks	47.6	10.9	23
Totals	332.4	83.9	25

Source: Central Bank

b. Severe Undercapitalization: As the hyperinflation progressed, the banks successively revalued their assets. The consultant notes that "the Bolivian banks appear to have utilized this accounting mechanism to the extreme.... The capital structure is particularly weak as out of the total reported capital base of US$42.8 million, US$37.5 million is 'capital' from revaluations. This represents a dangerously high ratio of 88.1% of the reported capital."5/

5/ ISTI, "The Bolivian Banking System," Op. Cit., Page 6.

c. High Operating Costs and Administrative Expenses: "For the twelve-month period ending December 31, 1986, total operating expenses of the banking system as a percentage of average total earnings of the system were slightly over 13% p.a. This is a significantly high number because it implies that, on average, banks must make a gross spread on their earning assets in excess of 13% p.a. in order to produce a profit".6/ The fact that total administrative expenses in relation to total income were 15%, requires a high spread between interest paid on deposits and interest charged on loans.

d. Losses Reported by a Number of Banks: The consultant found that almost half of the banks (for which data are available) are currently reporting losses. The profit and loss situation of 12 commercial banks is summarized in Table 13. Note that five of the twelve banks reported losses. Losses for three banks are particularly severe -- between 8 and 12 percent of net worth.

Table 13

Profit or loss ( ) as a % of Equity

Bank	
Progreso	52
Union	37
Hipotecario	27
Big Beni	9
Mercantil	5.3
Santa Cruz	2.1
La Paz	1.2
Credito Oruro	(.4)
Cochabamba	(.8)
Nacional	(7.7)
Potosi	(11.2)
Boliviano-Americano	(11.9)

Source: Ibid, Page 10

6/ Ibid, Page 7

e. The High Ratio of "Past Due" Loans: A significant proportion of the loan portfolio of the commercial banks consists of "Loans Past Due" and "Loans Past Due in Execution". This latter classification includes all loans past due for thirty days or more. The data are presented in Table 14. Note that for six out of the twelve banks for which data are available, the percentage of "Past Due Loans" ranges from 14 to 65 percent, while the proportion of the portfolio for loans "Past Due in Execution" ranges from 11 to 49 percent. The total amount of "Past Due Loans" of all Bolivian commercial banks was US$ 28 million at year-end, which represents approximately 10% of the total loan portfolio of the system.7/

f. The High Ratio of Non-Earning Assets: A high proportion of the banking system's assets earn no return (e.g. buildings and equipment). Table 15 shows that the proportion of non-earning assets to total assets is 39% or higher for nine of the twelve banks for which data are available. The ratio of the banks' real estate to their capital and reserves is 79%.

Table 14

Past Due Portfolio

Bank	% of Portfolio Past Due	% of Portfolio Past Due in Execution
Banco Crédito Oruro	65	49
Banco Nacional	27	23
BIG Beni	24	17
Banco Cochabamba	22	14
Banco Boliviano-Americano	20	14
Banco de Potosí	14	11
Banco Hipotecario	9	3
Banco Mercantil	7	4
Banco La Paz	6	5
Banco de Santa Cruz	5	4
Banco Progreso	5	2
Banco Unión	5	2

Source: ITSA, Ibid., Page 11

7/ Ibid., Page 11

Table 15

Non-Earning Assets

Bank	Non-Earning Assets as a % of Total Assets
Banco de Santa Cruz	60
Banco Progreso	57
Banco de Potosí	51
Banco Mercantil	51
Banco Hipotecario	50
Banco Boliviano-Americano	44
Banco Nacional	42
BIG Beni	39
Banco La Paz	39
Banco Crédito Oruro	36
Banco de la Unión	33
Banco Cochabamba	23

These various indicators support the consultant's conclusion that given the banking system's "high overhead costs, high deposit interest rates, a large percentage of non-performing loans and non-earning fixed asset investments, it can be seen that the total effect of these bank inefficiencies result in the low profitability and structural weaknesses apparent in the Bolivian banking sector. In addition to possibly paying current operating expenses from the deposit base, it is apparent that much of these funds must be utilized to support non-earning assets."8/

The data and analysis summarized above leave no doubt with respect to the weakness of the banking system or to the need to adopt effective remedial measures as soon as possible to avoid its further deterioration. Nevertheless, we would not go so far as to predict the

8/ Ibid Page 13.

imminent collapse of Bolivia's banking system for two reasons: (1) given the close tie-in between the ownership of the banks and the country's commercial, industrial and land-owning interests, the owners might well decide to beef up the capital of their banks if that should become essential to forestall their collapse; and (2) the Central Bank might step in to bail out any bank subject to a run. The disadvantage entailed by this latter course is discussed in Section III below.

3. Discussion of Alternatives to Proposed Project

a. Maintaining the Status-Quo

The credit system performs the key function of linking the supply of, and the demand for, loanable funds, thus ensuring that private savings, domestic and foreign, meet the demand of producers for short and medium term credit, including working capital. When banks are badly managed, when loans are made for speculative purposes or to finance unsound projects, when the banks' operating and administrative expenses are exorbitantly high and a large proportion of bank assets are non-earning, the result is likely to be a high proportion of "non-performing loans". As a corollary, productive enterprises are likely to find that a significant proportion of their credit requirements remains unmet. If credit is made available at all, it is likely to be at interest rates that they are unable to pay. While USAID does not claim that economic reactivation will be impossible under the status-quo, the weight of the evidence strongly suggests that economic activity -- and recovery -- will be significantly below potential as long as the banking system remains in its current disorganized state.

Even more significant is the danger that several banks might fail if the serious deficiencies in the banking structure and in their mode of operation remain uncorrected. In that eventuality, the authorities would face the grim choice of either permitting the institutions to fail or bailing them out (by paying off depositors) with

Central Bank credit. The former would further undermine confidence in the banking system and delay, or even reverse, the recovery of bank deposits, and hence the banks' ability to perform the credit function. At worst, it could set the stage for a general run on all commercial banks and cause the failure of even well-managed institutions. On the other hand, if the authorities chose to bail out any bank in difficulty, no matter how badly managed, the deficiencies of the present system would never be corrected and the situation would be likely to deteriorate progressively. In this eventuality, the Central Bank would be called upon to create ever larger amounts of credit to maintain the solvency of the banking system, a policy that could soon undermine the economic stabilization program. Thus, the maintainance of the status-quo should be viewed as an unacceptable alternative to the proposed project.

b. Nationalizing the Private Banks:

This alternative runs counter to prevailing GOB and USG policy. The policy has not produced satisfactory results where it has been tried (e.g. in El Salvador). Moreover, the Government's historical record in managing its own financial institutions, including the Central Bank, the Banco Agrícola and the Banco del Estado suggests that this course of action is not a viable alternative to the proposed project.

In conclusion: This analysis suggests that corrective action to improve the mode of operation of the banking system is urgently needed. In fact, essential corrective action has been delayed far too long. The analysis points to the need for the main elements that make up this project, including (a) the establishment of an independent Superintendence of Banks and much stricter supervision of the banks' mode of operation; (b) enactment of a new banking law; (c) measures to recapitalize commercial banks, strengthen their loan portfolios and encourage the growth of the deposit base, which are the main targets of the proposed deposit insurance scheme; (d) training of bank personnel; (e) reduction of legal reserve requirements (behind demand deposits) to increase the proportion of earning assets in the banks' portfolio; (f) reorganization of the Central Bank and (g) carrying out in-depth external audits and examinations of all national banks.

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VII. Conditions and Covenants

The following conditions, covenants and substantive involvement understandings will be included in the three obligating documents signed for the SFM Project.

A. Conditions and Covenants for the Project Agreement to be Signed with the GOB.

1. Prior to the signing of a contract with the FDIC for long-term technical services, the Grantee shall furnish to AID, in form and substance satisfactory to AID, a copy of the draft agreement to be signed by the Central Bank and the BDIF whereby the Central Bank agrees: a) to finance 50 percent of the cost of any bank intervention actions occuring during at least the first three years of the life of the BDIF (1988 to 1990)and/or to extend an adequate capitalization loan to the Fund when it begins operations; and b) to extend to the BDIF working capital loans from the Central Bank when necessary for bank intervention actions.

2. Prior to any disbursement, or the issuance of any commitment documents under the Agreement, to finance assistance to FENACRE, the Grantee shall furnish in form and substance satisfactory to AID:

a. evidence that FENACRE has planned for the utilization of the technical services of a long-term advisor, including provision of office space, secretarial support, etc;

b. documentation attesting to FENACRE's agreement (a) to use its best efforts to implement the recommendations of the management audit to be performed on its operations, and (b) to finance all operational costs associated with the expansion of its savings mobilization programs.

3. The Grantee hereby covenants that it will:

a. take whatever legal steps are necessary to establish the BDIF as an autonomous corporation by September 1987;

b. take whatever legal steps are necessary to re-establish the Superintendency of Banks by September 1987;

c. carry out a study of the structure of deposits in private Bolivian banks for the purposes of determining deposit insurance coverage principles; and

d. review the adequacy of insurance premium charges and BDIF capitalization at least once per year during the life of the Project.

B. <u>Substantive Involvement Understandings for the Cooperative Agreement with IDEA</u>

1. Prior to any disbursement, or the issuance of any commitment documents under the Cooperative Agreement, to finance activities of the FTC, the grantee shall furnish in form and substance satisfactory to AID:

a. evidence that the Training Advisory Board for the FTC has been established;

b. the first year operational plan and budget for the FTC, including charges to be made for IDEA support to the Center, and proposed tuition fees.

c. evidence that the staff of the FTC has been identified and selected.

2. IDEA covenants that over the life of the Project:

(i) an annual training plan and budget shall be developed and submitted for the approval of the IDEA Board, the Training Advisory Board and AID.

(ii) to provide anticipated counterpart funds to ensure the timely implementation of all activities envisioned under the Project.

(iii) to periodically survey financial sector training needs.

(iv) to obtain AID approval of all contracts exceeding $10,000 in value.

C. <u>Substantive Involvement Understandings for the Cooperative Agreement with ASOBAN</u>

1. Prior to any disbursement, or the issuance of any commitment documents under the Cooperative Agreement, to finance the new services of ASOBAN, the grantee shall furnish in form and substance satisfactory to AID:

a. evidence that the development of the new services and any necessary organizational changes have been approved by the Association's Board of Directors; and

b. a detailed implementation plan and budget for the first year activities envisioned

2. ASOBAN covenants that over the life of the Project that adequate operational budget support shall be provided to carry out all agreed-upon activities.

ANNEX A

ANALYSIS OF THE STATUS OF BOLIVIA'S COMMERCIAL BANKS

Presented below is an analysis of the structural and operational problems affecting Bolivia's banking sector. The analysis is based on statistics submitted by the banks to the Central Bank as of December 31, 1986. These statistics are now three months old and have not yet been verified by external audits. Although the data clearly shows that most banks are in precarious financial positions (for reasons explained below), Bolivia's commercial banks have proven themselves to be very resilient in the face of profound economic changes experienced during the 1980s. The fact that the banks are still in operation shows that their owners and managers are tough competitors who know how to survive in the Bolivian environment. One cannot assume that all banks are about to fail now that economic conditions are finally improving. In fact, many bankers now appear to be very interested in modernizing their banks so that they can take advantage of the competitive opportunities being created by the continued success of the Paz Estenssoro Government's economic policies. It is also very important to remember, as pointed out below, that the owners of Bolivia's commercial banks profited handsomely during the recent period of hyperinflation and dedollarization, even though their banks suffered. These owners still place a high value on having a bank as part of their industrial groups and should be able to invest the additional capital and make the additional expenditure necessary to put their banks back on their feet. As pointed out below, the problems the bankers must address are formidable. Whether and how fast they will move forward will depend to a great degree on the Government's resolve in continuing to make the difficult decisions necessary for the continued success of the N.E.P., including dealing directly with the financial sector's difficulties.

1. Impact of DeDollarization

In November 1982, the Bolivian Government issued a decree which prohibited the banking system from operating in US dollars. As a result, all US dollar debts in Bolivia were to be liquidated at the official rate of exchange, in Bolivian pesos. At the time, the official rate of exchange was roughly one quarter of the exchange rate on the parallel market. The immediate effect of this decree was to enable clients who had borrowed from Bolivian banks in US dollars to repay their loans to the banks in Bolivian pesos at extremely favorable exchange rates. By the same token, people holding US dollar deposits in the banking system were also to be paid off by the banks at the official exchange rate. When this occurred, the savings of many bank depositors were wiped out.

The principal dollar funding source for the dollar and dollar-tied loans which had been made by the banking system to local clients were borrowings from foreign banks. The dedollarization decree had a clause which called for the Central Bank to pay the foreign loans of the banks upon presentation of payment in pesos at the official exchange rate by the local banks. However, when local bankers made peso deposits in the Central Bank, the Central Bank refused to honor the local banks' payment requests.

Subsequent devaluations have further reduced the real value of Bolivian banks' assets which made it even more difficult to repay the debt. Some foreign creditors did receive payment for their dollar loans to the Bolivian banks, most likely from the Bolivian banks themselves, because the Central Bank did not make payment. However, the Bolivian banks still legally owe approximately US$67.5 million to foreign creditors. The dollar debt continues to appear as a liability on the books of the banks. If the banks were to actually pay this debt from their own resources, they would all be formally bankrupt. The potential losses to be accounted for by the banks are US$67.5 million against the

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total banking system capital equivalent of US$42 million as of December 31, 1986. On the other hand, it should be realized that if the debt were in fact paid for them (assumed by the Central Bank), this would cause only superficial strengthening of their balance sheets and would not correct the many operational weaknesses in their structure. Improved profitability would not automatically return, as many bankers contend.

Dedollarization also had a more far reaching effect on the banking system concerning access to foreign bank credit lines. As foreign banks have not been repaid in over four years, they have almost totally cut off all new financing to the Bolivian banking system. These credit lines were previously a primary source of funding for medium and long-term credits and the Bolivian banks must now depend almost solely on internal resources (e.g. refinancing lines) to fund their term loans. The availability of only short-term deposits causes the banks to extend only short-term (60-90 days maximum) commercial credits. While, several banks have had access to refinancing lines through the Development Department of the Central Bank, the availability of these credits has diminished because the refinancing lines were decapitalized during the hyperinflationary period. It is obvious that any long-term stabilization and recovery program for the Bolivian banking system must include access to international funding sources and increase term lending activities. For this to happen, a resolution of the dedollarization problem is a prerequisite.

There continues to be strong opposition within certain Government circles to GOB assumption of this debt. Many realize that the owners of the Bolivian banks profited greatly, both directly and through their various companies, from the dedollarization decree. They were able to make speculative gains using refinanced credits with negative interest rates, and they were able to "clean up" the balance sheets of their companies by repaying dollar debt in devalued pesos. Therefore, there is some GOB opposition to further "bailing out" of the banks on this issue which is reinforced by the realization that the direct payment of this debt would have a very negative effect on the country's reserves, its agreements with the IMF, and its debt negotiations with other creditors and creditor nations. Nevertheless, it will have to be addressed (probably through a compromise of some sort) in order for Bolivia's banks to begin to become financially solvent again.

2. Impact of Hyperinflation

During the hyperinflationary period, the rate of inflation served to reduce the real levels of overhead at the banks. This reduction in personnel costs and operating expenses had the immediate effect of encouraging banks to expand their branch operations. In fact, during the hyperinflationary period, many banks increased personnel, expanded their branch networks, and embarked upon capital expenditure programs such as the purchase of computer systems and the construction of new premises.

In August 1985, when the N.E.P. was put into effect, and high inflation was brought to halt, speculative demand for local currency dried up, and money supply growth was curtailed. As prices readjusted closer to worldwide levels, the Bolivian banks found themselves caught in a situation where:

- Total assets had declined to a fraction (one tenth) of pre-inflation levels. Earning assets had been decimated.
- Excess personnel and branches were generating expenses out of proportion to the earning assets of the banks.
- Real estate purchased during the hyperinflationary years as a hedge against inflation became a drag on profitability, as real estate values weakened. Revalued real estate assets, not producing daily income on the profit and loss statement, became an important negative factor affecting bank profitability.

With hyperinflation, even though interest rates were negative, banks could continue to produce profits as long as they were able to obtain a positive spread large enough to cover overhead and operating expenses. Inasmuch as overhead and operating expenses had dropped dramatically in real terms, banks survived fairly well in spite of the fact that inflation was rapidly eroding the real value of total assets, liabilities and capital of the banks. In 1986, rising real costs and diminished earning assets put a tremendous squeeze on the ability of the banks to remain profitable.

3. Severe Undercapitalization

As a direct result of the hyperinflationary period, Bolivian banks are now severely undercapitalized. This has occurred due to actual operational (loan) losses and the restructuring of capital accounts through increasing revaluation reserves. In the latter case, banks revalued fixed assets purchased during the inflationary period and reported these theoretical increases in market value as an increase in capital.

While it is recognized that the revaluing of fixed assets is a fairly common and accepted accounting principle in Latin America, the Bolivian banks utilized this accounting mechanism to the extreme. This type of revaluation reserve should not be considered equal to actual paid-in capital or retained earnings because real estate must be sold to generate cash. This is particularly important in the case of a bank (as opposed to manufacturing corporations, for example) as the capital of a bank is used to support its lending operations. The condition of the capital account is the measure of a bank's financial strength and ability to withstand losses in its loan portfolio.

The capital structure of Bolivian banks is particularly weak. Out of a total reported capital base of US$42.8 million, US$37.5 million is "capital" from revaluations. Conversely, actual paid-in capital, representing the shareholders' direct risk capital, is only US$3.9 million or 10.7 percent of total capital. When the recent profitability trends of the banking system are analyzed, it is disturbing to realize that the system reported total losses of US$3.8 million for 1986. When this is combined with accumulated losses of US$5.6 million for past periods, it can be seen that the Bolivian commercial banks have lost 22 percent of their reported capital over the past three years. If one considers only paid-in capital, the system has actually lost these funds more than 2.4 times in the same period.

Given that inflation for 1986 is estimated to have been between 35 and 65 percent, the banks' decision to maintain large real estate holdings through 1986 is understandable. One expects that with continued economic stability in 1987, the banks are already beginning to liquidate these assets. Nevertheless, this does not alter the fact that currently bank "reserves" are excessively invested in real estate. This situation is aggravated by the fact that the market value of these assets appears to have declined during 1986, and the values now reported on their books may be higher than the actual cash their sale will generate.

4. <u>Cost Structure of Commercial Banks</u>

For the 12-month period ending December 31, 1986, total operating expenses of the banking system as a percentage of average total earning assets was slightly in excess of 13 percent p.a. This is a significantly high number because it implies that, on average, banks must make a gross spread on their earning assets in excess of 13 percent p.a. in order to produce a profit.

The table below lists the banks in order of efficiency of their operating cost structure.

TABLE 1

Operating Costs as a Percentage of Earning Assets

Bank	Total Earning Assets (US$000 equivalent)	Total Costs as a % of Earning Assets
Banco de Cochabamba	35,433	7
Banco Hipotecario	23,884	9
Banco de Santa Cruz	47,929	11
Banco de la Unión	23,088	11
Banco de La Paz	17,414	13
Banco Boliviano-Americano	26,394	14
Banco Nacional	26,922	16
Banco de Crédito Oruro	29,207	16
BIG Beni	16,372	16
Banco Mercantil	19,329	17
Banco de Potosí	7,425	21
Banco del Progreso Nacional	4,958	26

There are two interesting conclusions to be drawn from the above table.

a. There does not appear to be much deviation in spreads among the banks. In general, most of the banks are within two to three percentage points of the average (13 percent).

b. In general, it appears that the larger banks can operate with proportionately lower operating expenses. This indicates that most banks in the system need to achieve greater economies of scale in their operations. Although all banks have been severely affected by real increases in administrative and operating expenses, the larger banks have been able to adjust in response to asset shrinkage.

Through interviews with bankers, it was learned that the banks initially reacted slowly to cut costs following the implementation of the N.E.P. Only when the seriousness of the cost increases became evident in the beginning of the second quarter of 1986 did banks begin to cut costs by closing mini-branches and reducing staff. Some banks reported staff reductions of 40 to 50 percent. Nonetheless, the impact of administrative and operating expenses on the Bolivian banks remains quite severe.

TABLE 2

Operational Costs of Bolivian Commercial Banks
(US$000 equivalent)

(for the year ending 12/31/86)

Total Personnel Expenses / Total Income	$13.6 million / $85.9 million	=	16%
Total Personnel Expenses / Total Expenses	$13.6 million / $88.8 million	=	15%
Total Administrative Expenses / Total Income	$12.8 million / $85.9 million	=	15%
Total Administrative Expenses / Total Expenses	$12.8 million / $88.8 million	=	14%

These extremely high cost structures are the most important factor in the decision of the banks to maintain high spreads. At this point, it is not likely that the banks can realistically cut expenses much further. Clearly, the effort to reduce costs as a percentage of earning assets will have to be based on increasing assets back towards pre-1982 levels. Cost reductions, while important to overall bank profitability, do not appear to be the key to revitalizing the banks, although they continue to be important. Rather, the key is to reach higher operating levels where economics of scale can allow them to reduce their spreads to a level of 3 to 5 percent.

5. Spread Management

Almost half of Bolivian commercial banks are currently reporting operating losses. This is an alarmingly high level of unprofitable institutions in any system. In comparing the operations of the profitable and the non-profitable banks, the most striking differences in their operations can be seen in the management of interest rate spreads.

The table below illustrates the relationship between profitability (Return on Equity) and gross spread (Net Revenue) as a percentage of earning assets.

TABLE 3

Profitability and Gross Spread

Bank	Profitability Ranking	Profitability ROE	Gross spread as a % Earning Assets
Banco del Progreso Nacional	1	52	44.2
Banco de la Union	2	37	15.2
Banco Hipotecario	3	27	14.5
BIG Beni	4	9	17.1
Banco Mercantil	5	5.3	19.3
Banco de Santa Cruz	6	2.1	11.5
Banco de La Paz	7	1.2	13.8
Banco de Credito Oruro	8	(.4)	4.8
Banco de Cochabamba	9	(.8)	7.5
Banco Nacional	10	(7.7)	2.8
Banco de Potosí	11	(11.2)	1.3
Banco Boliviano-Americano	12	(11.9)	12.4

Clearly, there is a very close relationship between overall profitability and spread management. It is apparent that current cost structures require a break-even spread of 11 to 13 percent. All banks, with the exception of the Banco de Santa Cruz, reported losses when gross spreads were below 13 percent.

6. High Delinquency Rate/Non-Performing Loans

While there are many financial indicators which are useful in assessing the financial health of a banking institution, by far the most important are quality of loan portfolio and profitability. Few banks get into serious permanent difficulties because of deficiencies in their

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liquidity structure (an indication of a bank's ability to meet depositor obligations) or deficiencies in their capital structure (an indication of a bank's ability to withstand sudden unexpected losses) <u>unless they are concurrently having difficulties producing a real profit</u>.

One of the difficulties in assessing a bank's profitability is that there are a myriad of ways that its management can disguise losses through manipulation of the bank's asset portfolio. Indeed, by rolling over past due loans or by accruing interest on non-performing credits, banks can appear to be generating profits while they should, in fact, be reporting losses.

By law, all banks are required to cease interest accruals on loans classified as "past-due in execution." This loan classification includes all loans past due 30 days or more. There is considerable doubt that the banks are accurately reporting this loan category, and they may, in fact, be rolling over many short-term loans and capitalizing interest payments due. The extent of this practice cannot be accurately determined without an in-depth audit and portfolio examination. Nonetheless, the banks' own financial statements report an extremely high percentage of non-performing loans. The industry average of non-performing assets to total assets was 17 1/2 percent for the period ending December 31, 1986.

Generally, a bank whose portfolio has deteriorated to the point that its loans are no longer producing income will necessarily register lower gross spreads. The table below shows the ranking of the banks based on the apparent quality of their loan portfolios as measured by their past due indicators.

TABLE 4

Portfolio Quality

Bank	% of Portfolio Past Due
Banco de Credito Oruro	65
Banco Nacional	27
BIG Beni	24
Banco de Cochabamba	22
Banco Boliviano-Americano	20
Banco de Potosí	14
Banco Hipotecario	9
Banco Mercantil	7
Banco de La Paz	6
Banco de Santa Cruz	5
Banco del Progreso Nacional	5
Banco de la Unión	5

There is a real cost to a bank (carrying cost) when it has to continue to fund a non-performing loan. A quick analysis of this carrying cost shows that the total past due loans for the Bolivian commercial banks totalled US$27.9 million at year-end. This represents approximately 10 percent of the total loan portfolio in the system. The system average cost of funds (as of December 31, 1986) was 16.6 percent p.a. for US dollar loans. As a result, the annual average cost to carry these non-performing loans would be approximately US$4.63 million. This figure represents 5 percent of the total income of the system and 9.5 percent of the banks' total interest expenses for the year. Obviously, an improvement in the quality of the loan portfolio would have an immediate positive impact on the banks profitability.

Loan loss reserves are not clearly reported on most bank financial statements and are normally included in the gross total of other liabilities. Further research of loan loss reserve levels shows that with the possible exception of Banco Nacional these reserves are totally inadequate.

TABLE 5

Loan Loss Reserves

Bank	% of Portfolio Past Due	% Loss Reserves to Total Portfolio
Banco de Credito Oruro	65	1.5
Banco Nacional	27	19.23
BIG Beni	24	.04
Banco de Cochabamba	22	1.11
Banco Boliviano-Americano	20	3.22
Banco de Potosí	14	.76
Banco Hipotecario	9	.69
Banco Mercantil	7	1.11
Banco de La Paz	6	.40
Banco de Santa Cruz	5	1.24
Banco del Progreso Nacional	5	.59
Banco de la Unión	5	.29

It is obvious that the Bolivian banks must increase their loss reserves to more prudently cover the potential losses from their past-due portfolio. This will be an additional cost to the banks' operations and illustrates the extremely weak structural condition of the Bolivian banking system.

7. Inefficient Use of Borrowed Resources

The greater the proportion of a bank's sources of funds invested in its loan portfolio as opposed to other non-earning assets, the greater its earning efficiency. As a worrisome corollary to the above, any bank with a significant disparity between sources (deposits) and uses (loans) and which is concurrently losing money may be showing that disparity because its fund sources are being incorrectly utilized to defray current operating expenses.

A study of the deposit and loan structure of the Bolivian banking system yields the following data:

TABLE 6

Loans as a Percentage of Deposits

Bank	Net Sources Minus Uses (Deposits Minus Loan Portfolio) (US$000 equivalent)	% of Total Sources
Banco de Crédito Oruro	5,705	31
Banco Boliviano-Americano	15,902	39
Banco de La Paz	4,255	27
Banco de Potosí	2,008	30
Banco de la Unión	6,004	23
Banco Mercantil	6,921	28
Banco Hipotecario	4,326	21
Banco de Cochabamba	4,690	26
Banco de Santa Cruz	1,944	5
Banco Nacional	7,567	25
BIG Beni	6,922	42
Banco del Progreso Nacional	(109)	0

This analysis shows that there are dramatic differences in the financial structure of the banks. Many banks have significant gaps in their loan-to-deposit structures. From this data it appears that

Bolivian banks are using their growing deposits in several contradictory and non-productive ways.

The table below also shows a wide disparity in the asset composition of Bolivian banks.

TABLE 7

Non-Earning Assets
as a Percent of Total Assets

Bank	Percentage
Banco de Santa Cruz *	60
Banco del Progreso Nacional	57
Banco de Potosí	51
Banco Mercantil	51
Banco Hipotecario	50
Banco Boliviano-Americano	44
Banco Nacional	42
BIG Beni	39
Banco de La Paz	39
Banco de Crédito Oruro	36
Banco de la Unión	33
Banco de Cochabamba	23

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* It is probable that Banco de Santa Cruz's unfavorable ranking (above) is the result of almost US$32 million which this bank has in "Other Cash" and "Other Assets." It is believed that a substantial portion of these assets are supporting the operations of the bank's Panamanian affiliate and as a result the bank's local earnings may be understated because the earnings from these assets are, in fact, accruing to the affiliate.

Clearly, the smaller banks, (Progreso and Potosí) and the medium-sized banks (Mercantil, Hipotecario and BIG Beni) will have higher percentages of their total assets invested in fixed assets (buildings and equipment). As these banks are able to increase their earning assets and grow to a size that will permit economies of scale they should be able to invest more and more of their deposits in earning assets. In a normal economy, larger banks such as Banco Nacional, Banco Boliviano-Americano and Banco de Santa Cruz should be performing much more efficiently than is indicated by the data above.

The figures nonetheless show that the banks are operating extremely inefficiently. In order for the banks to be able to reduce spreads to the 3 to 5 percent level, higher proportions of their total assets must be invested in earning assets.

8. Swap Activities and Dollar Dependency

The Bolivian banks once again find themselves operating in a free exchange market which allows them to take in dollar-denominated deposits and extend credit which is also dollar-based. There is a difference between interest rates on dollar-based and local-currency-based transactions. Deposit growth has been significant over the past 18 months; however, over 70 percent of this growth has been in dollar or dollar-equivalent deposits. Deposit and loan rates also vary significantly between dollar and local currency transactions. This phenomenon has allowed the banks to engage in "exposed swap activities" within their portfolios.

Currently, a Bolivian bank generating sources of funds (deposits) in US dollars and lending in bolivianos can increase its profitability by attracting its sources at the lower interest rate paid on US dollar deposits and making loans at the higher lending rate in bolivianos. In this case, the bank runs the risk of suffering an exchange loss in the event of a devaluation. Conversely, if a bank primarily generates its sources of funds in bolivianos by paying the higher rate of interest on boliviano deposits and makes loans in dollars at a lower rate of interest, then the bank is sacrificing its profitability on a day-to-day basis. As a result, the bank's overall loan spread will be low. However, in the event of the devaluation of the boliviano, the bank is in a position to make a substantial foreign exchange gain.

Both swap transactions described above have advantages and disadvantages depending upon whether or not there is, in fact, a devaluation. Prudent banking practices generally call for not engaging in such uncovered swaps and reducing exchange risk by matching assets and liabilities in each currency. Because there has been such a growth in dollar-denominated deposits, it appears that several banks are in fact engaging in the dollar deposit and peso loan swap activity described above.

As Bolivian banks continue to show significant deposit growth, their increasing dependency on dollar-denominated funding sources holds the potential for future problems. As of December 31, 1986, dollar deposits and local currency deposits with dollar value guarantees accounted for 65 percent of the total deposits in the private commercial bank sector. In some banks, notably Banco Boliviano Americano and Banco de Santa Cruz, this ratio is 72 percent and 94 percent, respectively, which is an extremely dangerous position to maintain in a country that does not produce significant foreign exchange in the legal private sector. The common notion that these banks are recapturing flight capital is not as believable as the theory that most dollar deposits currently generated are in fact funds that have not yet left the country.

Most of the Bolivian banks appear to have been matching their assets and liabilities by currency of exposure, i.e., dollar sources of funds are being used to fund loans in dollars, and boliviano sources are being used to fund loans in bolivianos. In this way, banks can theoretically maintain a hedged position. In the event of a devaluation, losses resulting from relative increases in the value of dollar-denominated bank liabilities should be offset by equivalent increases in the values of dollar-denominated assets. The fallacy in this theory comes about when the devaluation impact on dollar borrowers is so great that they cannot generate sufficient local currency income to pay back dollarized debt at the new exchange rate. Loan defaults are likely to occur, and simultaneously the banks can find themselves unable to meet dollar deposit obligations in a timely manner.

Although deposit rates have declined significantly over the past year, Bolivian banks are still "buying" dollar deposits by offering extremely high interest rates. Currently, deposits in dollars earn between 1.2 to 1.5 percent per month which is approximately three times the dollar rate in the international market. These rates are for short-term deposits (30 to 60 days), as depositors and investors continue to be unwilling to accept the longer-term political and financial risks of Bolivia. Consequently, banks have ceased virtually all term lending and are at best only marginally satisfying the credit demands of the country with very high cost, short-term working capital loans. Several banks are reporting significant commission income from fees charged each time these short-term credits are renewed.

The net result of this double-edged sword of high interest rates on short-term deposits and expensive short-term credits is an extremely fragile financial system which could further deteriorate or even collapse with any major shift in economic performance. The deposit base is highly volatile and rate sensitive. Deposits could dissipate rapidly. Loan portfolios are of suspect quality because the relatively high cost of borrowing tends to drive away all but marginal borrowers or related corporations. If there is a major devaluation, borrowers may not be able to repay their dollar loans at a new exchange rate. In the worst-case scenario, all the elements exist for another dedollarization of the financial system.

AID 1020-28 (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.)

Project Title & Number: STRENGTHENING FINANCIAL MARKETS 511-0598

Life of Project:
From FY 1987 to FY 1991
Total U.S. Funding $6,200,000
Date Prepared: April 1987

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 improve the performance of Bolivia's financial sector.	- increased domestic savings in Financial System - increased term lending to private sector firms - better financial sector - policies - ICIs well regulated - Better functioning ICIs - Better functioning BCB	ICI audits Evaluations of operations of financial sector BDIF and Superintendency records Baseline information and bench-marks to measure the project contributions towards the goal will be established shortly after the start of Project implementation.	- Banking law, if required, will be passed - political stability - GOB economic policies stay in place - WB and IDB projects successful - GOB makes financial sector policy choices in timely fashion - ICIs respond to NEP-generated opportunities - public regains confidence in ICIs - Successful WB and IDB projects will lead to closing/reorganization of public sector banks

AID 1020-28 (7-71)
SUPPLEMENT 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY 1987 to FY 1991
Total U.S. Funding $6,200,000
Date Prepared: April 1987

Project Title & Number: STRENGTHENING FINANCIAL MARKETS 511-0598

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 improve the effectiveness of Bolivia's private sector financial institutions, and to increase private sector participation in financial sector policy formulation.	- improved loan analysis and monitoring, more deposits, lower transaction costs, wider operations (geographic and clients), bigger loan portfolios, closer adherence to banking regulations and sound banking practices, improved operations of ICIs, regular accurate audits. - deposit insurance scheme functioning. - stronger ASOBAN. - FIC operating well. - Regular private-public policy discussions and better understanding/acceptance of financial sector policies.	ICI audits. Deposit insurance scheme records. Bank consolidation records. ASOBAN reports, activity evaluations. IDEA course records. Policy seminar and meeting records. Project evaluations.	- staffs and executives of ICIs respond to training. - public responsive to savings campaigns. - Banks willing to take consolidation measures and modify operations. - Banks responsive to ASOBAN programs. - seminars, research lead to improved policy measures.

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AID 1020-28 (7-71)
SUPPLEMENT 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY 1987 to FY 1991
Total U.S. Funding $6,200,000
Date Prepared: April 1987

Project Title & Number: STRENGTHENING FINANCIAL MARKETS 511-0598

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Outputs:	Magnitude of Outputs:		Assumptions for achieving outputs:
- FTC established	(X)		
- ICI officers trained	(1,300)	FTC course records	- banking law or Supreme Decree passed.
- FTC courses held.	(68)	Savings campaign records	- IDEA keeps functioning well.
- Savings mobilization campaigns (FENACRE)	(3 to 5)	ASOBAN program reports	- inputs available on time.
- new ASOBAN services initiated	(6)	External audit reports	- savings mobilization campaigns well designed.
- external bank audits done	(21)	Legal documents for deposit insurance scheme	
- BDIF established.	(x)		- good audit firms contracted on time.
- seminars	(12)	Seminar, research and training documents	
- studies.	(13)		- bank records are minimally adequate for audits
- policies implemented	(3 to 12)		- qualified deposit insurance staff found.
- capital markets study	(1)		- Superintendencia restarted
- capital market instruments developed	(1 to 5)		- professors, students interested and available for research - ICIs release employees for training and pay part of cost.

AID 1020-28 (7-71)
SUPPLEMENT I

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY 87 to FY 91
Total U.S. Funding $6,200,000
Date Prepared: April, 1987

Project Title & Number: STRENGTHENING FINANCIAL MARKETS 511-0598

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS		MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Inputs:	Implementation Target (Type and Quantity)			Assumptions for providing inputs:
	AID ($000)	GOB		
I. BDIF				
a. T.A. (48 p.m.)	1,032		Project accounting records. Project audits.	AID, GOB and private sector funds available for the Project.
b. Bank Audits	243	188		
c. Capitalization		26,014		
d. Operating Costs		1,327		
e. Commodities	40			
f. Staff Training	54			
II. FTC				
a. T.A. (36 p.m.)	677			
b. Course Costs	561	484		
c. Staff Training	45			
d. Operating Costs	79	60		
e. Commodities	80			
III. ASOBAN Services				
a. T.A. (18 p.m.)	316			
b. Staff Training	30			
c. Operating Costs		308		
d. Commodities	47	5		
IV. Savings Mobilization				
a. T.A. (49.5 p.m.)	711			
b. Staff Training	12			
c. Operating Costs		70		
V. Policy Research and Analysis				
a. T.A. (12 p.m.)	107			
b. Commodities	27			
c. Seminar/Research Cost	585	17		
VI. Other Costs				
a. Evaluations and Audits	130			
b. Project Coordinator (36 p.m.)	324			
c. T.A. Chief of Party (36 p.m.)	706			
d. Contingencies	394	172		
Total	6,200	28,645		

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ANNEX C

COST ESTIMATE DETAILS *

I. BOLIVIAN DEPOSIT INSURANCE FUND

A. Technical Assistance.

1. Short- and long-term Technical Assistance

One long-term, two-year advisor will be provided as well as 24 person months of short-term assistance under an institutional contract. Salary is calculated at $69,976 per year ($269.14 per day) for both long-term and short-term advisors. A multipler of 3 has been applied to base salary costs.

Total costs for the long-term advisor have been calculated as follows:

Salary	139,952
Overhead	279,904
Benefits	10,000
Post Differential	34,988
Education, Housing, TQA	40,000
Transportation of HHE	23,000
Travel and Per Diem	12,000
Other Direct Costs	5,000
Fixed Fee	5,000
Total	549,844

For short-term technical assistance eight round-trip airfares at $1,500 each ($12,000) have been calculated along with $50,370 in per diem (730 days x $69.00/day).

2. Bank Audits.

Audits of all Bolivian banks have been calculated at $750,000. AID will finance 75 percent, $562,000, of the total cost of the audits. This $562,000 has been divided between the Agribusiness and Artisanry Project (511-T-060), $320,000, and this Project, $242,500. The remaining 25 percent, $187,500 (which represents the approximate cost of the audits of the state banks) will be financed by the GOB.

* All figures in the consolidated tables and in the supporting tables have been rounded to the nearest one-hundred.

B. Training.

Two trips to Washington, D.C. for two people per year for three years are budgeted. Airfare is projected to be $3,000, course costs $6,300 and per diem $4,700 ($112/day x 21 days x 2).

Also included are three Latin American trips projected at $4,000 each for three years beginning in year 2.

C. Project Operating Costs.

A total of $1,127,254 for four years of staff salary and benefits have been calculated. Initial staff salaries are as follows:

1 Fund Director	$ 40,000/year
1 Senior Financial Analyst	35,000/year
4 Financial Analysts, $15,500/yr each	62,000/year
1 Controller - Investment Officer	17,000/year
1 Accounting clerk	10,000/year
1 Corporate Attorney	25,000/year
2 Secretaries-Administrative Assistants, $7,000/yr each	14,000/year
1 Messenger	2,000/year
	$205,000/year

Salary and benefits are projected to increase at 15 percent per year as more staff is hired. Rent has been calculated at $61,250 ($15,313 per year). General and Administrative costs (G&A) are calculated at $10,208 per year or $40,833 over the life of the component. Travel has been calculated at $9,000 per year or $36,000 over the life of the component. Legal services are calculated at $61,250.

D. Commodities.

Office furniture and office equipment are to be provided for a total of $10,000.

Two microcomputers with software are to be provided at $5,000 each. Approximately $20,000 will be utilized to obtain technical assistance to establish on-line operating procedures as well as follow-up systems development.

E. Capitalization.

A total of $26,014,000 is projected over the four-year life of the component. This consists of a GOB loan of $500,000 and insurance premiums from the member banks of $25,514,000 minus $1,326,587 (EDIF operating costs).

II. FINANCIAL TRAINING CENTER

A. Technical Assistance.

One long-term, two-year advisor will be provided as well as 12 person months of short-term technical assistance under an institutional contract. Salary is calculated at $69,976 per year ($260.14/day). A multiplier of 2.4 has been applied to base salary costs.

Total costs for the long-term advisor have been calculated as follows:

Salary	139,952
Overhead	195,933
Benefits	10,000
Post Differential	34,970
Education, Housing, TQA	40,000
Travel and Per Diem	12,000
Transportation of HHE	23,000
Other Direct Costs	5,000
Fixed Fee	5,000
Total	465,855

For short-term technical assistance, salaries have also been calculated at $269.14 per day. In addition, 12 round trips have been estimated at $18,000 ($1,500/trip) with per diem at $25,185 (365 x $69.00)

B. Staff Training.

Three trips per year at $5,000 per trip have been calculated over the three-year period: $5,000 x 3 = 15,000 x 3 = $45,000.

C. Course Delivery Costs.

1. Course - Related Costs

Each course has three cost components, as follows:

IDEA Overhead. The total overhead expenses of IDEA (salaries of administrative staff, administrative expenses, such as stationery, telephone, depreciation of furniture and equipment, insurance and rent) were allocated to all courses offered by IDEA, including those to be offered by the FTC, based on the duration of each course, in number of hours. The total overhead expenses of IDEA were calculated as $511,504 and the total number of hours estimated at 3,000. Overhead cost per hour is therefore $170.54. Twenty percent of this cost per hour has been applied to FTC courses, for a total of $34.10 per course hour.

Delivery Costs. This is the actual cost charged by the corporation, firm, or consultant for the delivery of a course. It includes instructor time, original course materials, cases, simulations, and all per diem and travel expenses. Delivery costs are based on rates currently charged for international seminars by corporations such as Systema Inc. in Puerto Rico, Banco Internacional de Colombia, and Citibank.

Other Operating Expenses. These are miscellaneous costs such as duplication of material, readings, purchase of texts, binders, and necessary materials, coffee service, social activities at opening and closing of courses, advertising, etc. Based on historical data available at IDEA and the complexity and duration of the courses, we have estimated a total of $74 per participant per course.

YEAR 1- COURSE COSTS

Senior-level (5 offerings)

Fixed costs (120 hours x $34.10)	$ 4,092
Delivery costs ($20,000 each)	100,000
Other (75 participants x $74)	5,550
	$109,642

The following is an estimate of the breakdown of the costs charged by firms or consultants for delivery of senior-level courses in the first year:

-Salaries (2 instructors, 10 days $270 p/day)	$ 5,400
-Overhead	6,480
-Travel	3,000
-Per diem	1,380
-Preparation of material at HQs	2,500
-Other Direct Costs	1,240
	$20,000

Mid-level (10 offerings)

Fixed costs (400 hours x $34.10)	$ 13,640
Deivery costs ($15,000 each)	150,000
Other (200 participants x $74)	14,800
	$178,440

The following is an estimate of the breakdown of the costs charged by firms or consultants for the delivery of mid-level courses in the first year.

-Salaries (2 instructors, 8 days $270 p/day)	$ 4,320
-Overhead	5,184
-Travel	3,000
-Per diem	1,104
-Preparation of material at HQs	1,000
-Other direct costs	392
	$15,000

Lower-level (10 offerings)

Fixed costs (480 hours x $34.10)	$ 16,368
Delivery costs ($10,000 each)	100,000
Other (200 participants x $74)	14,800
	$131,168

The following is an estimate of the breakdown of the costs charged by firms or consultants for the delivery of lower-level courses in the first year.

-Salaries (2 instructors, 7 days, $190 p/day)	$ 2,660
-Overhead	3,192
-Travel	3,000
-Per diem	966
-Preparation of material	182
	$10,000

Total course costs in Year 1 are $419,250

The delivery of the courses will be done 100 percent by an outside firm or consultant during the first year. AID will pay 75 percent of the total costs or $314,438. IDEA will pay 25 percent of the total costs or $104,812.

YEAR 2 - COURSE COSTS

Senior-level (4 offerings)

Fixed costs (120 hours x $34.10)	$ 4,092
Delivery costs ($10,100 each)	40,400
Other (75 participants x $74)	5,550
	$ 50,042

The following is an estimate of the breakdown of the costs charged by firms or consultants for the delivery of senior-level courses in the second year:

-Salaries (2 instructors, 1 foreign, 1 local, 10 days, $150/day each	$ 3,000
-Overhead	2,400
-Travel	1,500
-Per diem	690
-Preparation of material	1,000
-Other	1,510
	$ 10,100

Mid-level (11 offerings)

Fixed costs (400 hours x $34.10)	$ 13,640
Delivery costs ($7,280 each)	80,080
Other (200 participants x $74)	14,800
	$108,520

The following is an estimate of the breakdown of the costs charged by firms or consultants for the delivery of mid-level courses in the second year:

-Salaries (2 instructors, 1 foreign/1 local, 8 days $150/day	$ 2,400
-Overhead	1,920
-Travel	1,500
-Per diem	552
-Preparation of material	908
	$ 7,280

Lower-level (10 offerings)

Fixed costs (480 hours x $34.10)	$ 16,368
Delivery costs ($4,020 each)	40,200
Other (200 participants x $74)	14,800
	$ 71,368

The following is an estimate of the breakdown of the costs charged by firms or consultants for the delivery of lower-level courses in the second year:

-Salaries (2 instructors, 1 foreign, 1 local, 7 days - $90/day each	$ 1,260
-Overhead	840
-Travel	1,500
-Per diem	420
	$ 4,020

Total course costs for Year 2 are $ 229,930

The delivery of the courses will be done 100 percent by an outside firm or consultant, using a combination of foreign and local instructors as available. This is the reason we have budgeted lower delivery costs. AID will cover 50 percent of the total course costs or $115,150.

YEAR 3 - COURSE COSTS

Senior Level (3 offerings)

Fixed costs (72 hours x $34.10)	$ 2,455
Delivery costs ($5,400 each)	16,200
Other (45 participants x $74)	3,330
	$ 21,985

The following is an estimate of the breakdown of the costs charged by firms or consultants for the delivery of senior-level courses in the third year:

-Salaries (2 instructors-10 days, $100/day	$ 2,000
-Course material	2,000
-Other	1,400
	$ 5,400

Mid-level (8 offerings)

Fixed costs (320 hours x $34.10)	$ 10,912
Delivery costs ($4,380 each)	35,040
Other (160 participants x $74)	11,840
	$ 57,792

The following is an estimate of the breakdown of the costs charged by firms or consultants for the delivery of mid-level courses in the third year:

-Salaries (2 instructors-10 days,$100/day	$ 2,000
-Course material	$ 1,000
-Other	$ 1,380
	$ 4,380

Lower-level (7 offerings)

Fixed costs (360 hours x $34.10)	$12,276
Delivery costs ($2,520 each)	17,640
Other (140 participants x $74)	10,360
	$40,276

The following is an estimate of the breakdown of the costs charged by firms or consultants for the delivery of lower-level courses in the third year:

-Salaries (2 instructors-10 days, $80/day each	$ 1,600
-Course material	800
-Other	120
	$ 2,520

Total course costs for year 3 are $120,053

The delivery of the courses will be done 100 percent by local firms or consultants using foreign instructors as required.

AID will pay 30 percent of the total course costs or $36,021. IDEA will pay 70 percent of the total course costs.

2. Course Revenue

Course revenue has been projected for the life of the project as follows:

YEAR 1

5 Senior Level Programs x 15 participants x $500	$ 37,500
10 Mid-Level Programs x 20 participants x $400	80,000
10 Lower-level Programs x 20 participants x $300	60,000
Output: 25 offerings/475 participants	$177,500

YEAR 2

4 Senior Level Programs x 15 participants x $500	$ 30,000
11 Mid-Level Programs x 20 participants x $400	88,000
10 Lower-Level Programs x 20 participants x $300	60,000
Output: 25 offerings/480 participants	$178,000

YEAR 3

3 Senior Level Programs x 15 participants x $500	$ 22,500
8 Mid-Level Programs x 20 participants x $400	64,000
7 Lower-Level Programs x 20 participants x $300	42,000
Output: 18 offerings /345 participants	$128,500
Total Revenue	$484,000

D. FTC Operating Costs.

Total operating expenses for the FTC are calculated at $138,913 of which AID will pay $78,872 and IDEA $60,041. Staff salaries are calculated as follows: 1 Academic Director $19,500; 1 Academic Assistant $13,000; 1 Secretary $3,900 and 1 logistics clerk $1,950. These salaries reflect current salary levels at IDEA. An annual increase of 4 percent is assumed. Other operating costs include travel and per diem ($9,600 over the life of the project) stationery, insurance, and miscellaneous costs for a total of $19,200.

E. Commodities.

Furniture for additional staff has been calculated at a fixed, one-time cost of $10,000. Ten microcomputers with software have been calculated at $5,000 each for a total of $50,000. Library materials consisting of case studies, testing materials, and teaching aids have been calculated at a fixed, one-time cost of $20,000.

III. ASOBAN

A. Technical Assistance.

Short-term technical assistance for a period of 18 person months under an institutional contract is planned. Salary is calculated at $269.14/day. A multiplier of 2.4 has been applied to base salary costs. Eighteen trips at $1,500/trip are budgeted at $27,000 per diem is calculated at $37,260 ($69.00 x 540).

B. Training.

A total of $30,000 has been budgeted for ASOBAN staff training. Two trips per year at $5,000/year are calculated over the three-year life of project to visit U.S. and Latin American banking associations.

C. Project Operating Costs.

The following table details the cost of operating the six new services of ASOBAN:

Service	Year 1	Year 2	Year 3	Total
1. Central Information				
a.Manager	19,080	19,843	20,637	59,560
b.Programmer	12,720	13,228	13,757	39,705
2. Economics Unit				
Economist	19,080	19,843	20,637	59,560
3. Check Clearing				
1 Professional	12,720	13,228	13,757	39,705
4. Legal Unit				
Lawyer	19,080	19,843	20,637	59,560
5. Personnel Selection				
Half-Time Professional	7,950	8,268	8,599	24,877
6. Library				
Half-Time Professional	7,950	8,268	8,599	24,817
Total	98,580	102,521	106,623	307,724

Unit costs are calculated to include 94 percent for salary and 6 percent for operational support such as stationery, mail, supplies, insurance, etc. For example, in Year 1 the staff lawyer salary is $18,000 and $1,080 is for operational support. For Years 2 and 3, an inflation rate of 4 percent has been calculated.

D. Commodities.

Four microcomputers at $5,000 each are to be provided to the Central Information, Economics and Check Clearing units. In addition, $12,000 has been included for telecommunications modern equipment for the individual microcomputers.

IV. SAVINGS MOBILIZATION

A. Technical Assistance.

One long-term, two-year advisor will be provided to FENACRE as well as 18 person months of short-term assistance under an institutional contract. Salaries for both short and long-term advisors are calculated at $52,000 per year ($200/day). A multipler of 2.4 has been applied to base salary costs.

Total costs for the long-term advisor have been calculated as follows:

Salary	104,000
Overhead	145,600
Benefits	10,000
Transportation of HHE	23,000
Post Differential	26,000
Education, Housing, TQA	40,000
Travel and Per Diem	12,000
Other Direct Costs	5,000
Fixed Fee	5,000
	370,600

For short-term technical assistance to FENACRE, travel has been calculated at $12,000 and per diem at $16,650. For capital markets technical assistance $269.14/day has been applied with a multiplier of 2.4 for a total of $104,964 in loaded salary costs. Round trip air travel has been calculated at $4,000 with per diem at $15,525.

B. Training.

Three trips per year within Latin America have been projected over the life of the project. Each trip is budgeted at $1,333.

C. Promotional Campaigns.

It is expected that FENACRE will spend $70,000 over the life of the project in salaries, operating costs, advertising, and materials for savings mobilization promotional campaigns.

V. IMPROVEMENT OF POLICY RESEARCH AND ANALYSIS

A. Seminars and Research.

A global contract to cover operation of this component is planned.

1. Home Office support.

A base salary of $2,500 x a 2.4 multiplier for a unit cost of $6,000/month is budgeted. $18,000 per year ($6,000 x 3 p.m.) is envisioned for a three-year LOP of $54,000.

2. U.S. Experts.

A $269.00/day base is budgeted for a total of 8 person months. To the base month of $5,828 has been applied a multiplier of 2.4 or $13,987 per month. Per year costs are $111,896 for a total life of project of $335,688 in salary. Eight round-trip airfare at $12,000 and per diem at $16,560 is budgeted for a life-of-project total of $364,248.

3. U.S. Research Students.

$2,500 per month for each of four students is budgeted for six months per year x 3 years or $609,000. No overhead is calculated.

4. Bolivian Experts/Teachers.

A total of $1,666/month is budgeted with a local overhead rate of 10 percent applied, or $166.00 per month. This totals $21,991 per year or $65,974 for the three-year life of project.

5. Bolivian Research Students.

Nine students per month at $250.00/month is budgeted for a life-of-project total of $13,500.

6. Seminar Costs/Publications.

Local costs of carrying out seminars and publications are budgeted at $10,000/year of which AID will pay $9,333 per year for a total of $28,000.

7. Seminar Follow-Up/Policy Studies

A salary base (unloaded) for 12 persons months is budgeted at $69,940 (269.00/day). Round trip airfare is budgeted at $12,000 and perdiem is $25,185 (365 x $69.00).

B. Commodities.

Three microcomputers plus software at $5,000 each will be provided. Library and research materials are estimated at $12,000.

VI. OTHER COSTS

A. Evaluations and Audits

It is anticipated that three project evaluations will take place over the life of the project, two mid-term evaluations in years two and three and an end-of-project evaluation. It is projected that the two mid-term evaluations will cost $30,000 each and the final impact evaluation $40,000.

Audits will be carried out at the end of the second year of the project and at the same time as the end-of-project evaluation. They are expected to cost $15,000 each.

B. Chief of Party, Institutional Contract

A Chief of Party will be contracted for three years under the institutional contract. Salary is budgeted at $69,976, and a multiplier of 2.4 applied.

Total Costs for the Chief of Party have been calculated as follows:

Salary	209,928
Overhead	293,899
Benefits	12,000
Post Differential	52,482
Education, Housing, TQA	40,000
Travel and Per Diem	20,000
Transportation of HHE	23,000
Logistics (rent, secretary)	44,000
Other Direct Costs	5,000
Fixed Fee	6,000
	706,309

C. U.S. Hire Personal Services Contract

A personal services contract will be negotiated with a U.S. citizen. Estimated costs for the contractor are $324,000, using an average unit cost rate of $9,000/month.

D. Contingencies

Contigencies are calculated at 7 percent.

LIFE OF PROJECT ESTIMATED COSTS AND FINANCIAL PLAN
BOLIVIAN DEPOSIT INSURANCE FUND

	AID GRANT			HOST COUNTRY						
				G.O.B.			PRIVATE SECTOR			
	FX	LC	Total	FX	LC	Total	FX	LC	Total	GRAND TOTAL
I. TECHNICAL ASSISTANCE										
A. Institutional Contract - U.S. FDIC										
1. Long-term: 1 advisor, 24 pm	549,900		549,900							549,900
2. Short-term: 24 pm; 8 advisors, 3 pm each	482,200		482,200							482,200
B. Bank Audits	242,500		242,500	187,500		187,500				430,000
Subtotal, Technical Assistance	1,274,600		1,274,600	187,500		187,500				1,462,100
II. TRAINING										
A. 2 trips/yr for 3 yrs to FDIC in Washington, D.C.	42,000		42,000							42,000
B. 3 trips over the 4-yr project within Latin America	12,000		12,000							12,000
Subtotal, Training	54,000		54,000							54,000
III. PROJECT OPERATING COSTS										
A. Personnel Costs								1,127,300	1,127,300	1,127,300
B. Other Operating Costs								158,500	158,500	158,500
C. Data Processing Costs								40,800	40,800	40,800
Subtotal, Project Operating Costs								1,326,600	1,326,600	1,326,600
IV. COMMODITIES										
A. Furniture and Equipment		10,000	10,000							10,000
B. Computers, 2 microcomputers plus software and TA	30,000		30,000							30,000
Subtotal, Commodities	30,000	10,000	40,000							40,000
V. CAPITALIZATION (Central Bank Loan & member premiums)				500,000		500,000	25,514,000		25,514,000	26,014,000
TOTAL, BOLIVIAN DEPOSIT INSURANCE FUND	1,358,600	10,000	1,368,600	687,500		687,500	25,514,000	1,326,600	26,840,600	28,896,700

DISBURSEMENT SCHEDULE
BOLIVIAN DEPOSIT INSURANCE FUND

	YEAR 1		YEAR 2		YEAR 3		YEAR 4		TOTAL		G
	FX	LC	FX	LC	FX	LC	FX	LC	FX	LC	G
I. TECHNICAL ASSISTANCE											
A. Institutional Contract - U.S. FDIC											
1. Long-term: 1 Advisor, 24 pm	275,000		274,900						549,900		
2. Short-term: 24 pm; 8 advisors, 3 pm ea.	120,600		120,600		120,500		120,500		482,200		
B. Bank Audits	430,000								430,000		
Subtotal, Technical Assistance	825,600		395,500		120,500		120,500		1,462,100		1,
II. TRAINING											
A. 2 Trips/yr for 3 yrs to FDIC in Wash.DC.	14,000		14,000		14,000				42,000		
B. 3 Trips over the 4-yr.proj.within Latin Am.			4,000		4,000		4,000		12,000		
Subtotal, Training	14,000		18,000		18,000		4,000		54,000		
III. PROJECT OPERATING COSTS											
A. Personnel Costs		240,400		255,400		293,700		337,800		1,127,300	1,
B. Other Operating Costos		39,600		39,600		39,600		39,700		158,500	
C. Data Processing Costs		10,200		10,200		10,200		10,200		40,800	
Subtotal, Project Operating Costs		290,200		305,200		343,500		387,700		1,326,600	1,
IV. COMMODITIES											
A. Furniture and Equipment		10,000								10,000	
B. Computers,2 microcomput.plus software & TA	30,000								30,000		
Subtotal, Commodities	30,000	10,000							30,000	10,000	
V. CAPITALIZATION (Member premiums)											
Subtotal, Capitalization	6,436,700		6,233,000		6,521,700		6,822,600		26,014,000		2[illegible]
TOTAL, BOLIVIAN DEPOSIT INSURANCE FUND	7,306,300	300,200	6,646,500	305,200	6,660,200	343,500	6,947,100	387,700	27,560,100	1,336,600	2[illegible]

LIFE OF PROJECT ESTIMATED COSTS AND FINANCIAL PLAN
ICI IMPROVEMENT: FINANCIAL TRAINING CENTER

	AID GRANT			HOST COUNTRY						
				G.O.B.			PRIVATE SECTOR			
	FX	LC	Total	FX	LC	Total	FX	LC	Total	GRAND TOTAL
I. TECHNICAL ASSISTANCE										
A. Long-term: 1 advisor, 24 pm	465,900		465,900							465,900
B. Short-term: 12 pm	211,100		211,100							211,100
Subtotal, Technical Assistance	677,000		677,000							677,000
II. STAFF TRAINING										
A. 3 trips/yr for 3 yrs to U.S. and Latin America	45,000		45,000							45,000
III. COURSE DELIVERY COSTS										
A. Course Costs										
1. Direct Course Costs	363,500		363,500					484,000	484,000	847,500
2. IDEA Overhead		50,300	50,300							50,300
3. Other Course-Related Costs		51,800	51,800							51,800
B. Royalty Purchase	95,000		95,000							95,000
Subtotal, Course Delivery	458,500	102,100	560,600					484,000	484,000	1,044,600
IV. FTC OPERATING COSTS										
A. Personnel Costs		78,900	78,900					40,800	40,800	119,700
B. Other Operating Costs								19,200	19,200	19,200
Subtotal, FTC Operating Costs		78,900	78,900					60,000	60,000	138,900
V. COMMODITIES										
A. Furniture and Equipment	10,000		10,000							10,000
B. Computers and Software	50,000		50,000							50,000
C. Library Material	20,000		20,000							20,000
Subtotal, Commodities	80,000		80,000							80,000
TOTAL FINANCIAL TRAINING CENTER	1,260,500	181,000	1,441,500					544,000	544,000	1,985,500

DISBURSEMENT SCHEDULE
ICI IMPROVEMENT: FINANCIAL TRAINING CENTER

	YEAR 1 FX	YEAR 1 LC	YEAR 2 FX	YEAR 2 LC	YEAR 3 FX	YEAR 3 LC	YEAR 4 FX	YEAR 4 LC	TOTAL FX	TOTAL LC	GRAND TOTAL
I. TECHNICAL ASSISTANCE											
A. Long-term: 1 advisor, 24 pm	233,000		232,900						465,900		465,900
B. Short-term: 12 pm	70,400		70,500		70,200				211,100		211,100
Subtotal, Technical Assistance	303,400		303,400		70,200				677,000		677,000
II. STAFF TRAINING											
A. 3 trips/yr for 3yrs to US and Latin America	15,000		15,000		15,000				45,000		45,000
III. COURSE DELIVERY COSTS											
A. Course Costs											
1. Direct Course Costs	262,500	177,500	80,300	178,000	20,700	128,500			363,500	484,000	847,500
2. IDEA Overhead		25,600		17,000		7,700				50,300	50,300
3. Other Course-Related Costs		26,300		17,800		7,700				51,800	51,800
B. Royalty Purchase	95,000								95,000		95,000
Subtotal, Course Delivery	357,500	229,400	80,300	212,800	20,700	143,900			458,500	586,100	1,044,600
IV. FTC OPERATING											
A. Personnel Costs		38,300		39,900		41,500				119,700	119,700
B. Other Operating Costs		6,400		6,400		6,400				19,200	19,200
Subtotal, FTC Operating Costs		44,700		46,300		47,900				138,900	138,900
V. COMMODITIES											
A. Furniture and Equipment	10,000								10,000		10,000
B. Computers and Software	50,000								50,000		50,000
C. Library Materials	20,000								20,000		20,000
Subtotal, Commodities	80,000								80,000		80,000
TOTAL, FINANCIAL TRAINING CENTER	755,900	274,100	398,700	259,100	105,900	191,800			1,260,500	725,000	1,985,500

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LIFE OF PROJECT ESTIMATED COSTS AND FINANCIAL PLAN
ICI IMPROVEMENT: ASOBAN SERVICES

	AID GRANT FX	AID GRANT LC	Total	HOST COUNTRY G.O.B. FX	G.O.B. LC	G.O.B. Total	PRIVATE SECTOR FX	PRIVATE SECTOR LC	Total	GRAND TOTAL
I. TECHNICAL ASSISTANCE										
A. Institutional Contract										
1. Short-term: 18 pm	316,200		316,200							316,200
Subtotal, Technical Assistance	316,200		316,200							316,200
II. TRAINING										
A. 2 trips/yr for 3 yrs tc U.S. and Latin America	30,000		30,000							30,000
Subtotal, Training	30,000		30,000							30,000
III. PROJECT OPERATING COSTS								307,700	307,700	307,700
IV. COMMODITIES										
A. Computers and Equipment	32,000		32,000							32,000
B. Library Material	15,000		15,000				5,000		5,000	20,000
Subtotal, Commodities	47,000		47,000				5,000		5,000	52,000
TOTAL ASOBAN SERVICES	393,200		393,200				5,000	307,700	312,700	705,900

DISBURSEMENT SCHEDULE
ICI IMPROVEMENT: ASOBAN SERVICES

	YEAR 1 FX	YEAR 1 LC	YEAR 2 FX	YEAR 2 LC	YEAR 3 FX	YEAR 3 LC	YEAR 4 FX	YEAR 4 LC	TOTAL FX	TOTAL LC	GRAND TOTAL
I. TECHNICAL ASSISTANCE											
A. Institutional Contract											
1. Short-term: 18 pm	105,400		105,400		105,400				316,200		316,200
Subtotal, Technical Assistance	105,400		105,400		105,400				316,200		316,200
II. TRAINING											
A. 2 trips/yr.for 3 yrs.to US & Latin America	10,000		10,000		10,000				30,000		30,000
Subtotal, Training	10,000		10,000		10,000				30,000		30,000
III. PROJECT OPERATING COSTS											
Subtotal, Project Operating Costs		98,600		102,500		106,600				307,700	307,700
IV. COMMODITIES											
A. Computers and Equipment	32,000								32.000		32,000
B. Library Material	20,000								20,000		20,000
Subtotal, Commodities	52,000								52,000		52,000
TOTAL, ASOBAN SERVICES	167,400	98,600	115,400	102,500	115,400	106,600			398,200	307,700	705,900

LIFE OF PROJECT ESTIMATED COSTS AND FINANCIAL PLAN
ICI IMPROVEMENT: SAVINGS MOBILIZATION

	AID GRANT			HOST COUNTRY						
				G.O.B.			PRIVATE SECTOR			
	FX	LC	Total	FX	LC	Total	FX	LC	Total	GRAND TOTAL
I. TECHNICAL ASSISTANCE										
A. Long-term FENACRE: 1 advisor, 24 pm	370,600		370,600							370,600
B. Short-term FENACRE: 18 pm	215,800		215,800							215,800
C. Short-term Capital Markets, 7.5 pm	124,500		124,500							124,500
Subtotal, Technical Assistance	710,900		710,900							710,900
II. TRAINING										
A. 3 trips/yr for 3 yrs within Latin America	12,000		12,000							12,000
Subtotal, Training	12,000		12,000							12,000
III. PROMOTIONAL CAMPAIGNS								70,000	70,000	70,000
TOTAL, SAVINGS MOBILIZATION	722,900		722,900					70,000	70,000	792,900

DISBURSEMENT SCHEDULE
ICI IMPROVEMENT: SAVINGS MOBILIZATION

	YEAR 1 FX	YEAR 1 LC	YEAR 2 FX	YEAR 2 LC	YEAR 3 FX	YEAR 3 LC	YEAR 4 FX	YEAR 4 LC	TOTAL FX	TOTAL LC	GRAND TOTAL
I. TECHNICAL ASSISTANCE											
A. Long-term FENACRE: 1 advisor, 24 pm	185,300		185,300						370,600		370,600
B. Short-term FENACRE: 18 pm	71,900		71,900		72,000				215,800		215,800
C. Short-term Capital Markets, 7.5 pm	124,500								124,500		124,500
Subtotal, Technical Assistance	381,700		257,200		72,000				710,900		710,900
II. TRAINING											
A. 3 trips/yr for 3 yrs within Latin America	4,000		4,000		4,000				12,000		12,000
Subtotal, Training	4,000		4,000		4,000				12,000		12,000
III. PROMOTIONAL CAMPAIGNS		24,000		24,000		22,000				70,000	70,000
TOTAL SAVINGS MOBILIZATION	385,700	24,000	261,200	24,000	76,000	22,000			722,900	70,000	792,900

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LIFE OF PROJECT ESTIMATED COSTS AND FINANCIAL PLAN
POLICY RESEARCH AND ANALYSIS

	AID GRANT			HOST COUNTRY						
				G.O.B.			PRIVATE SECTOR			
	FX	LC	Total	FX	LC	Total	FX	LC	Total	GRAND TOTAL
I. SEMINARS AND RESEARCH										
A. Institutional Contract - U.S. Firm										
1. Home Office Backstopping, 3 pm/yr for 3 yrs	54,000		54,000							54,000
2. U.S. Experts for Seminars, 8 pm/yr for 3 yrs	364,200		364,200							364,200
3. U.S. Research Students, 4 students at 6 mos.	60,000		60,000							60,000
4. Bolivian experts/teachers for seminars, 12 pm/yr for 3 yrs.	66,000		66,000					16,500	16,500	82,500
5. Bolivian Student Research, 9 students at 6 mos.	13,500		13,500							13,500
6. Seminar costs and publications	28,000		28,000							28,000
B. Seminar Follow-up/Policy Studies										
1. 12 pm short-term personal services contracts	107,100		107,100							107,100
Subtotal, Seminars and Research	692,800		692,800					16,500	16,500	709,300
II. COMMODITIES										
A. Computers and software	15,000		15,000							15,000
B. Research materials, books, journals, etc.	12,000		12,000							12,000
Subtotal, Commodities	27,000		27,000							27,000
TOTAL, POLICY RESEARCH AND ANALYSIS	719,800		719,800					16,500	16,500	736,300

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DISBURSEMENT SCHEDULE
POLICY RESEARCH AND ANALYSIS

	YEAR 1 FX	YEAR 1 LC	YEAR 2 FX	YEAR 2 LC	YEAR 3 FX	YEAR 3 LC	YEAR 4 FX	YEAR 4 LC	TOTAL FX	TOTAL LC	GRAND TOTAL
I. SEMINARS AND RESEARCH											
A. Institutional Contract - U.S. Firm											
1. Home Office Backstopping, 3pm/yr for 3yrs	18,000		18,000		18,000				54,000		54,000
2. U.S. Experts for Seminars, 8pm/yr for 3yrs	121,400		121,400		121,400				364,200		364,200
3. U.S. Research Students, 4 students at 6mos.	20,000		20,000		20,000				60,000		60,000
4. Bolivian experts/teachers for seminars, 12 pm/yr for 3 yrs	22,000		22,000		22,000				66,000	16,500	82,500
5. Bolivian Student Research, 9 students at 6 mos.	4,500	5,500	4,500	5,500	4,500	5,500			13,500		13,500
6. Seminar costs and publications	10,000		9,000		9,000				28,000		28,000
B. Seminar Follow-up/Policy Studies											
1. 12 pm short-term personal services contracts	35,700		35,700		35,700				107,100		107,100
Subtotal, Seminars and Research	231,600	5,500	230,600	5,500	230,600	5,500			692,800	16,500	709,300
II. COMMODITIES											
1. Computers and software	15,000								15,000		15,000
2. Research materials, books, journals, etc.	12,000								12,000		12,000
Subtotal, Commodities	27,000								27,000		27,000
TOTAL, POLICY RESEARCH AND ANALYSIS	258,600	5,500	230,600	5,500	230,600	5,500			719,800	16,500	736,300

Presidencia de la República
MINISTERIO DE PLANEAMIENTO
Y COORDINACION
BOLIVIA

SUBCOORD Nº 17/87 1191

La Paz, 14 ABR. 1987

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

Estimado Señor Cohen :

Uno de los prerequisitos más importantes para que se produzca el crecimiento económico que pretende impulsar la Nueva Política Económica, es un sistema financiero en buen funcionamiento, que pueda movilizar y distribuir los recursos locales y externos para financiar las actividades productivas de inversión y las actividades empresariales. Las instituciones financieras de Bolivia están en proceso de recuperación después del resiente período de hiperinflación y todavía no están operando con la debida eficiencia. Esto representa un serio impedimento para la recuperación y crecimiento económico de Bolivia.

Reconociendo este hecho, el Supremo Gobierno ha decidido tomar una serie de medidas para mejorar las operaciones del sector financiero. Estas medidas incluyen el restablecimiento de la Superintendencia de Bancos, la creación de un Fondo Boliviano de Seguro de Depósitos, la presentación de una nueva ley de bancos al Congreso, la evaluación del rol futuro de los bancos estatales bolivianos, y una reorganización total del Banco Central. Estas y otras acciones serán llevadas a cabo en forma coordinada bajo la dirección del Banco Central y con la asistencia de USAID, el Banco Mundial, el BID y el FMI.

Para este propósito, el Gobierno de Bolivia solicita, mediante la presente, una donación de US$ 6.200.000. Estos fondos servirán para: (1) establecer el Fondo Boliviano de Seguro de Depósitos; (2) crear un Centro Boliviano de Capacitación Financiera (CCF) bajo el auspicio del Instituto para el Desarrollo de Empresarios y Administradores (IDEA); (3) ampliar los servicios ofreciods por la Asociación de Bancos e Instituciones Financieras de Bolivia (ASOBAN); (4) desarrollar programas de movilización del ahorro interno, y (5) investigar y desarrollar políticas del sector financiero.

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Presidencia de la República

MINISTERIO DE PLANEAMIENTO
Y COORDINACION
BOLIVIA

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El Supremo Gobierno propone contribur con un monto de hasta US$ 3.000.000 para capitalizar el Fondo Boliviano de Seguro de Depósitos, y financiar por lo menos 25% del costo de las auditorías ex - ternas de la banca. Las demás contribuciones de Bolivia al Proyecto totalizarán US$ 14,7 millones . Se entiende que aproximadamente US$ - 1,5 millones de la donación de AID será utilizada para esteblecer el Sistema de Seguro de Depósitos y que USAID/BOLIVIA administrará direc - tamente el resto de la donación del Proyecto con las instituciones del sector privado público que estarán comprendidas en el Proyecto.

Con este motivo, saludo a usted muy atentamente.

GONZALO SANCHEZ DE LOZADA
MINISTRO DE PLANEAMIENTO Y COORDINACION

ANNEX D 10

IDEA INSTITUTO PARA EL DESARROLLO DE EMPRESARIOS Y ADMINISTRADORES

RECEIVED USAID 10 ABR. 1987 LA PAZ

FILE	PD&I	
DIV	ACTION	INFO
DIR		✓
DD		
EXO		
DP		
PD&I		✓
CONT		✓
PRD		
HHR	✓	
Reply due	4/24	
Action tkn		

FILE COPY RETURN TO CENTRAL FILES

La Paz Abril 10, 1987.
No. IDEA-GG-332/87

Señor
David Cohen
DIRECTOR DE LA MISION
USAID EN BOLIVIA
Presente

De nuestra mayor consideración:

De acuerdo a conversaciones sostenidas con personeros de USAID, el Instituto I.D.E.A. incluirá en su organigrama el funcionamiento del Centro de Entrenamiento Financiero. Para cumplir con este objetivo solicitamos la asistencia financiera de USAID que permita el establecimiento de dicho Centro. Esta asistencia, que alcanza a $us. 2.242.737.== (Dos millones doscientos cuarenta y dos mil setecientos treinta y siete 00/100 Dólares americanos), permitirá cubrir la asistencia técnica, los salarios y el equipamiento respectivo, comprometiéndose el Instituto a alcanzar el autofinanciamiento del Centro hasta el tercer año de operación.

Las áreas de capacitación que en principio cubrirá el Centro son las siguientes: crédito, tesorería, tecnología, mercadeo, administración de recursos humanos, servicios administrativos, financiamiento en el comercio exterior, control financiero y seminarios relacionados con la movilización de ahorros. Además contaremos con la colaboración de ASOBAN, entidad que nombrará un Comité de Apoyo Académico al Centro.

Con este motivo y esperando su amable respuesta saludamos a usted,

muy atentamente,

Magda Lahore V.
Lic. Magda Lahore
GERENTE ACADEMICA

ML/ich.
cc: R.L.

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ASOCIACION DE BANCOS E INSTITUCIONES FINANCIERAS DE BOLIVIA

Av. Mariscal Santa Cruz 1392, Piso 15 Edif. Cámara Nacional de Comercio
Teléfonos 321379–361308 Casilla 5822 Cables "ASOBAN"

La Paz, 15 de Abril de 1987
CITE: G-A041/87

Señor
Dr. David Jessee,
JEFE UNIDAD SECTOR FINANCIERO
U.S.A.I.D.
Presente.-

De nuestra consideración:

De acuerdo a las conversaciones preliminares, sostenidas con personeros de U.S.A.I.D.-BOLIVIA, se les hizo conocer la necesidad de que las Instituciones financieras requieren que ASOBAN implemente la prestación de nuevos servicios y la ampliación de los que en este momento se les esta prestando, cuyo objetivo es el fortalecimiento técnico de todos los Bancos afiliados a esta Asociación.

La implementación de estos servicios requiere efectuar gastos que de acuerdo a sus posibilidades ASOBAN esta dispuesto a realizarlos.

Sin embargo del aporte que ASOBAN pueda efectuar es necesario solicitar la cooperación económica de AID de $us. 393.200.- para poder cumplir a cabalidad con los objetivos que ASOBAN se ha fijado en materia de asesoramiento y entrenamiento, tanto a su propio personal como al personal de los Bancos afiliados.

Con este motivo, saludamos a usted con toda atención.

Dr. Fernando Rollano M.
SECRETARIO EJECUTIVO
ASOBAN

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15 ABR. 1987

USAID/ BOLIVIA

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ANNEX E

AID AMB DCM ECON Rec'd 1/20

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FM SECSTATE WASHDC
TO AMEMBASSY LA PAZ 9172
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Action: PRD
Info: D/DD
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Reply due 1/26

AIDAC

Action tkn ______________

E.O. 12356: N/A
TAGS:
SUBJECT: STRENGTHENING FINANCIAL MARKETS PROJECT (511-0598)

1. THE DAEC REVIEWED THE SUBJECT PID ON DECEMBER 11. THE PROJECT IS APPROVED FOR FURTHER DEVELOPMENT SUBJECT TO THE FOLLOWING GUIDANCE. THE PP WILL BE SUBMITTED TO WASHINGTON FOR FINAL APPROVAL AND AUTHORIZATION.

PRELIMINARY REMARKS BY THE MISSION DIRECTOR AND WORLD BANK CONTRACTOR ROBERT VOGEL HELPED TO EXPLAIN THE PRESENT STATE OF THE FINANCIAL SECTOR IN BOLIVIA, ITS IMPORTANCE TO ECONOMIC REACTIVATION, AND THE DIVISION OF LABOR AMONG DONORS WORKING IN THE SECTOR. BOTH COMMENTED THAT THE STRENGTHENING FINANCIAL MARKETS PROJECT IS NOT A TYPICAL A.I.D. PROJECT, THAT THE INTERVENTIONS CONTEMPLATED ARE HIGHLY TECHNICAL AND INTERDEPENDENT WITH THOSE OF OTHER DONORS. THE COMPLEXITY AND LIMITED KNOWLEDGE WITHIN THE AGENCY REGARDING FINANCIAL SECTOR STRENGTHENING PROJECT WERE THE PRIMARY MOTIVATIONS FOR REQUESTING A WASHINGTON REVIEW OF THE PP.

2. DEPOSIT INSURANCE FUND. THE CENTRAL ISSUE OF THE DAEC REVIEW WAS THE NEED FOR, OPERATION OF, AND LEVEL OF CAPITALIZATION OF THE DEPOSIT INSURANCE FUND (DIF). THE PP WILL CLEARLY DESCRIBE THE RATIONALE FOR A DIF AND ITS ROLE IN REGULATING THE BANKING SYSTEM AS WELL AS INCLUDE DETAILED TECHNICAL, ECONOMIC, INSTITUTIONAL, AND FINANCIAL ANALYSES OF THE DIF. THE STRUCTURE AND LEGAL STATUS OF THE DIF WILL BE PRESENTED, AS WELL AS AN ANALYSIS OF THE PRINCIPAL FUNCTIONS AND OPERATING NORMS. OF PARTICULAR CONCERN IS THE NUMBER AND SIZE OF BANKS REQUIRED TO MAKE THE FUND VIABLE, THE CRITERIA FOR ENROLLMENT IN THE DIF, AND THE APPROPRIATE LEVEL AND SOURCE(S) OF CAPITALIZATION OF THE DIF.

3. DONOR COORDINATION. CONSIDERABLE CONCERN WAS EXPRESSED ABOUT DONOR COORDINATION, GIVEN THE NUMBER OF DONORS AND THE VOLUME OF RESOURCES FOCUSSED IN THE FINANCIAL SECTOR. AN EXPLANATION OF MECHANISMS FOR COORDINATION AT THE POLICY AND WORKING LEVELS WILL BE

INCLUDED IN THE PP, AS WELL AS CLARIFICATION OF THE VARIOUS DONOR INTERVENTIONS AND THE RELATIONSHIPS TO ONE ANOTHER. THE PP SHOULD ALSO DESCRIBE THE CHANNELS AVAILABLE TO THE MISSION FOR POLICY DIALOGUE WITH THE GOB, BOTH BILATERALLY AND WITH OTHER DONORS.

4. PHASING OF ACTIVITIES. THE APPROPRIATE PHASING OF ACTIVITIES DURING THE PROJECT WAS DISCUSSED. THE PP SHOULD LAY OUT A CHRONOLOGY OF PROJECT ACTIVITIES, THOSE OF OTHER DONORS IN THE SECTOR, AND THOSE TO BE CARRIED OUT UNDER OTHER USAID/B OR AID/W PROJECTS. THE CHRONOLOGY SHOULD ALSO IDENTIFY ANY PREREQUISITE ACTIONS WHICH NEED TO TAKE PLACE PRIOR TO INITIATION OF THE PROJECT. THE MISSION IS ENCOURAGED TO CONSIDER THE POSSIBILITY OF QUOTE MODULARIZING UNQUOTE GROUPS OF PROJECT ACTIVITIES TO ALLOW FOR AN EVALUATION OF EACH MODULE, AND APPROPRIATE DESIGN MODIFICATION, PRIOR TO INITIATION OF THE NEXT MODULE. THE DAEC EMPHASIZED THAT LAWS OR REGULATIONS NECESSARY TO COMPLETE PLANNED PROJECT ACTIVITIES MUST BE IN PLACE PRIOR TO PROJECT START UP AND APPROPRIATE CONDITIONS PRECEDENT SHOULD BE ESTABLISHED.

5. PAYMENT FOR TECHNICAL ASSISTANCE. IT WAS NOTED THAT THIS GRANT FUNDED PROJECT WILL PROVIDE EXTENSIVE TECHNICAL ASSISTANCE TO PRIVATE SECTOR, FOR-PROFIT BANKING INSTITUTIONS. A MECHANISM WILL BE INCLUDED IN THE PP TO HAVE THESE INSTITUTIONS PAY FOR TECHNICAL ASSISTANCE PROVIDED TO THEM UNDER THE PROJECT. SIMILARLY, AN ANALYSIS WILL BE MADE OF THE APPROPRIATENESS OF PAYMENT FOR THE VARIOUS TRAINING ACTIVITIES UNDER THE PROJECT, RECOGNIZING THAT THE PRINCIPAL BENEFICIARIES OF THE TRAINING WILL BE THE INDIVIDUALS TRAINED.

6. PARTICIPATING INSTITUTIONS. THE MISSION DIRECTOR CLARIFIED TO SOME DEGREE WHICH INSTITUTIONS WITHIN THE FINANCIAL SECTOR WILL PARTICIPATE IN WHICH PROJECT ACTIVITIES. THE PP WILL EXPLAIN THE ROLES OF VARIOUS FINANCIAL INSTITUTIONS IN THE SECTOR INCLUDING THE SAVINGS AND LOAN COOPERATIVES, PRIVATE BANKS AND PUBLIC SECTOR BANKS, AND WHAT THEIR PARTICIPATION WILL BE IN THE PROJECT.

7. PROJECT MANAGEMENT. MANAGEMENT OF THIS COMPLEX AND HIGHLY TECHNICAL PROJECT WILL REQUIRE THE CONTRACTING OF AN EXPERT WITH BROAD FINANCIAL SECTOR EXPERIENCE IN DEVELOPING COUNTRIES PRIOR TO PROJECT IMPLEMENTATION. THE PP WILL GIVE DETAILS OF THE MISSION'S PLAN TO MANAGE THIS PROJECT AND THE ROLE OF THE CONTRACTOR IN DONOR COORDINATION AND POLICY DIALOGUE, AS WELL AS PROJECT MANAGEMENT. SHULTZ
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CLASS: UNCLASSIFIED
CHRGE: AID 1/28/87
APPRV: D:DACOHEN
DRFTD: PD&I:AMDIAZ:MMY
CLEAR: 1.DD:GAW
2.PRD:TDJ
DISTR: USAID AMB DCM
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E.O. 12356: N/A
SUBJECT: STRENGTHENING FINANCIAL MARKETS PROJECT
(511-0598)

REFERENCE: (A) STATE 017162, (B) STATE 189806

1. USAID/BOLIVIA GREATLY APPRECIATES DETAILED GUIDANCE PROVIDED REFTEL FOR PREPARATION OF PROJECT PAPER. THE CONCERNS AND ISSUES RAISED IN THE DAEC WILL BE FULLY ADDRESSED IN FINAL PROJECT DESIGN. HOWEVER, WE WOULD LIKE TO CLARIFY OUR UNDERSTANDING CONCERNING PARAGRAPH 5 OF REFTEL SUGGESTING THAT A MECHANISM BE INCLUDED IN THE PP QUOTE TO HAVE THESE INSTITUTIONS PAY FOR TECHNICAL ASSISTANCE PROVIDED TO THEM UNDER THE PROJECT UNQUOTE. WHILE THIS TOPIC WAS DISCUSSED, THE DAEC DID NOT DECIDE TO REQUIRE BANKS TO PAY FOR TECHNICAL ASSISTANCE PROVIDED UNDER THE PROJECT. TECHNICAL ASSISTANCE (T.A.) TO BANKS WILL BE PROVIDED ON A SECTORIAL-WIDE BASIS TO STRENGTHEN THE WHOLE BOLIVIAN FINANCIAL SYSTEM, WHICH IS CURRENTLY IN A STATE OF VIRTUAL BANKRUPTCY. BY PROVIDING GRANT T.A., MISSION HOPES TO ADDRESS SECTORIAL POLICY CONSTRAINTS RATHER THAN TARGET T.A. TO ONLY THOSE BANKS WILLING AND ABLE TO FINANCE RELATIVELY EXPENSIVE OFF-SHORE CONSULTANTS. IN THE PROCESS, INDIVIDUAL, PRIVATE SECTOR BANKS WILL HAVE TO BE ASSISTED TO ACCOMPLISH THE PROJECT'S SECTORIAL OBJECTIVES. THUS, WE ENVISION THE NEED TO GRANT FUND TECHNICAL ASSISTANCE TO BANKS, AS REQUIRED TO STRENGTHEN BOLIVIA'S FINANCIAL MARKETS. THIS APPROACH IS CONSISTENT WITH PARAGRAPH 8 OF PD-14 ON THE IMPLEMENTATION OF A.I.D. PRIVATIZATION OBJECTIVES (WHICH ALLOWS BOTH LOAN AND GRANT ASSISTANCE TO STRENGTHEN MECHANISMS FOR PRIVATE DELIVERY OF SERVICES) AND WITH THE AGENCY'S FY 1986 DECISION THAT FUTURE USG ASSISTANCE TO BOLIVIA BE PROVIDED ON A GRANT BASIS.

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AID AMB DCM ECON

Rec'd 2/27

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PP RUEHLP
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P 270942Z FEB 87
FM SECSTATE WASHDC
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BT
UNCLAS STATE 057026

File: PD&I

LOC: 066 799
27 FEB 87 0944
CN: 07605
CHRG: AID
DIST: AIDE

Action: PRD
Info: D/DD
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CONT 2
RF 3
SF

AIDAC

E.O. 12356: N/A
TAGS:
SUBJECT: STRENGTHENING FINANCIAL MARKETS PROJECT (511-0598)
REF: (A) STATE 17162, (B) LA PAZ 00859, (C) LEVY/COHEN CONVERSATION 2/13/87

Reply due 3/6

Action tkn ______

ALTHOUGH WE BELIEVE THAT PARA 5 OF REF A IS AN ACCURATE REFLECTION OF THE PROCEEDINGS OF THE DAEC REVIEW OF THE SUBJECT PID, SUBSEQUENT CONVERSATION (REF C) HAS REFINED THE TERMS OF THE ISSUE OF PAYMENT BY BOLIVIAN PRIVATE SECTOR BANKS FOR PROJECT TECHNICAL ASSISTANCE. IT IS NOW UNDERSTOOD THAT PROJECT T.A. WILL BE DIRECTED TO CORRECT PROBLEMS OF THE BANKING SECTOR AS A WHOLE. RECOMMENDED PROCEDURES, POLICIES AND STRATEGIES MAY EITHER APPLY TO THE SECTOR AS A WHOLE OR TO PRIVATE BANKS AS INDIVIDUAL ENTERPRISES, SHOULD THEY ADOPT THEM. THE PRIMARY OBJECTIVE OF THIS T.A. IS TO LOWER THE BANKS' SPREAD POINTS APPLIED TO THE BASIC INTEREST RATE BY LOWERING THEIR OPERATING COSTS.

GIVEN THAT THE PURPOSE OF THE T.A. IS TO LOWER INTEREST RATES, A BENEFIT TO THE ECONOMY AND POTENTIALLY A STIMULUS FOR ECONOMIC REACTIVATION, AND THAT THE T.A.

WILL BE QUOTE GENERIC UNQUOTE FOR THE SECTOR, THE CASE AS PRESENTED DURING REF C FOR PARTIAL COST RECOVERY OR STRAIGHT GRANT FUNDING RATHER THAN FULL COST RECOVERY IS MUCH STRONGER. THEREFORE, DURING DEVELOPMENT OF THE PP FOR WASHINGTON REVIEW, THE MISSION WILL EXAMINE THE FOLLOWING ISSUES RELATIVE TO PAYMENT FOR T.A. TO THE BANKING SECTOR:

1) THE APPROPRIATENESS OF PAYMENT FOR QUOTE GENERIC UNQUOTE OR SECTORAL T.A.;

2) IF PAYMENT IS APPROPRIATE, AT WHAT PERCENT OF COST OF THE T.A. WOULD PAYMENT BE MADE AND THROUGH WHAT MECHANISM, ADVANCED PAYMENT, REIMBURSEMENT, OR COST RECOVERY, AND WHAT USE WOULD BE MADE OF THESE FUNDS;

3) THE OPERATIONAL FEASIBILITY OF A COVENANT IN THE PROJECT AGREEMENT TO THE EFFECT THAT COST SAVINGS TO PRIVATE BANKS RESULTING FROM PROJECT T.A. WILL BE USED

PROVIDED TO BANKS RESULTS IN COSTS SAVINGS WHICH ARE NOT PASSED ON THE BANK CUSTOMERS THROUGH LOWER SPREADS, THEN THE COST OF THE TECHNICAL ASSISTANCE SHOULD BE CHARGED TO THE BANKS. WHITEHEAD

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ANNEX F

STRENGTHENING FINANCIAL MARKETS
(No.511-0598)

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?

   The GOB is expected to take the necessary legal steps to facilitate attainment of the Project purpose. These steps could include the issuance of a Supreme Decree, which is believed can be expeditiously issued, to 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.seg)? (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

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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 strengthen the effectiveness of Bolivia's private sector financial institutions. As such, it will have an impact on (b), (c), and (e).

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).

By strengthening local financial institutions, the Project may attract foreign private sector participation in those institutions, including the use of U.S. experts.

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.

Bolivian contributions, both privater and public, to carry out the Project will be significant.
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.

11. <u>FAA Sec.601(e).</u> Will the project utilize competitive selection procedures for the awarding of contracts, except where applicable procurement rules allow otherwise?	Yes.
12. <u>FY 1986 Continuing Resolution, Sec.522.</u> 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. <u>FAA 118(c) and (d).</u> 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. <u>FAA 121 (d).</u> 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. <u>FY 1986 Continuing Resolution Sec.533.</u> Is disbursement of the assistance conditioned solely on the basis of the policies of any multilateral institution?	No.
16. <u>ISDCA of 1985 Sec. 310.</u> 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.

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?

The Project responds to (c) and (e). Bolivian self-help efforts are significant. The A.I.D. assistance only complements local efforts and resources.
A key target of the Project is to support the development of a cooperative relationship between the Bolivian Association of Banks (ASOBAN) and a successful banking association from another country.

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 GOB and the Bolivian private sector 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.

The Project supports GOB and Bolivian private sector initiatives. As such, it is based on Bolivia's needs and will use to the maximum extent possible local human and financial resources.

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2. <u>Development Assistance Project Criteria (Loans Only)</u>

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

b. <u>FAA Sec.620(d).</u> 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. <u>Economic Support Fund Project Criteria</u>

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

c. <u>ISDCA of 1985 Sec. 207.</u> 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. procurement will be from the Bolivia, and Code 941 countries, if deemed desirable to accomplish the purpose of the Project.
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? If the facilities of other Federal Agencies will be utilized, are they particularly suitable, not competitive with private enterprise, and made available without undue interference with domestic programs?	Yes. Assistance may be required from the U.S. Federal Deposit Insurance Corporation (FDIC). The assistance that may be procured from the FDIC is not expected to be available from other sources.
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.

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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ANNEX G

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 Bolivian private sector (The Association of Banks and Financial Institutions of Bolivia, the Instituto para el Desarrollo de Empresarios y Administradores, FENACRE) have the financial capacity and human resources capability to effectively utilize and maintain the proposed Strengthening Financial Markets Grant Project.

George A. Wachtenheim
Acting Mission Director
USAID/Bolivia

Date: 4/15/87

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