

AGENCY FOR INTERNATIONAL DEVELOPMENT  
UNITED STATES A.I.D. MISSION TO EL SALVADORACTION MEMORANDUM FOR THE DIRECTOR

THRU: DDIR, John Lovaas  
FROM: ANR, Gordon Straub<sup>\*</sup> and PRJ, Michael Deal<sup>pd</sup>  
SUBJECT: Equitable Rural Economic Growth (CRECER) 519-0397

Issue: Your approval is requested for the Concept Paper and Statement of Work for the Request for Proposals for the design of this \$15 million, six year Activity. It will contribute to increased equitable economic growth by helping to reduce rural poverty. The Activity will be a design and perform (DAP) activity, with the design beginning in September 1994 using up to \$266,000 in FY 1994 PD&S funds. Authorization and obligation of this new Activity is expected to occur in March 1995 using FY 1995 funds.

Background: El Salvador has become a transformed nation. The Peace Accords of January 1992 closed the civil war and opened the way to the successful elections of March 1994. The political transition from war to peace has been made. The economic reforms initiated in 1990 have returned the economy as a whole to broad-based growth, permitting the absorption of the demobilized fighters and the economic reactivation of the formerly conflictive zones. Modest reductions in urban poverty have been seen, although the trend has not yet been measured in the rural areas. The peace process and the macroeconomic reforms, despite rough spots in their implementation, are essentially achieving what they were designed to do.

The basic conditions for poverty reduction are in place. The economy has responded quickly and buoyantly to the economic reform program and to the Peace Accords. Despite progress, concern remains about whether the rural poor have obtained a part of the greater benefit. Endemic poverty is the greatest problem for the 4.0 million Salvadorans who live in rural areas. In 1993, 2.6 million of these people are poor, and 1.3 million persons of these are extremely poor.

The causes of poverty are complex. It has been linked to insecure land tenure, to the inability to reduce dependence on debt, to dependence on basic grains cultivation for subsistence, to the limited diversification of production into nontraditional crops, to dependence on a narrow local market. Further, poor people are kept poor due to problems with contracts and other aspects of commercial law, to the tangled and contradictory legal

framework governing cooperatives, and to absence of a proactive GOES policy which promotes smaller businesses. The underlying problems of illiteracy, inadequate primary schooling, and large families, are broader conditions which contribute to the impoverished condition.

#### Results of the Mission Review

The Concept Paper to address the causes of poverty was reviewed by you on January 26, 1994, and again on March 24. Based on these reviews, the concept has been refined in both agricultural and non-farm activities. Ties to GOES activities, to other USAID activities, and to other donor programs have been more clearly drawn. The three former components have been reduced to two: Component One shows the policy agenda and GOES strengthening required. Component Two promotes cooperatives and other rural NGOs as the means by which the rural poor will gain access to the benefits of sectoral and macroeconomic reform. It also includes reforms to the rural credit union system. The review approved the selection of the Design and Perform procurement mechanism.

#### The Activity

The six year, \$15 million, Equitable Rural Economic Growth Activity (CRECER) is attributed to our Strategic Objective, Improve Equitable Economic Growth. The Activity will also contribute to our Strategic Objectives for Environmental and Natural Resource Management and for Enduring Democratic Institutions and Practices.

The goal of the Activity is to increase equitable economic growth. The purpose of the Activity is to reduce rural poverty in El Salvador. The purpose will be accomplished by improving sectoral policies and by participation of rural NGOs in order to lower production and marketing costs, by increasing access to production factors, by opening markets, and by facilitating participation by the rural poor in policy decisions and poverty alleviation programs. At the end of the Activity, rural poverty as measured by the Multiple Purpose Household Survey will not exceed 60% of the rural population, down from 65% in 1993. This implies that about 200,000 persons will escape poverty.

The end-of-activity status leading to the reduction in poverty will include:

- ◆ A policy framework conducive to broadly based rural growth. The framework will be evidenced by a continuation of free market sectoral policies, a revised set of cooperative laws, procedures for nonjudicial resolution of land disputes,

enforcement of commercial sales and land rental contracts, promotion of convenient rural financial intermediation, and promotion of diversified, export-led production.

- ◆ Capacity in the GOES to collect basic data required to support routine policy analysis and formulation. The capacity will be determined by the statistical soundness of data.
- ◆ Growth trends of 5% per year in production agriculture, 6% per year in agroindustry (mainly for export), and an annual target yet to be determined in non-farm service and production industries, as measured by data collected by the Central Reserve Bank. The active participation of the rural NGOs will be shown to have been a significant factor in broadly spreading the economic benefits of this growth.
- ◆ Rural credit unions will be restored to a role as decentralized, financially viable local intermediaries for savings and small loans, as measured by the strength of their balance sheet and the health of their loan book.

The Activity will consist of two components which complement one another to accomplish the Activity purpose. Component One, Policy Reform, will open the policy process to public participation, provide the data necessary for effective policy making, and create the capability to convert that data into decision-making information. Component Two, Participation of Rural Organizations, will prepare rural NGOs which represent the poor to assume a role in the policy-making process and to facilitate the participation of their membership in income-producing activities. It will also promote policy reforms necessary to revive the rural credit unions as a means of providing small loans for agricultural or non-farm enterprises.

#### The Design and Perform Procedure

In response to revised Agency procurement guidelines, the design and perform option of contracting has been selected for the Activity. The Mission will use PD&S funds to finance a competed procurement of the activity design. During the design phase, the contractor and USAID will involve the GOES and rural NGOs in a manner which encourages their participation in and ownership of the final design. The deliverables under the contract will be an Activity Paper, a draft Amplified Activity Description, a scope of work to implement the Activity, an Amplified Activity Description, and evidence of broad collaboration and consensus among NGOs and GOES actors. The contractor will work under the supervision of a Activity Design Committee chaired by the Office of Projects.

Upon delivery of an acceptable design and documents, USAID will open negotiations with the contractor for implementation of the activity without further competition. Implementation could be delayed by conditions precedent to first disbursement, although the participative design structure is expected to minimize such a period. Once the contract has been amended to implement the Activity, the Contractor will field the technical assistance team and begin work under the supervision of the Activity Implementation Committee chaired by the Productive Resources Office.

Design Schedule is proposed as follows:

May 13, 1994	RFP and final Concept Paper approved
May 27	RFP released to Offerors
Jul 29	Proposals received
Sep 16	Design Contract awarded
Oct 17	Design team arrives in El Salvador
Jan 30, 1995	Final activity paper, contract SOW, and activity budget delivered
Feb 15	Authorization and initial obligation
May 1	Implementation team arrives in El Salvador

Recommendation: That you approve the attached Concept Paper and Request for Proposal as the guidance for entering a design and perform procurement of the Equitable Rural Economic Growth (CRECER) Activity. Based on this approval, we will proceed to initiate the design of this new Activity using FY 1994 PD&S funds.

APPROVED: \_\_\_\_\_ *[Signature]*

DISAPPROVED: \_\_\_\_\_

DATE: \_\_\_\_\_ *5-25-94*

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U:\PRJPUB\DOCS\WHERRY\CRECERAM\B: May 9, 1994

Office of the Controller  
 REVIEWED *[Signature]* 5/20/94  
 DMH 19 MAY 1994 *[Signature]* culy s/w  
 DATE

Equitable Rural Economic Growth Activity  
519-0397

USAID El Salvador  
Office of Projects  
Office of Agriculture and Natural Resources  
Private Sector Office

May 13, 1994

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Equitable Rural Economic Growth Activity  
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**I. INTRODUCTION AND SUMMARY**

Poverty in El Salvador is the single greatest moral challenge to the newly elected GOES, both the executive and legislative branches. As it worked to consolidate the political transition from war to peace, the GOES was unable to mount a concerted attack on the causes of poverty with the same vigor that it spent on economic reform. Now that the macroeconomic framework is supportive of growth, microeconomic reforms need to be undertaken as well. The GOES must undertake sectoral programs which ensure that the poor participate in the benefits of that growth.

The Equitable Rural Economic Growth Activity (CRECER) will assist the GOES to reform sectoral policies which have the effect of disenfranchising the rural poor. These policies include land tenure security, cooperative law, diversification of incomes, financial intermediation, GOES institutional roles, and explicit implementation of the economic reforms to the rural areas. The Activity will also assist cooperatives and other rural NGOs to bring the poor into contact with income producing programs and to participate in the formation of programs which affect rural life.

**II. BACKGROUND**

**A. El Salvador after the War**

In the first years of the 1990's, El Salvador has become a transformed nation. The Peace Accords of January 1992 brought the civil war to a close and opened the way to the successful elections of March 1994. The political transition from war to peace has been made. The economic reforms initiated in 1990 have returned the economy as a whole to broad-based growth (although fragile), permitting the absorption of the demobilized fighters and the economic reactivation of the formerly conflictive zones. Modest reductions in urban poverty have been seen, although the trend has not yet been measured in the rural areas. Social services -- basic health and primary education -- are now available virtually everywhere in the entire country. The peace process and the macroeconomic reforms, despite rough spots in their implementation, are essentially achieving what they were designed to do.

The Government of El Salvador (GOES) has now begun to address issues delayed by the war: a reduced role for the state in the economy, enduring judicial reform, decentralization of some government functions to the municipalities, and environmental degradation which is already limiting economic growth. But greater than these is the

need to quickly and effectively deal with the impoverished condition in which 60% of Salvadorans live. Poverty and its accompanying hopelessness were intimately linked to the causes of the civil war. Rural people are worse off than those in the cities by nearly every indicator. A durable peace cannot occur while rampant poverty remains.

The basic conditions for poverty reduction are in place. The economy has responded quickly and buoyantly to the economic reform program and to the Peace Accords. Real gross domestic product grew by 3.4 percent in 1990, 3.3 percent in 1991, 5.1 percent in 1992 and 5.0 percent in 1993. In agriculture, the largest source of rural incomes, the corresponding figures were 7.4 percent, 0 percent (a drought year), and 9.0 percent and 2.9 percent. Agroindustry, from 1990-93, grew by 3.3 percent, 4.9 percent, 5.9 percent and 7.2 percent, while private investment in non-traditional agricultural exports (NTAEs) doubled between 1992 and 1993.

Despite the positive statistics, concern remains about how the rural poor have obtained a part of the greater benefit. It is well documented that poorer and illiterate people are less likely than their better-off, literate neighbors to take advantage of economic gains which depend on new technology, market access, and acceptance of risk. Subsistence corn and bean farmers, being outside the cash economy, are unlikely to realize much benefit from the reforms at all. These farmers did gain income if they sold grain, since the removal of grain price controls caused farmgate prices to rise. Although growth in agricultural activity is encouraging, future gains will be more difficult to come by. To a large extent, the growth induced by structural economic reforms depended on unmet demand for basic grains, mainly rice, in traditional domestic markets which are nearing saturation. Production of nontraditional crops has room to increase. The impressive gains in agriculture also pass by those who are not employed on a farm, and the number of these people is likely to increase as more efficient agricultural methods are introduced. A small, densely populated country like El Salvador must seek sources of off-farm jobs to complement its agricultural employment and diversify its risk to commodity cycles and drought.

## **B. The Rural Sector**

The rural sector, for purposes of this activity, is defined as all of El Salvador outside the San Salvador metropolitan area. Endemic poverty, as measured by per capita cash income, is the greatest problem for the 4.04 million Salvadorans who live in rural areas. GOES surveys in 1992 indicate that 2.6 million of these people are poor, meaning that they cannot purchase two basic monthly food baskets, valued at \$15 each in rural areas, for each member of the household. Within the poor, 1.3 million persons are categorized as

extremely poor. The extremely poor cannot afford to purchase one basic monthly basket of food. Rural monthly per capita income was \$27, barely above the level of extreme poverty, compared to monthly urban (including San Salvador) per capita income of \$61. However, these income levels are known to be under-reported, and the donor community is adjusting them upwards in line with World Bank estimates of the under-reporting. A tabular analysis of the rural poor is shown in Annex 1.

Rural households are uniformly poorer than their urban counterparts; the average rural family is larger (five persons instead of four). Unemployment rates are higher in rural (9.2) than in urban areas (7.2); access to schools, clinics, and potable water is less. Literacy, educational level, and health indicators all show rural residents to be less well off than urban dwellers. Women are heads of household in 17-28% of cases, with the higher figure applying to the eastern area of El Salvador.

Rural workers directly involved in the agricultural economy (633,000 people) comprise about 48% of total employment, with jobs being outside the towns. Of these, 250,000 have full-time jobs in agriculture, while the remainder are seasonal or part-time employed. Seasonal labor is related to harvest, while part time labor is linked to rental of small plots (milpa) for cultivation of corn, beans or sorghum. There is little reliable data on how these people gain income when they are not employed in agriculture. However, a job in the countryside is no guarantee of adequate income. Fully 97% of those employed in agriculture are in unskilled tasks; the median monthly cash wage varies from \$51 in the west to \$28 in the east central area. The average monthly agricultural wage for women is 17% lower than men's, and almost all tasks performed by women are associated with seasonal harvests. In general, women are not permanently employed for wages because of the need to perform child care or carry firewood and water. However, women generally keep chickens or small livestock to supplement the family diet or income.

A 1993 study for USAID on land tenure looked at the fraction of the rural population which did not own agricultural land. The worst-off are some 63,000 long-term unemployed agricultural workers with cash incomes averaging \$6 per month and 184,000 landless day laborers whose incomes average \$21 per month. These persons are the poorest of El Salvador's poor, having unskilled labor as their only economic asset.

The rural population dependent on the non-farm economy (782,700 persons) are supported by some 189,000 persons employed in manufacturing, 203,000 in commerce, and 188,000 in services. The remainder are spread among 5 other genres of employment. These people are employed full-time, generally in the towns, with skilled and semi-skilled labor as a significant fraction of the jobs. Non-

farm jobs are characterized by the need for basic literacy and arithmetic skills. The average monthly income for rural non-farm employment is \$50-80, with the lower figures in the east central region. This income level is just above the poverty line. Women are not usually found in higher-paid positions, although a large number are individual proprietors of small shops.

Increases in the real productivity in rural non-farm enterprises has not yet occurred. The development of larger private industrial parks has pointed up the need for the GOES to improve basic infrastructure such as telecommunications and utilities (electricity, water, sewer). Ease and security of road transport, both internally and for export, as well as efficient port facilities, also constrain the movement of manufacturing enterprises into the countryside. Significant increases in rural employment will not occur until the infrastructural impediments to dispersed industry are resolved.

The supply of non-farm labor in the towns is fed by migration (labor export) from the agricultural caserios, or townships, where work is scarce and poorly paid. Migration also occurs directly to the San Salvador metropolitan area. Evidence from the National Reconstruction Program indicates that semi-skilled service workers, eg, mechanics, do not make a permanent move to a new labor market. Rather, they float among several places, working at the same trade in each place for a while. Merchants and manufacturing workers tend to be more fixed in their location.

The poor, undercapitalized, and illiterate are known to participate less robustly in the economic benefits of macroeconomic reforms as does the literate population and financially better-off middle and upper classes. Based on analysis of its own programs, USAID accepts that macroeconomic policy reform is a necessary first step, but not sufficient alone to achieve broadly based growth. Macroeconomic reforms and market liberalization have been commonly assumed to have leveled the playing field for all parties, but in fact, it remains tilted away from those with the smallest initial resource base. In order to reach the poor, especially the landless, unemployed, and subsistence farmers, additional sector-specific policy reforms are necessary. These reforms should not distort markets or skew benefits artificially toward the poor, but rather, make markets work more effectively and thus provide poor rural people with the same wherewithal as others to respond to market signals and participate in the expanding economy.

Poverty among rural workers has been linked to insecure land tenure both in rentals and ownership, to the inability to save money or reduce dependence on debt, to dependence on basic grains cultivation for subsistence, to the limited diversification of production into nontraditional crops, to dependence on a narrow local market, to

problems with contracts and other aspects of commercial law, to the tangled and contradictory legal framework governing cooperatives, and to absence of a proactive GOES policy which promotes smaller businesses. The underlying problems of illiteracy, poor schooling, and large families born early on are broader conditions which contribute to the impoverished condition. The causes of rural poverty go beyond a scarcity of conventional factors of production; they include as well the incapacity of these citizens to participate effectively in a market economy.

As El Salvador enters the next century, equitable economic growth and subsequent reduction of poverty will require increased non-farm employment and more remunerative agricultural production. This implies the development and vigorous implementation of strong policies aimed at the rural sector. These would include job creation outside metropolitan San Salvador, diversification of smallholder agriculture away from basic grains and into nontraditional crops, promotion of production of exports to markets outside El Salvador, and explicit inclusion of the rural poor in opportunities for upward economic mobility.

### III. POVERTY IN EL SALVADOR

#### A. Constraints to Income Generation

##### 1. Land Tenure is Not Secure

Access to land remains one of the most contentious issues of post-war El Salvador. Some 50% of Salvadoran farmers are renters, but the form of access, either ownership or extended rental, does not appear to be the determinant variable in agricultural success or failure. Most small farmer land is intensively used. Idle land is more often a result of lack of inputs than for conservation or fertility enhancement. An owner of 0.7 ha can earn as much net income as a non-farm worker from the tiny farm, but a renter needs 2.7 ha to gain the same return. Landowners tend to have farms of 2.0 ha, while renters have 1.1 ha. Rental is not a barrier to higher incomes if rented farms could be increased in size. Rental is a stable form of tenancy, but no written rental contracts for small farmers now exist due to the Land Reform Law. Under this law, three years consecutive formal rental can lead to expropriation of the land in favor of the renter.

The ideal condition, fee simple ownership, has not been achieved in either the 1981 land reform or land transfer after the 1992 Peace accords. Under Phase One of the 1981 reform, large farms were turned over to the farm workers and held as a cooperative. These cooperatives function under paternalistic legislation which prevents efficient use of the land, restricts its sale or transfer (including inheritance), and requires government approval before undertaking

any new investment. In 1991, a revision to the land reform (supported by USAID) permitted the cooperative members to decide if the land should be held in common or in individual parcels. However, few of the cooperatives have moved towards clear personal ownership of the land. The Land Bank, established in 1991, is financing the transfer of large properties to groups of beneficiaries. Similar to the previous land reform, the new owners hold title pro indiviso, meaning that individual ownership will be established at some later date. Sale, inheritance, and use of the land as loan collateral are deferred until that division occurs.

## 2. The Cooperative Law Framework Promotes Poverty

USAID is currently assisting poor rural cooperatives to produce and export nontraditional agricultural products. Clients include Agrarian Reform Phase I cooperatives, cooperatives composed of ex-combatants, cooperatives organized by campesino organizations and cooperatives of heretofore unorganized small farmers. They receive production and marketing assistance and in some cases, management training. These cooperatives are constrained by a conflicting body of cooperative law which diminishes efficiency and reduces their creditworthiness.

Salvadoran cooperatives in general are unable to compete in the private sector due to the antiquated and inconsistent laws which govern them. The legal framework relies heavily on governmental paternalism and does not consider the cooperative to be a business. It prevents cooperatives from developing a strong internal management structure within their boards of directors and makes profit illegal. Land reform cooperatives must submit their annual budgets to the Ministry of Agriculture and may not rent or sell the land which was distributed to them in the reform process. The result has been that the land reform cooperatives, which have some of the most productive agricultural land, are pockets of poverty. Like-minded producers or consumers cannot form service cooperatives due to the prohibition of a profit. Cooperatives to sell basic grains or nontraditional crops cannot be used to pool the limited resources of small farmers until the legal framework is modified. USAID's 1994 ESF Program will include conditionality on modernizing cooperative law which directly promotes cooperatives as models for uniting the rural poor. Additional assistance will be required to ensure that the rural poor can take advantage of the reformed legal framework.

## 3. There is Little Diversification of Incomes

Most rural families which depend on agricultural income have developed a variety of means to spread the risk of reduced income from a bad harvest. This may involve planting several crops, a mix of farm and off-farm income, and access to unpriced assets such as

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water and fuelwood. In order to diversify into more profitable agriculture, the family must first have enough market information to assess and then control the inherent risk of the new crop. Accessing information is one of the highest costs paid by rural residents, and availability of information is an area in which the playing field is least level for the rural poor. Reliable data are essential to breaking local monopolies and increasing rural economic opportunities. Where little free information dissemination occurs, the rural poor are the least likely to receive it, especially if it is in written form.

Expansion into nontraditional agriculture requires the farmer to manage a variety of unknowns at once. The new crop requires information on seed, chemical, cultural, and marketing options. Often the best catalyst is to see a neighbor growing the crop. The new crop will require purchase of inputs, and thus involves debt from family, suppliers, or a more formal lender. In many countries, cooperatives ease the transition to new crops, but cannot yet do so in El Salvador. Marketing is further complicated by the absence of product grades which allow pooling of production and more capable producers to be paid for a higher quality product. The inability to enforce domestic and international contracts restricts access to markets, especially for high value NTAEs.

USAID's Coffee Technology Transfer Project (PROCAFE) and the Cooperative League of the USA (CLUSA) are organizing cooperatives of small agricultural producers, helping them to diversify and integrate vertically into processing and marketing. This assistance has typically been through the resolution of interlocking problems, no one of which was insuperable, but taken as a whole, rendered export agriculture a risky venture. El Salvador is a decade behind the rest of Central America in non-traditional agricultural exports and thus must continue to identify innovative products such as marigolds, organic coffee, and radishes. Its growers are only now attaining the critical mass of product needed to be considered serious suppliers and to exercise leverage in El Salvador on the impediments to their business.

Technology and external market contacts are generally available, but cold chambers, transport, the legal system, and banking are still catching up. Water conservation during irrigation must be developed in order to spread new crops to different regions and into additional months. Most of all, the stakeholders in NTAE must see themselves as mutually supportive. Suppliers, producers, transporters, quarantine inspectors, lenders and others must share information so that they can reduce the inherent risks to their segment of the nascent industry. Unfortunately, little of this integration has taken place to date in any of the major NTAE categories.

Economic power typically is concentrated in groups rather than in individuals, therefore increased access to economic opportunity often can be enhanced through effective organizations. Thus, for the rural poor to obtain factors of production and access to markets, as well as to effectively respond to new opportunities in participatory policy making, they must be organized. In El Salvador, grassroots organizations which represent rural poor interests, although plentiful, are generally weak and marginally effective. For all practical purposes, the rural poor are atomistically on their own.

A lack of representation of producers through cooperatives or specialized organizations also constrains diversification in agriculture. Such organizations can present concerns to local and national government in an organized manner, and unite the smaller producers into a viable marketing groups. Two coffee marketing cooperatives have made considerable progress, but the nascent committee for the Atiocoyo Irrigation District, and the cooperatively managed former Food Regulatory Institute (IRA) facilities face management, financial, and membership difficulties.

The families which depend on non-farm businesses face similar needs diversification. In November 1993, the GOES began an economic census in order to improve the quality of data on the non-farm part of the rural economy, as well as in metropolitan San Salvador. In the rural areas, newly entering female proprietors may begin with sales in the local market, basic food preparation, eg, tortilla, or in sewing. Male proprietors often start out in low-level sales positions. Many unskilled workers begin as wage laborers, often with an informal personal business, until they can attain the capital necessary to expand their own. In many cases, several members of the household may work for a wage, while contributing to the informal family business.

The analysis presented here focuses on small business rather than microenterprise, since the employment effects of small business development have been shown to be greater than in microenterprise. The Small Business Program of FUSADES has identified three main constraints to successful small enterprise development. They are restricted access to appropriately structured debt capital, lack of managerial skills, and lack of bargaining power within their business groups and with local and national government. In order to enter the formal economy, a business has to pass through an extensive and convoluted registration procedure and maintain appropriate business records for tax and banking purposes. In some cases, the lender may provide training or assistance to the entrepreneur in managing the financial part of the business. Information needs on costs, markets, etc. are as valid for non-farm businesses as for those in agriculture, and the opportunity cost of gaining that information is as high.

Small businesses need access to reliable electrical service and water; telephone service is also a benefit since it permits the entrepreneur to conveniently access a wider market than the local area. A well functioning financial system assists small businessmen because it permits them to use checks instead of cash and to collateralize or sell accounts receivable. The ease and speed with which machinery or production inputs can be imported is another factor in growth of smaller businesses.

#### 4. Rural Financial Intermediation Is Ineffective

The main method of capitalizing small farmer agriculture, used both by the GOES and by donors, has been through debt, with no corresponding savings activities being supported. Formal lending is provided to farmers through the GOES Agricultural Development Bank (BFA). Its loans are tied by rigid requirements (avio) for chemicals or fertilizers which may be unnecessary or inappropriate; the loan may also require the use of outdated production techniques. Small business lending of the private commercial banks and the moribund GOES agency, FEDECREDITO, has been limited. The GOES agency, FIGAPE, has been more active, but has high non-cash costs associated with obtaining a loan. Up to 14% of the total amount of a loan is absorbed by the cost (cash for transport, documents etc, and non-cash in lost work days) of obtaining it. However, farmers and non-farm borrowers have been shown to accept market rates of interest if the paperwork burden is not too high and the money is available without an extended wait.

Collateral guarantee requirements are high, reflecting the bank's assessment of risk in the rural areas and also the potential cost of foreclosure. However, most rural loans are made against the anticipated harvest or the personal reputation of the borrower. Informal lenders in rural areas finance mainly working capital for small non-farm businesses, and may charge up to 20% per day for short term money.

Poverty is not only a lack of day-to-day cash flow, but is also the inability to accumulate sufficient savings to purchase inventories, leverage a lease, or buy fertilizer. If rural poverty is defined as net worth instead of current income, most poor rural families have difficulty escaping the thrall of debt. Since they have few funds left after consumption needs, savings must be based on small deposits to a conveniently available institution. The formal savings opportunities presently available are inconvenient: banks and other financial intermediaries are located too far from the rural household, and most banks are not oriented towards small accounts. USAID's experience with village banking has been successful, although the implicit subsidy for delivering the loans has been very high in relation to the amount lent. Further, there

has been no appropriate financing mechanism to which these banks can "graduate" when they have outgrown the village bank model.

Rural credit unions are the missing link in the financial sector which separates the micro-lending of the village banks and the small industrial lending of PROPEMI and the commercial banks. The second-tier agency, FEDECREDITO, became politicized during the 1980's, and acquired the generic list of ills seen in other Latin countries: centralized control, heavy bureaucracy, narrow portfolio concentration, decapitalization of the local credit unions, administratively fixed interest rates. The problem is not capital, since FEDECREDITO has access to the Central Reserve Bank. To the extent that FEDECREDITO management is willing, it is possible to appropriately restructure rural lending to reflect the needs of small farmers and businesses. This effort, undertaken through dialogue and consultation with the management and clientele groups of FEDECREDITO, could result in agreement on reforms which would lead to the revitalization of the credit unions as financial intermediaries. As consensus is attained for specific changes in FEDECREDITO's statutes and procedures, it would be plausible to test pilot activities in selected credit unions to demonstrate the value of the reforms. However, nationwide implementation of credit union reforms must rely on the GOES, possibly with the assistance of a multilateral donor.

##### 5. GOES Institutions Have Been Ineffective in Reducing Poverty

The Union of Agrarian Reform Cooperatives Producing and Exporting Coffee (UCRAPROBEX) was formed as a union, not a cooperative, to circumvent paternalistic laws which prevent cooperatives from earning a profit and thereby adequately capitalizing themselves. UCRAPROBEX plays an important role in affecting GOES policy for privatization and serving its membership. Its member cooperatives became an effective lobby for eliminating ISIC, imposing the coffee check-off, and founding PROCAFE. The technology transfer done by PROCAFE is increasing the incomes of the cooperatives under the UCRAPROBEX umbrella.

Although the GOES has taken the appropriate measures to place production of corn, sorghum, rice, and beans on a stable, market-driven footing, it has been unsuccessful with smaller farmers in promoting diversification of income sources away from these minimally profitable crops. The sweeping reorganization of the Center for Agricultural Technology (CENTA), financed by the World Bank in 1992-1993 is expected to help small farmers gain access to higher value crops. However, the renewed CENTA is only now beginning its new programs and time will be required before its staff can gain farmers' confidence and convince them to risk time and money on an NTAE crop.

In the agriculture sector, most of the GOES budget for technical assistance to farmers was placed in salaries and directed at coffee and basic grains. However, in 1993, the World Bank assisted the Ministry of Agriculture to shed two-thirds of its workforce without loss of productivity. The use of a decentralized extension model greatly expands the reach of its technicians. Assistance to coffee farmers has been privatized. MAG is implementing new systems for planning and financial administration. This institutional restructuring is expected to permit the MAG to devote more of its annual budget to program costs, that is, to increasing farm profitability. MAG has explicitly targeted small and medium farmers.

However, MAG is ill equipped to carry out its mandate for improving the lot of small farmers, since it doesn't know much about them. Rural data collection is carried out by MAG's Directorate for Agricultural Economy (DGEA); most rural income and all agricultural studies, statistics, policies and economic decisions (private and public) rely on data derived by DGEA. Due to insufficient budget, inexperienced staff, and an inappropriate sampling framework, national and local data are no longer reliable. The MAG's Policy Analysis Unit (UAP) provides most of the analysis for GOES consideration of policy alternatives for agriculture and rural life. It has direct access to the Economic Cabinet and provides staff assistance on tariff structure, trade negotiations, and NAFTA. However, its staff is too small (6 analysts), poorly trained and not well-experienced.

Policy decisions for the rural sector are made without significant consultation with the beneficiaries of these policies. In agriculture, MAG has begun ad hoc exercises in participatory policy decisions. These include a Rice Council for production, processing and distribution and a Seed Council to examine the reduced use of improved seed use and to advise the Ministry on breaking a monopoly in the industry. MAG has also taken a participatory approach to the World Bank sponsored Task Force on land management issues. Despite this initiative, public input to decision making is not an institutionalized practice. Apart from agriculture, there is no coordinated GOES policy on economic development in the rural areas. No ministry coordinates such policy, and it has been only tangentially touched upon in more general policy discussions.

## **B. Rural Income Generation Efforts to Date**

### **1. The GOES**

As a starting point for combatting rural poverty, the Ministry of Planning drafted, in-house, a rural growth policy framework that will be presented to the government which takes office in June 1994. Central to the framework are improved policy-making, increased

public participation, decentralization, and modernization of state. In agriculture, the MAG is moving towards a regulatory role that defines broad agricultural policies and facilitates other productive rural activities, and has identified its primary beneficiaries as small and medium size farmers. A GOES Task Force on Land Management Issues sponsored a conference in February to seek national consensus on issues of land tenure, rural credit, property taxes, unification and modernization of the property registry and reforming the cadastre. USAID's recent studies of land tenure, rural credit and debt overhang were basic documents for the Task Force. Non-farm growth has not yet been actively promoted.

## 2. USAID

The CRECER Activity builds on policy reforms that the Mission has promoted under previous ESF-funded Policy Reform Programs by improving the policy reform process and direct assistance to public and private actors in the policy process. USAID has assisted major policy reforms associated with economic stabilization and structural reform such as the land market, the Land Bank, privatization of IRA (basic grains marketing) and ISIC (coffee technology), the development of private grain storage and marketing systems, and accession to GATT. To reach the poor, USAID has promoted the production of nontraditional crops, especially through cooperatives, as well as small farmer production of coffee. As a part of the National Reconstruction Program, agricultural starter packages, investment credit, and production credit were provided to demobilized fighters. Distribution of farm land to them and to squatters continues. In small business, USAID has provided investment and operating credit to both small and microenterprise. USAID has worked with nearly 200 indigenous NGOs in a variety of rural programs. In attacking the broader contributors to rural poverty, USAID has invested heavily in primary education, vocational training, primary health care, rural electrification, and potable water and sanitation. USAID activities have assisted rural dwellers to acquire their citizenship documents and personal identification so that they can now travel freely and conduct business without intermediaries.

## 3. Other Donors

The World Bank financed the reorganization of the Ministry of Agriculture (FRISA) and has shown interest in handling land tenure security issues. It hosted the initial roundtables on this topic, including not only land transfer, but also the cadastre and registration system. The World Bank and the InterAmerican Development Bank are also pressing for a more active rural financial strategy and have an interest in rural credit unions. The Central Reserve Bank (BCR), with technical assistance from both donors, is preparing a rural credit strategy as part of the dialogue. Among

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others, the strategy is expected to recommend restructuring the Agricultural Development Bank (BFA) with more local control, and it may go so far as to recommend privatizing the BFA or replacing it. The IDB supports rural social infrastructure development through the Social Investment Fund (FIS). It has also improved the financial environment for long and medium term investment through its Multi-Sector Investment Loan and is continuing to support agriculture through large scale irrigation activities. The multilateral banks are supporting the GOES effort in modernization of the state and civil service reform.

The UNDP has carried out small integrated rural development activities. The European Economic Community (EEC) and Food and Agricultural Development Institute (FIDA) are implementing rural poverty alleviation activities based on local participation and group action. The Italian Government's ADEL Activity in Chalatenango seeks to promote local social and economic development through community organizations and group action.

#### IV. THE ACTIVITY

##### A. Strategic Fit

The six year Rural Equitable Economic Growth Activity (CRECER) is attributed to USAID's Strategic Objective, Improve Equitable Economic Growth. Through direct collaboration with the policy analysis, dialogue and reform activities, the Activity will contribute to a second Strategic Objective, Environmental and Natural Resource Management. By encouraging active participation of the rural poor in development organizations, CRECER will contribute to a third Strategic Objective, Enduring Democratic Institutions and Practices. The Activity will be financed by \$5.0 million in GOES contributions, \$1.2 million in NGO contributions, and \$15.0 million from USAID, for a total of \$21.2 million.

Three program outcomes associated with improved equitable economic growth are supported by the activity:

- Maintenance of an adequate policy environment through sound sectoral policies
- Increased nontraditional agricultural and perhaps other nontraditional exports and an increased rate of growth in the agricultural sector, and
- Increased employment through equitable production opportunities, increased wage labor, individual productivity, and reduced underemployment.

The Activity is intended to complement multilateral donor efforts in the rural sector by creating an environment conducive to efficient use of the multilateral resources. This will be accomplished by

modernizing the appropriate GOES agencies in anticipation of their new role, by identifying and mobilizing NGOs as representatives of the rural sector and development partners to the GOES, and by fostering consensus between government policy makers and the various segments of the rural population.

#### B. Goal and Purpose

The goal of the Rural Equitable Economic Growth Activity is to increase equitable economic growth. The purpose of the Activity is to reduce rural poverty in El Salvador. The purpose will be accomplished by improving sectoral policies and by participation of rural NGOs in order to lower production and marketing costs, to increase access to production factors, to open markets, and to facilitate participation by the rural poor in policy decisions and poverty alleviation programs. At the end of the Activity, rural poverty as measured by the Multiple Purpose Household Survey will not exceed 60% of the rural population, down from 65% in 1993. This implies that 200,000 persons will lift themselves above the poverty threshold.

USAID seeks to improve the sectoral policy environment and the institutional capacity, especially of NGOs, to take advantage of the substantial rural poverty alleviation activities which are anticipated to be financed by multilateral donors such as the World Bank and the Interamerican Development Bank. USAID also desires to improve the efficiency of selected GOES programs which are not enjoying the maximum desired effect in rural areas.

The end-of-activity status leading to the reduction in poverty will include:

- ◆ A policy framework conducive to broadly based rural growth. The framework will be evidenced by a continuation of free market sectoral policies, a revised set of cooperative laws, procedures for nonjudicial resolution of land disputes, enforcement of commercial sales and land rental contracts, promotion of convenient rural financial intermediation, and promotion of diversified, export-led production.
- ◆ Capacity in the GOES to collect basic production and marketing data, based on demand from the productive sectors, required to support routine policy analysis and formulation. The capacity will be determined by the statistical soundness of data.
- ◆ Growth trends of 5% per year in production agriculture, 6% per year in agroindustry (mainly for export), and similar annual growth in non-farm service and production industries, as measured by data collected by the Central Reserve Bank. The active participation of the rural NGOs will be shown to have

been a significant factor in broadly spreading the economic benefits of this growth.

- ◆ Rural credit unions will be restored to a role as decentralized, financially viable local intermediaries for savings and small loans, as measured by strength of their balance sheet and the health of their loan book.

The Activity will consist of two components which complement one another to accomplish the Activity purpose. Component One, Policy Reform, will open the policy process to public participation, provide the data necessary for effective policy making, and create the capability to convert that data into decision-making information. Component Two, Participation of Rural Organizations, will prepare rural NGOs which represent the poor to assume a role in the policy-making process and to facilitate the participation of their membership in poverty reduction programs.

The Activity beneficiaries are the 2.5 million rural poor, especially 200,000 persons who rise above the poverty threshold. The designation of counterpart institutions will be undertaken as part of the design exercise.

### C. Component One - Policy Reform

The component will address distortions in public policies which tilt the economic playing field away from the poor and rural population. It will implement a participatory policy reform process around a policy agenda, improve the collection and dissemination of sound economic and social data, and improve policy analysis expertise. The sequence of events which will lead to accomplishment of the component's outputs will be drawn up by the design contractor.

To increase the participation of the rural poor in the benefits of the growing economy, the Activity will assist the GOES to achieve consensus on a policy agenda and then to aggressively implement it. The details of the policy agenda will be part of the activity design; the agenda is expected to include the following areas:

- A change in the agrarian reform law to permit stable land rental without risk of expropriation.
- Promotion within the reform cooperatives to select fee simple or other form of individual ownership of the cooperative's assets.
- A study of the requirements and procedures for the eventual division of land held pro indiviso.
- A change in the various cooperative laws to permit and to promote service and sales cooperatives, both agricultural and nonfarm.

- Seek improved timeliness and resolution in the legal procedures for breach of contract
- Promotion of appropriate structuring of rural lending to reflect the needs of small farmers and small businesses.

To achieve lasting reform, it will be necessary to increase the capacity of the GOES to perform sound analysis, and conduct participatory policy formulation. The degree of that capacity will be determined by the methodology used for policy analysis and the number and variety of private organizations regularly consulted in policy formulation.

It will be important that activities supported by donors in the Ministries of Agriculture, Economy, and others will conform to the expected budgetary and personnel capabilities of these entities. In general, this will require least cost solutions to data collection, with straightforward sampling methodologies and uncomplicated data entry and manipulation requirements. Any work recommended to be contracted out should fall within the GOES' ability to procure and administer the contract. Analytic requirements should also be commensurate with the experience and training of the GOES civil servants likely to be tasked with the analysis.

The analysis of the data and recommendation of policy alternatives will be undertaken by the Agricultural Policy Unit (UAP) of the MAG and as-yet undesignated offices in other GOES agencies and NGOs. Institutional strengthening will be required for these agencies to provide day-to-day problem identification and policy analysis. This is expected to entail in-country training for day-to-day data analysis and response to common policy questions which arise in the normal conduct of public affairs. In support of the outward-facing nature of the Salvadoran economy, training may also be provided to support international trade negotiations and to translate trade liberalization into functioning policies which open economic opportunities for the rural sector. A capacity will also be developed for specialized analysis such as land tenure, rural credit, and marketing of NTAEs and nonfarm products.

The component will install and perpetuate participative policy development within the GOES. The Activity will finance technical assistance to institutionalize the GOES' use of an effective, open policy formulation process, and will require development and implementation of a participatory procedure for identifying priority constraints in the rural sector and for examining options for their solution. Public hearings or other means may be used to build consensus around the proposed policy solutions.

In order to develop policy alternatives and subsequently analyze them, adequate data collection will be necessary. This collection will be done in part by the Directorate for Agricultural Statistics

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(DGEA) in MAG. The Directorate of Statistics and Census (DGEC) will be used to complete the image of rural El Salvador, especially for the nonfarm segments of the economy. Institutional strengthening will be required for the DGEA and any other selected agency to provide accurate and timely data as a basis for policy analysis and public/private information dissemination. The activity is expected to finance the design and installation of a new sample frame and appropriate sampling technology, both for agricultural and nonfarm activities. A subset of this will be the methodology for a new nontraditional agriculture survey. These surveys must incorporate forward and backward linkages to agricultural production and foreign trade flows. It is also anticipated that the Activity will finance development of an improved means of communicating data and analysis to public and private organizations.

USAID desires to return the DGEA to its pre-war capability, when it conducted semiannual multipurpose national surveys, together with smaller specialized surveys such as NTAE production and processing. The sample frame and methodology had been adapted from the U.S. Department of Agriculture. Preliminary data must be available in a timely fashion, with final publication not long thereafter. Statistical accuracy must meet international criteria and control of both sample and data quality must be installed.

The DGEC is conducting a nationwide economic census in 1994, for non-farm activities, including food processing, transport, and commercial activities. It will be followed (probably in 1995) by an agricultural census of farms (production units). A population census was taken in 1992. DGEC has no installed sampling methodology to gather economic data for sectors or limited geographic areas. It does not publish preliminary data.

A team of technical experts for up to three years is anticipated in order to accomplish the data, analysis, and consultation activities.

#### **D. Component Two - Participation of Rural Organizations**

This component will strengthen the capacity of government and private sector leaders, and the organizations they represent, to analyze issues, and engage a broad spectrum of Salvadoran society in debate and consensus-building around key policy reforms which merit the confidence of the citizenry. The activity will involve both public and private institutions and coordinate closely with multilateral and other donors. By supporting studies, seminars, and public debate, a broader consensus will be built on the extent and pace of reforms which affect the rural sector.

The Activity will finance technical assistance to improve the capabilities of Salvadoran organizations to develop credible

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programs for helping their constituents. The final result of any of these programs will be increased income for the constituent group. The activity will also assist rural groups to seek coalitions with other economic or social groups where they have shared economic or social interests, thus increasing the political viability of the agenda of the poor. CRECER will take advantage of the lessons learned in Latin American or other clearly transferable cases. The experience of USAID in Honduras and Guatemala may be especially relevant.

Technical assistance will assist the selected NGOs to help rural households capture diverse income opportunities, both in nontraditional agriculture and in non-farm activities. For example, a small entrepreneur might furnish parts to a larger, urban manufacturer in addition to making a product for local sale. Similarly, a small farmer might be convinced to adopt erosion control measures which include the use of a high-value crop such as pineapple. The variety of options available will depend on the economic endowment of each local area.

The selected NGOs might also help farmers gain security in their land, access credit, markets, and technology, and develop value-added steps to their production. For instance, a roundtable of producers, transporters, suppliers, brokers, regulators, educators, etc., could discuss impediments to economic activity. Such a meeting might be sponsored by vegetable brokers seeking product to sell or by suppliers seeking to generate additional demand for seeds or equipment. To the extent that worthwhile income increases would result, the NGOs and the GOES will collaborate to create quality grades and standards to differentiate higher value products and thus establish a basis for differences in price.

The NGOs will use Activity-financed assistance to help farmers and small entrepreneurs avoid marketing pitfalls such as poor sales contracts or inappropriate product selection. For example, assistance might help reduce the cost (in time or money) of gathering production or market price information, assist members to deal with courts and arbitrators, or seek adjustment in banking procedures. In complement to the policy analysis assistance provided to the GOES, technical assistance will help the NGOs to assist constituents to participate in policy deliberations with municipal and national governments.

The NGOs to be selected under the activity would be drawn from cooperatives, rural based NGO's, commodity groups, resource user groups, or small processor associations. The activity design will seek local NGOs which meet the following criteria:

- Policy analysis. The NGOs will have these skills or be willing to acquire them, including use of data and research. Public relations and lobbying experience is not sufficient.
- Advocacy Skill. The NGO will have demonstrated ability to apply data and analysis in a constructive dialogue which promotes sectoral reform.
- Commitment to the Public Interest. The NGOs will be apolitical in nature and representative of an array of rural interests rather than a specific point of view.
- Power of Convocation. The NGO must have or be able to develop sufficient standing to call high-level meetings and have them attended by key decision-makers in the policy reform process.
- Economic Impact. The NGO must have demonstrated its potential for increasing the incomes of its members/clientele though, inter alia, improved or diversified production, better marketing techniques, and sound financial and management practices.

The selection of these NGOs will be made during the final design of the activity; some may be selected after activity implementation begins. USAID will exercise an administrative approval over the selection process.

#### Rural Finance

Poverty is not only a lack of day-to-day cash flow, but is also the inability to accumulate sufficient savings to purchase inventories, leverage a lease, or buy fertilizer. The Activity will promote appropriate structuring of rural lending to reflect the needs of small farmers and small businesses. This effort will be undertaken through a dialogue and consultation with the management and clientele groups of FEDECREDITO, the second-tier organization which by law regulates the credit unions and gives them access to Central Bank credit lines. These consultations are anticipated to result in agreement on reforms which would lead to the revitalization of the credit unions as financial intermediaries.

The reform dialogue with the credit unions is new; considerable discretion may be required in approaching the nature and sequence of the reforms. CRECER will therefore incorporate flexibility which will permit rapid movement through the reform agenda should the reforms prove to be quickly accepted. However, credit union reform is considered to be an independent item so that the rest of the Activity will not be harmed if the reforms are adopted slowly. The Central Reserve Bank has sufficient resources for rediscount to

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credit unions; CRECER will confine itself to savings mobilization and intermediation within a financially sound set of institution.

As consensus is attained for specific changes in FEDECREDITO's statutes and procedures, the Activity will finance pilot activities in selected credit unions to demonstrate the value of the reforms. However, nationwide implementation of the reforms must rely on the GOES, possibly with the assistance of a multilateral donor.

A team of technical experts will be required for the activity life to provide advice on cooperative and NGO development. The team will conduct in-country training of NGOs' staff and will assist them in designing and implementing their programs for poverty alleviation and access to the policy process.

#### E. Illustrative Budget

Component One is budgeted at \$6.0 million in USAID funding plus \$5.0 million of GOES counterpart. The counterpart is based on estimated expenditures by MAG to support DGEA and UAP once they are staffed at their optimal levels and employees are compensated at the pay scales expected under the PRISA reforms. Component Two is budgeted at \$9.0 million in USAID funding plus NGO counterpart of \$1.2 million.

#### V. THE DESIGN AND PERFORM PROCEDURE

In response to revised Agency procurement guidelines, the design and perform option of contracting has been selected for the Activity. In this option, the Mission will use PD&S funds to finance a competed procurement of the activity design. During the design phase, the contractor and USAID would involve the GOES and rural NGOs in a manner which would ensure their approval of the final design. The policy agenda shown in Component One represents the starting point for negotiations. The deliverables under the contract will be a activity paper, a scope of work to implement the design, and a budget for the activity. The contractor will work under the supervision of a Activity Design Committee chaired by the Office of Projects.

Upon delivery of an acceptable design and documents, USAID can open negotiations with the contractor for implementation of the activity without further competition. Implementation could be delayed by conditions precedent to first disbursement, although the design structure would aim to minimize such a period. Once the contract has been amended to implement the Activity, the Contractor will field the technical assistance team and begin work under the supervision of the Activity Implementation Committee chaired by the Productive Resources Office.

Equitable Rural Economic Growth Activity  
519-0397

Annex 1

**Statistical Analysis of Poverty Measures**

Rural is defined for the CRECER activity as all of El Salvador outside the metropolitan capital. It includes the relatively large towns of Santa Ana and San Miguel, since they are based on the rural economy, as well as market towns such as Cojutepeque and Usulután. The data are drawn from the 1993 Multiple Purpose Household Survey (MPHS), as is the definition of the geographical areas.

- West is Santa Ana, Sonsonate, Ahuachapán.
- Central I is La Libertad, San Salvador, Chalatenango, Cuscatlán (less bits of the metropolitan San Salvador area)
- Central II is San Vicente, La Paz, Cabañas
- East is Usulután, San Miguel, Morazán, La Unión

Population figures are given in thousands; percentages are the fraction of the total amount in the geographical area.

	Total Rural	West	Central I	Central II	East
Total Population	4,038.6	1,247.8	1,062.0	700.9	1,027.7
Total Employed	1,320.7	443.3	350.1	220.6	306.8
Unemployment	10.2% 134.4	8.6% 42.0	9.7% 37.5	7.7% 18.5	10.6 36.4
Total Households	813.5	260.4	212.1	131.8	209.3
Households in Poverty	65.3% 513.5	62.3% 162.2	65.0% 138.0	68.7% 90.5	67.3% 140.8
Households in Extreme Poverty	31.7% 257.6	28.6% 74.7	31.4% 66.7	38.6% 39.8	36.5% 76.4
Women Heads of Household	23.0% 186.9	28.5% 57.7	23.9% 50.6	25.9% 34.2	21.2% 44.4

2. Agricultural Families

	Total Rural	West	Central I	Central II	East
Employed in Agriculture	632.8	234.5	144.6	118.9	134.8
Full-time Agricultural Employment	250.3	103.6	49.8	43.6	53.3
Agricultural Income per month (median)	¢250-450	¢450	¢350	¢250	¢350

3. Off-farm families

	Total Rural	West	Central I	Central II	East
Total Employed other than Agriculture	782.7	208.8	300.3	101.6	172.0
Manufacturing	188.9	56.3	62.9	26.1	43.6
Commerce	203.5	64.2	56.1	31.6	51.7
Services	188.5	57.3	54.1	27.8	49.3
Other Off-farm Employment	107.9	32.0	32.4	16.1	27.5
Income per month (median)	¢400-700	¢400-700	¢400-700	¢450	¢400-700

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Logical Framework  
Equitable Rural Economic Growth Activity  
519-0397

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	MAJOR ASSUMPTIONS
<p style="text-align: center;">GOAL</p> <p>To increase equitable economic growth</p>	<p>Rural poverty in 1998 will not exceed 60% of the rural population, down from 65% in 1993.</p>	<p>GOES Multiple Purpose Household Survey</p>	<p>Macroeconomic framework remains open, export-oriented, market-led.</p> <p>Consensus in GOES and political parties to expand democratic processes.</p>

PURPOSE	END OF PROJECT STATUS (EOPS)		
<p>To reduce rural poverty in El Salvador.</p>	<p>1. A policy framework conducive to broadly based rural growth.</p> <p>2. Capacity in the GOES collect basic data required to support routine policy analysis and formulation.</p> <p>3. Growth trends of 5% per year in production agriculture, 6% per year in agroindustry (mainly for export), and _% per year in non-farm service and production industries.</p> <p>4. Rural credit unions will be restored to a role as decentralized, financially viable local intermediaries for savings and small loans.</p>	<p>1a. Continuation of free market sectoral policies</p> <p>b. Revised set of cooperative laws</p> <p>c. Procedures for nonjudicial resolution of land disputes, d. Enforcement of commercial sales and land rental contracts</p> <p>e. Promotion of convenient rural financial intermediation</p> <p>f. Diversified, export-led economic activity.</p> <p>2a. Statistical soundness of data.</p> <p>b. Utility of data to productive sectors</p> <p>3a. Data collected by the Central Reserve Bank.</p> <p>b. Participation of rural NGOs in broadly spreading the economic benefits of this growth.</p> <p>4a. Net worth and income statement</p> <p>b. Soundness and diversification of loan book.</p>	<p>To be developed by the design contractor</p>

OUTPUTS

Component One

- 1. A change in the agrarian reform law to permit stable land rental without risk of expropriation.
- 2. Land reform cooperatives select fee simple or other individual ownership of assets.
- 3. Study the requirements and procedures for the eventual division of land held pro indiviso.
- 4. Change in cooperative laws to promote service and/or sales cooperatives.
- 5. Timely resolution legal redress for breach of contract
- 6. Increased capacity of GOES to perform sound analysis and conduct participatory policy formulation.

To be developed by the design contractor

To be developed by the design contractor

To be developed by the design contractor

Component Two

- 1. Capacity of GOES and private sector to analyze issues and engage a broad spectrum of Salvadoran society for consensus on policy reforms
- 2. Rural households capture diverse income opportunities, in NTAE and non-farm activities.
- 3. Farmers and small entrepreneurs avoid marketing pitfalls such as poor contracts or product selection.
- 4. Consensus is attained for specific changes in FEDECREDITO's statutes and procedures, poor sales contracts or inappropriate product selection.
- 5. Appropriate restructuring of rural lending to reflect the needs of small farmers and small businesses.

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INPUTS			
USAID \$15.0 million GOES \$5.0 million NGOs \$1.2 million.			

Equitable Rural Economic Growth  
519-0397

Initial Environmental Examination

Basic Activity Data

Activity Location: El Salvador  
Activity Title: Equitable Rural Economic Growth  
Activity Number: 519-0397  
Activity Funding: \$15 Million (LOP)  
Life of Activity: 6 years  
IEE prepared by: Peter Gore  
USAID/El Salvador  
Environmental Officer  
Recommended Threshold Decision: Positive  
Mission Threshold Decision: Concur with Recommendation  
Date Prepared: April 22, 1994



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Charles E. Costello  
Mission Director  
USAID/El Salvador

25 MAY 1994

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Date

Equitable Rural Economic Growth  
519-0397

USAID/El Salvador intends to sign a Handbook 3 Bilateral Agreement with the Ministry of Planning for assistance to a variety of GOES entities and NGOs involved with alleviation of rural poverty. The Equitable Rural Economic Growth Activity (No. 519-0397) has a planned life of six years with planned obligations not to exceed \$15.0 million.

The Equitable Rural Economic Growth Activity will play a lead role in helping USAID/El Salvador meet its strategic objective of "increased equitable economic growth". It will contribute to all three of the program outputs of 1) Maintenance of an adequate policy environment through sound sectoral policies; 2) Increased nontraditional agricultural and perhaps other nontraditional exports and an increased rate of growth in the agricultural sector, and 3) Increased employment through equitable production opportunities, increased wage labor, individual productivity, and reduced underemployment.

The Activity is intended to complement multilateral donor efforts in the rural sector by creating an environment conducive to efficient use of the multilateral resources. This will be accomplished by modernizing the appropriate GOES agencies in anticipation of their new role, by identifying and mobilizing NGOs as representatives of the rural sector and development partners to the GOES, and by fostering consensus between government policy makers and the various segments of the rural population.

The goal of the Equitable Rural Economic Growth Activity is the Mission Strategic Objective to increase equitable economic growth. Its purpose is to reduce rural poverty in El Salvador. The purpose will be accomplished by improving GOES sectoral policies which constrain the development of a vibrant rural economy in which the poor have opportunity to participate. Achievement of the purpose will also include participation of rural NGOs as intermediaries which help to lower production and marketing costs, to increase access to production factors, to open markets, and to facilitate participation by the rural poor in policy decisions and poverty alleviation programs. A particular emphasis will be placed on the improvement of the rural credit union system as a means of small loans.

USAID seeks to improve the sectoral policy environment and the institutional capacity, especially of NGOs, to take advantage of the large activities which are anticipated to be financed by multilateral donors such as the World Bank and the Interamerican Development Bank. USAID also desires to improve the efficiency of selected GOES programs, such as the Central Reserve Bank's credit lines, which are not now enjoying the maximum desired effect in rural areas.

The Activity will consist of two components which complement one another to accomplish the Activity purpose. Component One, Policy Reform, will open the policy process to public participation, provide the data necessary for effective policy making, and create the capability to convert that data into decision-making information. Component Two, Participation of Rural Organizations, will prepare rural NGOs which represent the poor to assume a role in the policy-making process and to facilitate the participation of their membership in poverty reduction programs.

The Activity specifically seeks to invigorate agricultural production and processing as well as a variety of small non-farm businesses in the rural areas. Small farms especially have been a major source of soil erosion and subsequent downstream siltation. Modern production techniques, whether for large or small farms, require the use of chemical inputs whose uncontrolled use represents a possible pollution hazard. Processing of agricultural produce uses large amounts of water and can generate significant volumes of biodegradable waste. USAID has taken aggressive steps in its agricultural production activities to mitigate these problems. Inasmuch as the Activity will directly augment the production and processing of agricultural crops, an environmental assessment of the design is warranted.

Small businesses, taken as point sources of pollution, can generate both biodegradable and nondegradable solid wastes. Many are dependent upon water for their activities. Each one contributes a small amount to the problem of solid waste disposal and to the load on the inadequate sewage systems of the rural towns. Indeed, the Mission authorized the Environmental Protection Project (PROMESA) as a multisectoral activity to seek application of environmental management techniques beyond agricultural enterprises. Assessment of the environmental impact of the non-farm interventions of the Activity is also warranted.

### Recommendations

Pursuant to Section 216.2(a) of AID environmental procedures, an environmental analysis/evaluation is required for new projects. Analysis of the Concept Paper for Equitable Rural Economic Growth indicated that it should receive an Initial Environmental Examination because the Activity contained elements that had potential environmental impacts. Some negative environmental effects may be caused by the promotion of increased production by small farms and non-farm businesses.

Based on the information above, we recommend a positive determination for the Threshold Decision for the Project and that an Environmental Assessment be performed for the Equitable Rural Economic Growth Activity.