REHABILITATION OF PRODUCTIVE ENTERPRISES

A CREDIT SYSTEM DEVELOPMENT PROJECT IN UGANDA

PROJECT PAPER

Project No.: 617-0104

USAID/UGANDA

AUTHORIZED IN SEPTEMBER 1984

Note: Although the Project was authorized in September 1984, this final version of the Project Paper was not printed until May 1985. See Preface and Introductory Material for detailed explanation with respect to modifications from the original USAID submission of June 1984.

AFR/PD/EAP
May 9, 1985

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Note: The Project Paper proper, commencing 30 some pages into this document, has its own detailed table of Contents.

PREFACE

Although the basic design and thrust of this project remains unchanged, the project paper proper does not reflect certain recommendations and decisions regarding the pre-implementation period, phasing, budget, and measures adopted to enhance the flow of benefits to the needy made during the official review and approval process in AID/W (June - September 1984). These modifications are detailed in two Tabs to the Action Memorandum requesting authorization incorporated in the following pages.

With respect to benefits to the needy, the primary purpose of the project was changed from its previous focus on lending system improvements to the following:

> <u>Improved income for the rural poor and increased agricultural production through increased investment in agricultural enterprise (primary production, processing, marketing, and other agriculturally related operations)</u>.

Conditions expected at the end of the project and lower level indicators, however, still include the original system and enterprise development objectives in addition to new targets associated with the flow of benefits to the needy. (See Tab A.)

A post-authorization attempt to revise the Project Paper was made in Washington, but it was found that some of what was proposed, (the involvement of the Private Development Corporation of the Philippines, for example) was not possible, and in other cases adequate data, information and consultation with Ugandan institutions was not available for a complete, thorough and internally consistent revision. The exercise thus would have required engaging in considerable fiction. Finally, to a degree, the revision has been overtaken by events as the economic and institutional setting in Uganda continues to evolve.

With the above in mind, it was eventually decided to leave substantial revision for a subsequent PP supplement which will have to be accomplished in any case and forwarded to Washington for review and approval prior to moving ahead with Phase II at the end of Project Year 2 (September 1986). In the meantime, material in pages immediately following (listed below) should be consulted as the officially approved version for purposes of the initial and experimental Phase I (October 1984 - September 1986) of the project:

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Revised Part I - Summary and Recommendations

Action Memorandum requesting authorization

Project Authorization

Tab A. Revisions to Project Documentation to Assure an Increased flow of Project Benefits to the Needy, and,

Tab B. Supplementary Statement on Pre-Implementation Period and Budget

The project paper proper (commences some thirty pages into the document) should be consulted for background and concepts underlying design and feasibility aspects of the project and as the starting point for the development of Phase II.

PART I - SUMMARY AND RECOMMENDATIONS

A. Grantee and Executing Agencies.

The Ministry of Finance is the designated grantee for this project and will sign the Grant Agreement on behalf of the Government of Uganda. The Bank of Uganda (central bank of the country) will be the official executing agency.

B. Recommendation.

1. A grant in the amount of $18.2 million, over a five year period commercing in October 1984, should be authorized to the Government of Uganda for the preparation and execution of the intermediate credit system development project described in Part III of this project paper. The contribution to the project from the recipient country will amount to the U.S. dollar equivalent of $8.2 million (31% of total project cost).. Of the total project cost of 26.4 million, sub-borrowing enterprises are expected to contribute approximately $3.2 million while intermediate credit institutions will finance about $5 million. (See Financial Plan.)

2. Waivers:

a) A blanket waiver request to allow the purchase by sub-borrowers of items of Geographic Code 935 source and origin of up to $3 million is requested as part of the authorization. This is due to a design team estimate that up to 100 sub-borrowers under the project will be rural based, for the most part, and geographically disbursed with little access to procurement information on commodities other than those normally available in the vicinity of the enterprise. Likewise, maintenance and repair services will only be available for equipment normally in use the sub-project area, and few, if any, of the commodities likely to be imported by sub-borrowers are currently imported by Uganda from the United States.

b) A blanket six month source/origin shipping waiver and a determination of non-availability of US Flag vessels will be requested from AID/W (SER/COM/TS) shortly before the first project commodities are purchased. Although such a determination could be supported at this time from Europe and Japan to Mombassa, because there is currently no US flag liner service on these routes, this may not be the case at the time project procurement is initiated.

C. The Project.

The project consists of assistance to improve income of the rural poor and increase agricultural production in Uganda through increased productive investment in agricultural enterprise.

Assistance is further provided to help in strengthening the capacity of both borrowers and lenders in the country for productive investment in agriculture through provision of (a) technical assistance and training for improved managerial and technical capacity of both groups, and (b) start-up lending capital for priming of the credit systems to be strengthened and to enhance experience and capital mobilization capability necessary for self-sustained development in the future.

The structure of the project is built around the notion of separate but mutually reinforcing packages aimed at the two key levels, credit intermediary and borrowing enterprise. Overall management and coordinating responsibility for the project will be lodged with the Central Bank of the country (The Bank of Uganda [BOU]). As a practical matter, however, the effort will be directed primarily through the efforts of US contractors in collaboration with the management of the lead lending institution, the Uganda Development Bank (UDB). The project will also be carried out in a collaborative style with a World Bank/UNDP team, currently working with the UDB in critical line positions to strengthen industrial lending and overall management of the institution and its operating procedures.

In the AID/W review of the project, it was agreed that the project, as originally conceived and presented in the PP, (a three-phased, $32 million, seven and one-half year effort) should be modified in order to: a) eliminate the last phase of the project, cutting the project to five years at less than $20 million, b) incorporate further analysis of project assumptions and an accelerated trial operations activity in order to meet certain early credit demands and validate or adjust design structure on the basis of this experience (AID/W is to approve design adjustments and the revised plan for the main implementation phase of the project on the basis of an evaluation of this early experience), and c) adjust budget assumptions and guidelines for non-credit elements of the project to encourage more of an indigenous, lower cost approach to technical assistance, training and management of project activities. These modifications along with a new adjusted budget and other changes relative to the flow of benefits to the needy are detailed in Tabs A and B to the Action Memorandum requesting authorization incorporated in the following pages.

D. Summary Findings.

The Project Committee has reviewed the detailed economic, financial, institutional, social, environmental and administrative analyses carried out for the proposed project (Parts IV and V and corresponding Annexes). In each case, the project was found feasible and beneficial. The project is also found appropriate within the framework of official USAID country program and sector strategies. Project authorization, therefore, and early execution, are recommended.

E. Legal Criteria:

The project meets all applicable statutory criteria. As this is an intermediate credit institution (ICI) project, planning and costing requirements of Section 611 (a) of the 1961 FAA are considered satisfied through institutional analysis and the application of detailed AID program, policy and project criteria as applied to both ICIs and sub-borrowers under the lending component of the project. With respect to the Host Country contribution requirement, combined GOU and participating ICI and enterprise inputs to the project are calculated at 31% of total project cost (See Financial Plan). The GOU request for assistance in the form of this project is attached as Annex G.

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ACTION MEMORANDUM FOR THE ACTING ASSISTANT ADMINISTRATOR FOR AFRICA

FROM: AFR/PD, Norman Cohen

SUBJECT: Rehabilitation of Productive Enterprises (617-0104)

Problem: You are requested to authorize a grant in the amount of $18.2 million from development assistance funds for the Rehabilitation of Productive Enterprises (RPE) project in Uganda. The FY 1984 obligation amount is $6.0 million. The RPE project will be the centerpiece of the AID program in Uganda, utilizing the lion's share of Uganda's OYB in each of the three fiscal years, FY 1984 - FY 1986.

Background: In the analysis of the USAID the most serious development problem facing Uganda today and the rural and urban poor (in terms of employment and adequate markets for primary production) is severely debilitated productive capacity to meet requirements for consumption and export. Constraints associated with this generalized problem include lack of investment capital and a continuing liquidity problem in financial systems, lack of sound delivery vehicles for credit and associated services, and lack of administrative and technical absorptive capacity of the producer group.

In response to these factors the RPE project, as initially conceptualized, was to provide rapidly disbursing credit and associated technical assistance through the Cooperative Development Bank (subsequently dropped as a viable lending alternative) to a target group of primarily export oriented agricultural enterprises (mainly cotton and coffee) and some heavier non-agricultural industries. During design analysis, however, it was found that: a) the needs of the original target group were being addressed by other donors, while the principal gap was in the area of investment capital for non-specific cash crops and agriculturally related industries in general, and b) the project must move at a pace commensurate with the weak existing institutional environment (public and private) implying the need for a long-term system building effort to develop required absorptive capacity at both intermediate lending and sub-borrower (target enterprise) levels.

It also became necessary to revise certain elements of project design and conditions in order to assure that project objectives related to the flow of benefits to the needy are adequately addressed during implementation and sufficiently reflected in authorization documentation (See Tab A).

Discussion:

A. The Project:

The project, as redesigned, consists of assistance to improve income of the rural poor and increase agricultural production in Uganda through increased productive investment in agricultural enterprise. Assistance is further provided to help in strengthening the capacity of both borrowers and lenders in the country for productive investment in agriculture through provision of (a) technical assistance and training for improved managerial and technical capacity of both groups, and (b) start-up lending capital for priming of the credit systems to be strengthened and to enhance experience and capital mobilization capability necessary for self-sustained development in the future.

The structure of the project is built around the notion of separate but mutually reinforcing packages aimed at the two key levels, credit intermediary and borrowing enterprise. Overall management and coordinating responsibility for the project will be lodged with the Central Bank of the country (The Bank of Uganda [BOU]). As a practical matter, however, the effort will be directed primarily through the efforts of US contractors in collaboration with the management of the lead lending institution, the Uganda Development Bank (UDB). The project will also be carried out in a collaborative style with a World Bank/UNDP team, currently working with the UDB in critical line positions to strengthen industrial lending and overall management of the institution and its operating procedures.

In the AID/W review of the project, it was agreed that the project, as presented in the PP (a three-phased, $32 million, seven and one-half year effort) should be modified in order to: a) eliminate the last phase of the project, cutting the project to five years at less than $20 million, b) incorporate further analysis of project assumptions and an accelerated trial operations activity in order to meet certain early credit demands and validate or adjust design structure on the basis of this experience (AID/W is to approve design adjustments and the revised plan for the main implementation phase of the project on the basis of an evaluation of this early experience), and c) adjust budget assumptions and guidelines for non-credit elements of the project to encourage more of an indigenous, lower cost approach to technical assistance, training and management of project activities. These modifications are described along with a new adjusted budget in Tab B. Subsequent to authorization these changes, along with those described in Tab A relative to the flow of benefits to the needy, will be incorporated within the project paper proper so that it may serve as a valid management tool during implementation.

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B. Financial Summary of the Project:

1. The US Contribution to the project, summarized below, will total $18.2 million of which $6.0 million is to be obligated in FY 1984. This, as noted above, represents a very substantial reduction from the $33.9 million activity proposed in the PP. Of the total, $10.0 million is for the credit component representing the foreign exchange costs of sub-projects to be financed, and $8.2 million is for all other costs including technical assistance, training, commodities, procurement services for sub-projects, auditing, data management and evaluation etc. These figures include a 7% compounded inflation factor. The detailed revised budget is shown in Tab B.

Category	LOP Funding Requirements ($000)
Credit (includes inflation)	10,000
Project Operations	
Technical Assistance & Training	5,582
Other Costs (Commodities, Procurement, Research Evaluation etc.)	1,333
Sub-Total	6,915
Inflation	1,292
Sub-Total	8,208
Grand Total (rounded)	18,210

2. The Host Country will contribute an estimated US$5 million to the project in the form of local currency components of project sub-loans while borrowing enterprises will contribute another $3.2 million in equity contributions and technical assistance cost associated with sub-projects for a combined contribution of $8.2 million or 31% of total cost.

C. Socio-economic, Technical and Environmental Soundness:

1. AID/W has reviewed the detailed economic, social, financial, institutional, and administrative analyses carried out for the proposed project (Parts IV and V of the PP and corresponding Annexes). In each case the project was found feasible (or likely to be feasible) and in compliance with AID policy and programming criteria. The project is also found appropriate within the framework of official USAID country program and sector strategies.

2. Environmental Determination: Although the IEE resulted in a negative determination for Class I sub-activities, and deferred threshold decisions for Class II and III sub-activities, and an environmental assessment is not required before authorization, the project involves activities and locations that are as yet not specifically identified and confirmed for financing. This is an Intermediate Credit Institution (ICI) project; the sub-project list is still illustrative. A system has been designed and approved, however, which provides for environmental classification of loan applications and ascending levels of review depending on the size of the activity and its potential for environmental harm and for the institution of mitigating measures and/or further analyses as necessary prior to sub-project approval and funding. Procedures are described in detail in the Environmental Analysis, pp. 85-90 of the PP.

3. Human Rights: In the case of Uganda, Section 116 (a) of the FAA restricts AID activities to assistance that directly benefits needy people. In this project, benefits to the needy should be substantial as a result of its employment impact, the establishment of new and/or more competitive markets for the production of primary agricultural commodities by small holders, increased availability of lower cost farm inputs for improved profitability on small farms and the increased supply of lower cost basic household food items for poor consumers. In addition, in the review process, the project has been revised and measures adopted to enhance the flow of benefits to the needy. (See Tab A.) Section 116 is thus considered satisfied.

4. Section 611 (a) As this is an ICI project, planning and costing requirements of Section 611 (a) of the FAA are considered satisfied through the application of detailed AID program, policy, and sub-project criteria as applied to both ICIs and sub-borrowers under the lending component of the project.

D. Implementation Plan: Implementation arrangements and plan, detailed on pp. 92-110 of the PP, have been reviewed and deemed sound by the USAID and AFR. Subsequent to authorization, however, they will have to be adjusted to a degree in order to take into account revisions to the first two years of the project detailed in Tab B. Implementation arrangements for the last three years of the project may also need to be modified on the basis of experience during the pre-implementation trial operations period.

E. Procurement and Waivers: The procurement of commodities will be accomplished under policies set forth in Chapter 19 of

Handbook 1, Supplement B. Kenya will be regarded as a local cost source under the extended shelf items rule. Most procurements under the lending activity of the project will be for over $5,000 but less than $100,000 in value. The procurement services agent (PSA) acting for and together with private sector sub-borrowers will be expected to follow good commercial business practices and use informal (negotiated) procurement methods for these purchases. For individual procurements exceeding $100,000, formal competitive bidding procedures will be followed with the USAID retaining its right to approve the issuance of IFBs and related contract awards.

With respect to waivers, a blanket waiver to allow the purchase by sub-borrowers of items of Geographic Code 899 origin/Code 935 source of up to $ 3.0 million is requested as part of the authorization. This is due to a design team estimate that up to 100 sub-borrowers under the project for the most part will be rural based and dispersed with little access to procurement information on commodities other than those normally available in the vicinity of the enterprise. Likewise, spare parts, maintenance and repair services are only available for equipment normally in use in the area, most of which is of Code 899 origin. Little, if any, of the equipment and spare parts likely to be imported by sub-borrowers is currently imported by Uganda from the United States.

In addition, a blanket six month source/origin shipping waiver and a determination of non-availability of US Flag vessels will be requested from AID/W (SER/COM/TS) shortly before the first project commodities are purchased. Although such a determination could be supported at this time from Europe and Japan to Mombassa, because there is currently no US flag liner service on these routes, this may not be the case six months from now.

F. Justification to the Congress: An Advice of Program Change was submitted to Congress on June 15, 1984, and the waiting period expired on June 30, 1984, without objection.

G. Conditions and Covenants: Conditions and covenants to ensure timely and effective implementation of the project are included in the attached authorization.

Recommendation: That you sign the attached Project Authorization and thereby a) approve funding of $18.2 million for a grant to the Government of Uganda for the credit project as described in the attached project paper (as modified by Tabs A and B) and b) approve the requested source/origin waiver.

Clearances:

DAA/AFR, A. R. Love	[illegible]	Date	9/24/[illegible]
DAA/AFR, P. Birnbaum	[illegible]	Date	9/24/84
A-AAA/PRE, C. Buchanan	(draft)	Date	9/24/84
GC/AFR, T. Bork	[illegible]	Date	[illegible]
AFR/EA, E. Spriggs	(draft)	Date	9/14/84
AFR/DP, H. Johnson	[illegible]	Date	9/24/84
AFR/TR/ARD, R. Holmes	(draft)	Date	9/14/84
AFR/PMR/RCS, T. Rattan	(draft)	Date	9/21/84
SER/COM/ALI, P. Hagan	(draft)	Date	9/14/84
PPC/PDPR, M. Zak		Date	
DAA/PPC, A. Herrick	CBH	Date	9/25/[illegible]

AFR/PD/EAP: ~~JHeard~~: 8/29/84: 1130J

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PROJECT AUTHORIZATION

Name of Country: Uganda

Name of Project: Rehabilitation of Productive Enterprises

Number of Project: 617-0104

1. Pursuant to Section 531 of the Foreign Assistance Act of 1961, as amended, I hereby authorize Rehabilitation of Productive Enterprises Project (the "project") for Uganda (the "Cooperating Country") involving planned obligations of not to exceed eighteen million two hundred thousand U.S. dollars ($18,200,000) in grant funds over a three year period from date of authorization subject to the availability of funds in accordance with the A.I.D. OYB/allotment process, to help in financing foreign exchange and local currency costs for the Project. The planned life of the Project is five years from the date of initial obligation.

2. The project consists of assistance to improve income of the rural poor and increase agricultural production in Uganda through increased productive investment in agricultural enterprise. Assistance is further provided to help in strengthening the capacity of both borrowers and lenders in the country for productive investment in agriculture through provision of (a) technical assistance and training for improved managerial and technical capacity of both groups, and (b) start-up lending capital for priming of the credit systems to be strengthened and to enhance experience and capital mobilization capability necessary for self-sustained development in the future.

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

4.a. Source and Origin of Commodities, Nationality of Services

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

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the Cooperating Country or countries included in A.I.D. Geographic Code 941.

4.b. Conditions Precedent.

(1) Disbursement for Technical Assistance. Prior to the first disbursement under the Grant for technical assistance, or to the issuance by A.I.D. of any commitment document to finance such assistance, the Grantee shall furnish to AID, in form and substance satisfactory to AID, except as AID may otherwise agree in writing, evidence of:

(a) The establishment of a high level, inter-agency project committee to provide for national oversight of the project's execution and to serve as a vehicle for policy level intervention when necessary. The evidence submitted should include terms of reference and operating procedures for the committee, and

(b) The establishment, or intention to establish within a satisfactory time period, of a consolidated agricultural projects appraisal department within the Uganda Development Bank which will draw from the existing Crops and Livestock departments.

(2) Disbursement for Lending. Prior to the first disbursement under the Grant for lending, or to the issuance by AID of any commitment document to finance such disbursement, the Grantee shall furnish to AID, in form and substance satisfactory to AID, except as AID may otherwise agree in writing:

(a) Evidence of an established rediscount facility in the Bank of Uganda, to be utilized by project Intermediate Credit Institutions (ICIs), particularly the Uganda Development Bank, for securing the local currency counterpart contributions required for the sub-lending program. This evidence shall include the terms, conditions, and operating procedures for access and drawdowns from this facility;

(b) Evidence of the establishment of a special account for repayments by ICIs of Project loans which are to be relent for purposes in accord with project criteria in general, together with procedures for use of funds in the special account.

(c) Evidence of the development of an officially approved operations manual for the lending component of the project including credit policy and regulations and lending criteria for ICIs, sub-borrowers, and sub-projects. This will also include:

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(c.1.) Procedures for complying with AID's environmental regulations

(c.2.) Evidence of the intent of the credit policy to provide for loans to sub-borrowers at positive real rates of interest (above officially established rate of inflation)

(c.3.) Evidence of the establishment of lending policies and criteria for sub-loan and sub-borrower eligibility which will assure effective participation of needy people in the benefits of investments to be financed by the project. Among other things, the policy will require that only sub-project proposals that demonstrate that one or more of an illustrative list of approved benefit impacts (to be included in the presentation) will, in fact, occur, will be approved. The policy will also require that the basis for approval be documented.

(c.4.) Procedures for referring proposed sub-loans to AID for approval with respect to AID's project, program, policy and legal requirements;

(d) Evidence of compliance with environmental analysis, review and mitigating measures procedures outlined in project implementation letters for sub-projects to be financed by the first disbursement and agreement with respect to environmental procedures for all subsequent disbursements;

(e) Signed loan agreements with the applicable ICIs to participate in the lending activity; (Once a loan agreement is signed with one ICI, lending may commence through that particular ICI. New loan agreements may be signed over the life of the project, each to be approved by AID, as each new ICI applies to participate in project lending activity. The loan agreements will stipulate compliance with project lending criteria and provide for terms and conditions acceptable to AID.)

(f) Evidence of acceptance of negotiated ongoing maximum levels of delinquency and default rates, at both ICI and sub-borrower levels, over the life of the project. It will be further accepted that if such rates exceed the agreed upon levels (in either or both the ICI in question and the sub-borrower group) disbursements for lending through that ICI will be stopped until the BOU and AID are satisfied that the rates have dropped below the levels in question and that adequate measures have been taken to avoid future occurrences of the problem;

(g) A statement that imported project commodities will be exempted from import duties and inspection fees etc.

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(3) Disbursement for Phase II. Prior to the first disbursement under the Grant for Phase II, or to the issuance by AID of commitment documentation for such disbursement, the Grantee shall submit to AID, in form and substance satisfactory to AID, except as AID may otherwise agree in writing:

(a) detailed plans and costs for Phase II project execution (based on the findings of the comprehensive evaluation to be carried out toward the end of Phase I in late 1986), and

(b) government approval of a plan to establish an independent technical assistance entity by the end of the project. The evidence should indicate approval of the concept and the substance of the proposed plan for arriving at the independent enterprise. The evidence should also indicate approval of the initial establishment of the technical assistance entity under the proposed Prime Contract.

4c. Covenants.

The Grantee shall covenant that, except as AID otherwise agrees in writing, it will:

(1) Assure that proposed sub-loans for an amount exceeding $200,000 in AID financed costs will be submitted to AID for approval prior to disbursement;

(2) Assure that the AID receives copies of all sub-loan proposals in general for purposes of information and monitoring;

(3) Assure that loans made available under the project will be payable through ICIs to private enterprises in both foreign exchange and local currency in accordance with the approved loan application submitted by the private enterprise. Repayment of loans at both the ICI and private enterprise levels will be entirely in local currency, the amount thereof determined with respect to the foreign exchange loan, in accordance with the rate of exchange prevailing at the time the foreign exchange is disbursed to or on behalf of the borrower.

(4) Attempt to reach agreement with commercial ICIs interested in participating in the project with respect to a combination of interest rates and a possible local currency credit guarantee scheme which will allow such ICIs to project a satisfactory return to their participation at an acceptable risk;

(5) Continue to review and revise interest rate ceilings in line with inflation rates;

(6) Make its best efforts to:

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(a) resolve the edible oil ex-factory tax question in a manner condusive to the development of the local industry and production for the Uganda market;

(b) resolve disputes over ownership of private enterprises soliciting credit for sub-projects under the project; and

(c) provide and maintain qualified counterpart personnel on a timely basis in the UDB;

(7) Require participating ICIs to develop procedures for making sub-loans under the project that include environmental analysis and review procedures satisfactory to AID; and

(8) Require participating ICIs to include the following conditions/covenants in each sub-loan agreement:

(a) With respect to all Class II and Class III activities, a covenant whereby the borrower agrees that production operations will not commence until adequate facilities for organic and toxic waste treatment are in place and whereby the borrower agrees to a right of inspection by the representatives of the lender, GOU or AID to insure compliance with, and the adequacy of, any environmental design requirements or environmental protection facilities agreed to as part of the loan approval process; and

(b) In the case of large industrial opertions which will receive loan funds in increments, a condition precedent to receipt of subsequent increments of loan funding requiring evidence that satisfactory progress has been made on installation of waste treatment facilities and verification (by intial monitoring) that the design of the facilities is adequate.

4.d. <u>Waiver</u>.

(1) Pursuant to the authority of HB 1B, CH 5B4a(2) and (7), and based on the justification contained in Annex C to the project paper, I hereby approve a source/origin waiver to AID Geographic Code 899 in an amount not to exceed $3 million, for procurement of commodities by sub-borrowers under the project.

Mark L. Edelman

Mark L. Edelman
Acting Assistant Administrator
Bureau for Africa

9-25-84

Date

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Clearances:
DAA/AFR, P. Birnbaum PB Date 9/24/84
AFR/DP, H. Johnson for HJ by [illegible] Date 9/24/84
AFR/PD, N. Cohen NC Date 9/25/84
AFR/PD/EAP, JHeard JH Date 9/24/84
AFR/EA, E. Spriggs for [illegible] Date 9/24/84
GC/AFR, T. Bork [illegible] Date [illegible]
DAA/PPC, A. Herrick AKH Date

GC/AFR:MAKleinjan:afn:09/14/84:632-3808:0431H

Tab A.

REVISIONS TO PROJECT DOCUMENTATION TO ASSURE AN INCREASED FLOW OF PROJECT BENEFITS TO THE NEEDY

REHABILITATION OF PRODUCTIVE ENTERPRISES PROJECT (RPE) - UGANDA

I. Introduction:

It has become nececessary to revise certain elements of project design and conditions in order to assure that project objectives related to the flow of benefits to the needy are adequately addressed during implementation and sufficiently reflected in authorization documentation. The purpose of this tab is to detail those revisions for review and approval.

Other modifications having to do with pre-implementation activity, the budget, phasing and duration have also been determined on the basis of technical recommendations from the project review process. These are detailed in Tab B. As a practical matter, given limited time remaining in the fiscal year for authorization, negotiation and obligation of the grant in the field, it was decided to indicate changes in this form for purposes of authorization and to revise the PP itself as soon as possible thereafter. For this reason, the reviewer will note certain inconsistencies between what is presented here and the text of the PP. Proposed revisions to the PP are detailed under Section IV below.

II. Background:

The original goal structure and design of this project was built around a set of assessed constraints related to the overriding Ugandan economic problem of severely debilitated productive capacity in relation to the country's ability to meet its requirements for both consumption and export. Constraints included lack of investment capital, lack of sound delivery vehicles for credit and associated services, lack of administrative and technical capability at the producer level, etc. The project was thus designed to address the principal gap which was assessed to be a generalized lack of financial, technical and administrative absorptive capacity for capital investment at all levels amongst both borrowers and lenders.

The product of the above effort, therefore, focussed on institution and system building while incorporating badly needed lending capital as a contribution to "prime" the system and to meet the immediate needs of a portion of the productive sector which for now and in the foreseeable future had no access to other sources of such assistance, ie., agricultural enterprise (not including the major cash export crops, cotton and coffee where needs are being addressed by other donors).

In line with the system focus of the design exercise, analyses concentrated on economic, financial, and institutional feasibility in terms of the lending channels to be strengthened and a set of illustrative sub-projects in relation to potential viability and return on investment. The analyses did not focus sufficiently on the question of benefit incidence in relation to the needy, as enterprises to be financed represented target clientel of a somewhat different character, ie., the low and mid-level entrepreneurial group (average investment loan size in the range of $30,000 to $80,000).

It was hypothesized on the basis of other analyses and field observation, nevertheless, that the needy would in fact benefit substantially from sub-project financing in the following ways:

- Increased employment and reduced under-employment of rural and urban poor wage earners as a consequence of investments in expanded agricultural enterprise operations both on and off the farm. It is estimated 1,500 new jobs will be created directly and an additional unknown number from secondary effects.

- The establishment of new and/or more competitive markets and improved prices (from increased competition amongst processors and buyers of primary production) for agricultural commodities, most of which is in the hands of small holders through the financing of such ventures as oil mills, feed mills, poultry and dairy processing operations etc.

- Increased availability of domestically produced, lower cost, farm inputs for lower production costs and improved profitability at the small holder level.

- Increased domestic production of a variety of food crops resulting in increased availability and lowered cost to rural poor consumers of such basic commodities as cooking oil, maize flour, beans, vegetables, milk and milk products. It is for such items (with the addition of sugar, tea, salt and soap) that the bulk of rural disposable income is dedicated.

Although the above linkages and benefits have not been analytically demonstrated, the necessary analyses can now be carried out as part of pre-implementation assessment activity as well as on a case by case basis as sub-projects are considered for financing. (See following section.)

Is important to note here, that the vast majority of Ugandan population is, in fact, needy. About 90% of the population lives in rural areas and engages in farming to meet subsistence and cash income needs. Land holdings average less than 2.3 Ha. and farming is carried out with very simple hand tools for the great majority. A high percentage of households are unable to meet basic food requirements throughout the year and annual expenditure levels on basic household commodities for most families hover in the area of $100 or less. [Source: "The Uganda Social and Institutional Profile, August 1984, prepared for AID by The Experiment in International Living.]

III. Measures to Enhance the Flow of Project Benefits to the Needy.

A. Purpose of the Project.

The primary purpose of the project has been revised from its previous focus on lending system improvements as follows:

Improved income for the rural poor and increased agricultural production through increased investment in agricultural enterprise (primary production, processing, marketing, and other agriculturally related operations).

Conditions expected at the end of the project and lower level indicators will include the original system and enterprise development objectives in addition to new targets associated with the flow of benefits to the needy.

B. Lending Criteria:

Currently proposed lending criteria, detailed on pp. 83 and 84 of the PP, incorporate standard AID program and policy criteria (adequate planning and costing, environmental, financial, technical, social, and managerial soundness) in addition to requiring sub-projects to meet one of three key conditions; labour intensive technology, potential for import substitution or export, or provision for increased markets, inputs, or services for agricultural production based on locally available inputs. Additional criteria relate to ICI and sub-borrower eligibility in terms of institutional capability, ownership, operating policies etc. The spirit of the criteria is to promote a viable, self-sustaining private enterprise growth and development process, while also emphasing traditional principles of prudent investment and assuring the application of important AID policies.

One of the criteria relates to social soundness or equity, although lacking is definition in terms of exactly what is to be weighed in such a determination. To correct this gap, it is now proposed that prior to financing any sub-project, it must be demonstrated that the investment will result in one or more of the following benefit impacts relative to the ultimate target group of needy people.

1. Increased employment of rural or urban poor wage earners or potential wage earners (to include on or off farm employment of small holder family members).

2. Increased income for small holder agricultural producers through improved markets and better prices for primary production and/or through reduced cost of production from lower cost farm inputs.

3. Increased availability and lower cost of basic food commodities to rural and urban poor consumers from increased domestic production.

4. As a corollary to No. 3., improved nutrition/health of rural and/or urban poor as a result of increased availability and/or lower cost of essential food commodities required for adequate diet.

5. Increased real wages paid to under-employed/underpaid workers due to improved enterprise profitability, expanded operations, appropriate technology, etc.

6. More efficient utilization of family labour (women, children, parents) on the farm or within the household enterprise. This could also include village enterprises in production, processing or provision of agriculturally related goods or services.

7. Increased and/or more effective participation of women in the enterprise financed and economic benefits to be derived therefrom.

8. Improved economic returns to small producers, processors, or intermediaries from reduced government participation in all or portions of the production and marketing chain for given commodities.

9. Improved returns to rural or urban poor cooperative members or enterprise shareholders from improved efficiency and economies of scale, more equitable management and distribution of profits, etc.

It is recognized that there is some redundancy in the above list and that other potential impacts could undoubtedly be developed and added. At this point, however, these impacts are illustrative and will need to be mutually agreed upon by AID and the Grantee. They will also be further refined during detailed planning efforts in the pre-implementation period. On the basis of early experience, there may also be a need to negotiate modifications during implementation. In any case, the basic principle of a solid flow of benefits to the needy will be maintained and emphasized throughout the project. Finally, if and when qualified sub-project demand exceeds availability of project funding, the greater the flow of benefits associated with a particular sub-project, the greater the priority that will be accorded to it in the selection process for financing.

B. Conditions:

A condition precedent to the first disbursement for lending requires the grantee to furnish, in form and substance satisfactory to AID, an officially approved operations manual for the lending component of the project including credit policy and regulations and lending criteria for ICIs, sub-borrowers and sub-projects. To further assure compliance with project objectives with respect to the needy, the condition has been strengthened to include detail with respect to the matter of benefits to the needy as follows:

> " ...the manual will also include evidence of the establishment of lending policies and criteria for sub-loan and sub-borrower eligibility which will assure effective participation of needy people in the benefits of investments to be financed by the project. Among other things, the policy will require that only sub-project proposals that demonstrate that one or more of an illustrative list of approved benefit impacts will, in fact, occur, will be approved. The policy will also require that the basis for approval be documented. "

Contract assistance will be provided to both lenders (ICIs) and sub-borrowers to assure that the above policies and criteria are faithfully observed in practice during implementation.

IV. Proposed Revisions to Project Paper to Reflect Design Changes Emphasizing the Needy as the Principal Target Group of Beneficiaries:

Part II of the Paper (Background and Rationale sections) will be revised to incorporate an analysis of constraints associated with the condition of needy (especially the rural poor) as part of the Problem Analysis. The condition of the needy will also be documented in the section on the Economic Setting.

Part III of the Paper (Detailed Description) will be revised as follows:

Overview and Approach sections will be modified to include summary descriptions of strategy to reach the needy target group in line with the thinking expressed above.

Detailed Activity Descriptions will be revised to incorporate special activities (scopes of technical assistance and training interventions) designed to assure compliance with objectives to increase participation of the needy in benefits of the project. Under the data management section of the project, which already includes a number of studies touching on the issue to a greater or lesser extent (base line data, credit demand, profiles of client enterprises, constraints to enterprise development, alternative capital markets, women and development) increased emphasis will be placed on analyzing and developing ways and means of promoting greater spread effects.

The Evaluation Plan, also covered in Part V, will be revised to incorporate analyses in both scheduled evaluations, years 2 and 5, as to the effective pursuit of benefit objectives for the needy and achievements related thereto. The evaluation will draw heavily from the Data Management activity for relevant baseline and time-series information.

Part IV (Project Analyses) will be modified to incorporate an analysis of benefit incidence and how it may be increased under the Social Soundness and Economic Analyses sections. Institutional, financial and lending criteria sections will also be modified appropriately.

Part V (Implementation Arrangements) will require relatively little modification on the question of benefits to the needy, although it will be revised to accomodate other changes in phasing, budget and pre-implementation activity.

Annexes will be modified appropriately where necessary, especially the expanded project analyses and the logical framework.

AFR/PD/EAP: JHeard: 9/21/84: 1186J

SUPPLEMENTARY STATEMENT ON PRE-IMPLEMENTATION PERIOD AND BUDGET
PROJECT PAPER
REHABILITATION OF PRODUCTIVE ENTERPRISES
UGANDA

I. Introduction.

Based on a comprehensive review of the RPE project paper by the Africa Bureau it was agreed that the project should be modified in accordance with the following guidelines:

A. The basic design of the project is considered valid. Proposed modifications pertain only to the pre-implementation period, project phasing and length, and budget assumptions.

B. The third and last phase of the project is to be eliminated, cutting the project from a seven and one-half year effort to approximately five years.

C. The initial pre-implementation period is to be modified to incorporate further analysis of project assumptions and an accelerated trial operations activity in order to meet certain early credit demands and validate or adjust design structure as described in the PP.

D. Budget assumptions and guidelines for non-credit elements of the project are to be reworked to encourage more of an indigenous, lower cost approach to technical assistance, training and management of project activities.

Upon approval in final form these changes will be incorporated within the project paper proper so that it may serve as a valid management tool during implementation. In the meantime, and for purposes of authorization, proposed modifications and budget adjustments are as described below:

II. Modifications to Basic Design.

A. Project Period and Phasing.

The third and last phase of the project, originally to commence in January 1989 and run for three years, is eliminated. The assumption is that if a third phase is warranted by experience and analysis during implementation, the need would be handled through an RPE II follow-on project. Also, given the more ambitious effort to be realized during what was to be the initial pre-implementation period, i.e., pilot lending and other operational activity, this

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period has been extended to two years and will run from obligation of the initial tranch of funding (September 1984) to the end of September 1986. Overall project length, therefore, including the three-year primary implementation effort, will come to five years and conclude in September 1989.

B. Pre-Implementation: September 1984 - September 1986.

1. Concept.

During the original pre-implementation period (June 1984 - Dec. 1985) critical planning, preparation and gearing-up activities were to take place including contractor recruitment and mobilization, the meeting of conditions precedent, preparation of detailed work and procurement plans, etc. Under the revised package, the objective is to augment this activity with:

- an additional analytical effort to revalidate and/or adjust design structure and approach as necessary in order to adopt more flexible, efficient, less demanding and less costly vehicles and procedures for lending to target clientele (through private commercial banking channels to the extent possible), and,

- a pilot lending effort to be implemented on an experimental basis with a select group of high priority sub-projects which are determined to be more ready to finance in terms of established feasibility and sound investment and management plans.

On the basis of the above experience, the design, structure and plan for the main operational phase of the project (fiscal years 1987-1989) will be modified as warranted depending on the nature and magnitude of changes contemplated. Washington review and approval will be required prior to proceeding with Phase II.

2. Implementation.

a) Finance and Development Specialist.

As soon as possible following execution of the Grant Agreement, a finance and development banking specialist will be recruited and contracted for services in Uganda. Ideally this person should combine a background and skills as an AID finance or projects officer and as an intermediate credit and development banking specialist. The contract will be structured flexibly to retain the person's professional services on an as required basis over the course of the pre-implementation period. It is estimated that approximately nine months of consulting time will be needed which would be provided in five or six trips of an average of six to eight weeks each.

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The plan, role and functions of the specialist will be as follows:

(1) Assist the GOU and the USAID with the meeting of principal conditions precedent for both technical assistance and lending, i.e., establishment of the high level project oversight committee and its groundrules, the consolidation and restructuring of the Crops and Livestock Departments of the UDB together with the group to be brought in from the Private Development Corporation of the Philippines (See below), development and approval of an operating procedures manual for project lending (including the refinement and negotiation of ICI, sub-borrower, and sub-project criteria), loan agreements between the Bank of Uganda (BOU) and participating ICIs, and the establishment and operating procedures for the rediscount facility in the BOU for the provision of the local currency contribution requirement for UDB lending.

(2) Assist the GOU (Bank of Uganda), USAID and REDSO/ESA with the development, approval and establishment of simplified criteria and procedures for project review and approval, procurement, disbursement and vouchering, implementation management in general and monitoring, with special attention directed to environmental criteria and procedures, now considered to be overly rigorous for efficient implementation. (Modification of environmental criteria and procedures will have to be approved by REDSO/ESA as may other changes if substantive.)

(3) In collaboration with the Philippine group, assist participating ICIs, early prospective sub-borrowers and the USAID with the review, refinement and approval of an initial group of sub-projects to be financed during the pre-implementation period including the development of management plans and follow-up assistance activity for such projects from technical assistance to be supplied by the project during the main implementation phase.

(4) Assist the USAID with the development of scopes of work and solicitations for the various short and long term contracts under the project, including technical assistance and training for ICIs and sub-borrowers, procurement assistance, auditing services, and further analysis and evaluation.

(5) In collaboration with the Philippines Group assist the USAID with the planning and realization of an evaluation of pre-implementation experience against the original design of the project and with redesigning of the main implementation Phase of the project to the extent warranted by findings and recommendations of the

evaluation, including revision of various scopes of work for longer term technical assistance and training activity and the development and presentation of a PP supplement for field or Washington approval depending on the nature and magnitude of changes contemplated.

b) The Private Development Corporation of the Philippines.

Subsequent to authorization of the project a sole source waiver for the procurement of technical assistance from the Private Development Corporation of the Philippines (PDCP) will be sought in order to provide uniquely relevant technical assistance and training services to ICIs participating in the project, especially to the Uganda Development Bank. The objective is to bring to bear lessons learned from over a decade of experience of this organization in successful third world development lending on project operations.

As soon as possible following execution of the Grant Agreement, PDCP will be invited (under invitational travel procedures) to send a delegation of senior officers and technicians to Uganda sometime in the fall of this year (1984) to assess the situation and negotiate a draft contract for provision of the assistance tentatively described below. Such an agreement would hopefully be signed before the end of calendar year 1984 with actual assistance to commence in early 1985. It is currently envisioned that the assistance package from PDCP would consist of:

- Technical assistance extending over a period of one year in the form of one resident advisor and short term consultancies by specialists as required in finance and credit, accounting, agro-industry and marketing, project appraisal, data collection/analysis, evaluation and training. (The exact mix of skills to be brought in on a short term basis will have to await detailed planning and negotiations to be carried out by the USAID with the advance group from PDCP with assistance from the contract finance specialist described above.)

- Training in the form of participation of various key UDB and other ICI staff members in development banking courses given at PDCP headquarters in the Philippines and, on occasion, specially tailored courses to be given in Uganda by PDCP advisors, depending on PDCP's assessment of training needs made during its initial visit and early advisory work in the banking community.

More specifically, assistance to be provided is expected to include:

(1) a detailed reassessment of the proposed operating structure and plan for the project and appropriate modifications for initial lending operations (in collaboration with the contract finance specialist),

(2) technical assistance to the UDB in the consolidation and structuring of the combined Crops and Livestock Departments in collaboration with the contract finance specialist and development of an effective, streamlined project appraisal and approval procedure to be utilized during the pilot lending period. Assistance will also be directed to the development of improved supervision, monitoring and collection procedures.

(3) Assistance to participating ICIs, early prospective sub-borrowers and the USAID with the review, refinement and approval of an initial group of sub-projects to be financed during pre-implementation including the development of management plans and follow-up assistance activity for such projects from technical assistance to be supplied by the project during the main implementation phase.

(4) Assessment of training needs and development of a comprehensive training plan for ICI staffs for courses both in Uganda and at PDCP headquarters and monitoring would be carried out by the resident advisor.

(5) Assistance in the development of an initial base line data collection effort for project lending operations and for the installation of an ongoing data collection, analysis and reporting system - to feed into the Data Management component of the project once it commences under the main implementation phase.

(6) In collaboration with the contract finance specialist assistance to the USAID in the planning and realization of an evaluation of pre-implementation experience against the original design of the project and in the redesign of the main implementation Phase of the project to the extent warranted by findings and recommendations of the various scopes of work for longer term technical assistance and training activity and the development of a PP supplement if necessary.

3. Phase II - Implementation - September 1986 - September 1989

This period, unless otherwise modified by the experience of Phase I, will remain more or less as described in the project paper except that:

- It will commence somewhat later than originally contemplated, i.e., Sept. instead of Jan. 1986, and,

- The scope and budget for the prime contract will be modified to encourage indigenous or locally resident firms or PVOs (local in the greater East Africa context) to bid on either the prime contract or as a joint venturers or sub-contractors especially with respect to portions of the project dedicated to assistance to sub-borrowers (the technical assistance entity or business advisory service as described on pp. 32-38 of the PP) and procurement of commodities financed by the credit component.

- Advance work originally to be carried out by the Prime Contractor, i.e., assistance in the consolidation of the crops and livestock departments of the UDB and much of the other preliminary administrative, financial and technical arrangements for the project, will now be carried out by the PDCP and the development finance contractor, thus simplifying and somewhat lowering preliminary short term technical assistance costs and requirements originally contemplated as part of the package including substantial initial mobilization costs.

III. Modifications to Project Budget.

The revised budget, detailed in the following tables, reflects modifications described above. Principal changes incorporate:

- An extended pre-implementation period, ie., 2 years as opposed to 18 months in the original implementation plan.

- Heavy front end loading of technical assistance and training activity associated with the Private Development Corporation of the Philippines and the Finance/Development Banker inputs.

- Reduced overhead on overall direct contract costs, ie., from 85% to 35%.

- Reduced salaries and other costs associated with the Technical Assistance Entity in line with emphasis on use of local organizational capability to address the need on the sub-borrower side.

- An additional evaluation in Year 2 to validate or modify design on basis of pre-implementation experience.

- An adjusted credit line to reflect the projected earlier start of lending operations.

The above changes have a ripple effect through the original budget which has been adjusted accordingly, as have counterpart contriutions. Assumptions for the old budget remain valid for the most part. Once the project has been authorized, a new budget will be integrated within the revised PP with a new master set of adjusted assumptions.

BUDGET TABLE 1

DETAILED EXPENDITURES BY PROJECT YEAR
($000)

Project Year	1 FY 85	2 FY 86	3 FY 87	4 FY 88	5 FY 89	Total
AID FINANCED INPUTS		-				
Credit Line	500	800	2000	2400	2600	8300
Inflation (7%)		56	289	540	808	1693
Sub-total	500	856	2289	2940	3408	9993
Long Term TA						
Chief of Party			165	165	165	495
Finance Anal. (UDB)			155	155	155	465
Ag-bus. Mgt. (TA Ent)			85	85	85	255
Accounting (TA Ent)			85	85	85	255
Finance Anal.(TA Ent)			85	85	85	255
PDCP Loan Off.	75	75				150
Sub-Total	75	75	575	575	575	1875
Short Term TA						
Finance/DevBanker	60	60				120
PCDP	50	50				100
Agro-Ind.		25				25
Bus Analyst		25				25
Other Int. & Local		50	150	150	100	450
Sub-Total	110	210	150	150	100	720

(Budget Table 1. Cont.)

Project Year	1 FY 85	2 FY 86	3 FY 87	4 FY 88	5 FY 89	Total
Local Hire						
Professional Staff	30	80	130	190	190	620
Support Staff	10	20	50	50	50	180
Sub-Total	40	100	180	240	240	800
Local Travel	10	40	70	90	90	300
Local Office Costs	12	22	22	22	22	100
Training						
In-Country (ICIs)	10	20	20	20	10	80
US & Third Country	40	40	40	40	20	180
In-Country Entprs.	10	20	20	20	10	80
Sub-Total	60	80	80	80	40	340
Sub-Total Direct Contract Costs.	307	527	1077	1157	1067	4135
Contract Overhead (Consolidated: 35% on above costs - credit)	107	184	377	405	373	1447
Sub-Total TA and Trng.	414	711	1454	1562	1440	5582
Other Costs						
Commodities						
Vehicles	45	55	30	15		145
Office Equip		50	20	5		75
Computers		40				40
Sub-Total	45	145	50	20		260
Procurement Services	25	43	100	100	100	368
Research Fund (Data Management)		30	50	50	20	150
External Audit	10	50	100	100	100	360

(Budget Table 1. Cont.)

Project Year	1 FY 85	2 FY 86	3 FY 87	4 FY 88	5 FY 89	Total
Intn'l Vol Services (IESC)	5	10	10	10	10	45
Evaluations		50			100	150
Sub-Total - All non Credit Costs	499	1039	1764	1842	1770	6915
Inflation - 7% compounded	--	72	256	414	550	1292
Sub-Total - Non Credit costs)	499	1112	2020	2257	2320	8208
Total AID Financed Contributions	999	1968	4309	5197	5728	18201

Rounded: Credit: 10,000 All other costs: 8,208
Total AID: 18,210

COUNTERPART CONTRIBUTIONS						
Bank Financed Inputs. (Local Cur. Loan Component)	250	400	1000	1200	1300	4150
Inflation at 7%		28	145	270	404	847
Sub-Total:	250	428	1145	1470	1704	4997
Enterprise Financed Inputs						
Enterprise Equity	150	240	600	720	780	2490
TA Entity			50	60	65	175
Sub-Total	150	240	650	780	845	2665
Inflation - 7%		17	163	176	263	619
Sub-Total inc. Inf.	150	257	814	956	1108	3285
Total Host Country Contribution	400	685	1959	2426	2812	8282
TOTAL PROJECT COST	1470	2790	6731	8128	9127	28246

BUDGET TABLE 2

SUMMARY OF TOTAL PROJECT COST BY FUNDING CATEGORY

	AID	Banks	Enterprises	Total
A. Credit	8300	4150	2490	14940
Inflation - 7%	1693	847	507	3047
Sub-Total (Rounded)	10000	4997	2997	17994
B. Project Operations				
TA & TNG	4135		175	4310
Overhead at 35%	1447			1447
Sub-Total	5582		175	5757
Other Costs				
Commodities	260			260
Procurement Services	368			368
Research Fund	150			150
External Audit	360			360
Int'l Vol. Services	45			45
Evaluation	150			150
Sub-Total	1333			1333
C. Sub-Total: All Non-Credit Costs	6915		175	7090
Inflation at 7%	1292		40	1332
Sub-Total (Rounded)	8210		215	8425
Grand Total (Rounded)	18,210	4,997	3,212	26,419
Per Cent Contribution	69%	19%	12%	100%

Combined Total of Host Country Contributions: $8,209 or 31% of Total Project Cost

AFR/PD/EAP: JHeard: 8/20/84: 1111J

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AGENCY FOR INTERNATIONAL DEVELOPMENT

PROJECT DATA SHEET

1. TRANSACTION CODE: A (A = Add, C = Change, D = Delete)

Amendment Number:

DOCUMENT CODE: 3

2. COUNTRY/ENTITY: UGANDA

3. PROJECT NUMBER: 617-0104

4. BUREAU/OFFICE: AFRICA — 06

5. PROJECT TITLE *(maximum 40 characters)*: Rehabilitation Productive Enterprise

6. PROJECT ASSISTANCE COMPLETION DATE (PACD): MM 09 DD 30 YY 89

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

A. Initial FY 84 B. Quarter 4 C. Final FY 86

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

A. FUNDING SOURCE	FIRST FY B. FX	C. L/C	D. Total	LIFE OF PROJECT E. FX	F. L/C	G. Total
AID Appropriated Total	6,000		6,000	18,210		18,210
(Grant)	(6,000)	( )	(6,000)	(18,210)	( )	(18,210)
(Loan)	( )	( )	( )	( )	( )	( )
Other U.S. 1.						
Other U.S. 2.						
Host Country		2,000	2,000		8,200	8,200
Other Donor(s)						
TOTALS	6,000	2,000	6,000	18,210	8,200	26,410

9. SCHEDULE OF AID FUNDING ($000)

A. APPROPRIATION	B. PRIMARY PURPOSE CODE	C. PRIMARY TECH. CODE 1. Grant	2. Loan	D. OBLIGATIONS TO DATE 1. Grant	2. Loan	E. AMOUNT APPROVED THIS ACTION 1. Grant	2. Loan	F. LIFE OF PROJECT 1. Grant	2. Loan
(1) FN	274	042							
(2)									
(3)									
(4)									
TOTALS									

10. SECONDARY TECHNICAL CODES *(maximum 6 codes of 3 positions each)*: 070

11. SECONDARY PURPOSE CODE

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

A. Code	DEL						
B. Amount	18,210						

13. PROJECT PURPOSE *(maximum 480 characters)*

Improved incomes for rural poor and increased agricultural production through increased investment in agricultural enterprise.

14. SCHEDULED EVALUATIONS: Interim MM 03 YY 86; MM YY; Final MM 08 YY 89

15. SOURCE/ORIGIN OF GOODS AND SERVICES: ☐ 000 ☒ 941 ☒ Local ☒ Other *(Specify)* 899

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

17. APPROVED BY

Signature: Irwin A. Coker

Title: Mission Director

Date Signed: MM 06 DD 01 YY 84

18. DATE DOCUMENT RECEIVED IN AID/W, OR FOR AID/W DOCUMENTS, DATE OF DISTRIBUTION: MM 06 DD 01 YY 84

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TABLE OF CONTENTS

PART I - SUMMARY AND RECOMMENDATIONS

A. Grantee and Executing Agencies.

The Ministry of Finance is the designated grantee for this project and will sign the Grant Agreement on behalf of the Government of Uganda. The Bank of Uganda (central bank of the country) will be nominated as the official executing agency.

B Recommendations.

1. A grant in the amount of $32.9 million, over a seven and one-half year period commencing in July 1984, should be authorized to the Government of Uganda for the preparation and execution of the intermediate credit system development project described in Part III of this project paper. The contribution to the project from the recipient country will amount to the U.S. dollar equivalent of $ 17.9 million (36 % of total project cost). Of the total project cost of $50.8 million, sub-borrowing enterprises are expected to contribute approximately $6.9 million while intermediate credit institutions will finance about $11 million. (See Financial Plan, p. 51.)

2. Waivers:

a) A blanket waiver request to allow the purchase by sub-borrowers of items of Geographic Code 935 source and origin of up to $8 million is included in Annex C, Waivers. This is due to a design team estimate that up to 120 sub-borrowers under the project, for the most part, will be rural based and geographically disbursed with little access to procurement information on commodities other than those normally available in the vicinity of the enterprise. Likewise, maintenance and repair services will only be available for equipment normally in use in the sub-project area, and few, if any, of the commodities likely to be imported by sub-borrowers are currently imported by Uganda from the United States.

b) Annex C includes a request for a certificate of non-availability of US shipping. This will exclude from cargo preference rules any shipment of commodities not originating in the United States. Also included is a request to allow shipping costs of up to $3.0 million to be financed on Code 935 vessels.

C. The Project

The project is designed to address the principal gap identified in the problem analysis, ie., the lack of absorptive capacity of both borrowers and lenders in Uganda for productive investment in agricultural enterprise. This will be accomplished through provision of; a) technical assistance and training for improved managerial and technical capacity of both groups and b) start-up lending capital for priming of the systems to be strengthened and to enhance experience and capital mobilization capability necessary for self-sustained development in the future.

The structure of the project is built around the notion of separate but coordinated and mutually reinforcing packages aimed at the two key levels, credit intermediary and borrowing enterprise. Overall management and coordinating responsibility for the project will be officially lodged with the Department of Development Finance of the Bank of Uganda. As a practical matter, however, the effort will be orchestrated and directed primarily through the efforts of a U.S. "Prime Contractor" in collaboration with management of the lead ICI, the Uganda Development Bank (UDB). The project will also be carried out in a collaborative style with a World Bank/UNDP team, currently working with the UDB in critical line positions to strengthen industrial lending and overall management of the institution and its operating procedures.

D. Summary Findings.

The Project Committee has reviewed the detailed economic, financial, institutional, social, environmental and administrative analyses carried out for the proposed project (Parts IV and V and corresponding Annexes). In each case, the project was found feasible and beneficial. The project is also found appropriate within the framework of official USAID country program and sector strategies. Project authirization, therefore, and early execution, are recommended.

E. Legal Criteria:

The project meets all applicable statutory criteria. As this is an intermediate credit institution (ICI) project, planning and costing requirements of Section 611 (a) of the 1961 FAA are considered satisfied through institutional analysis and the application of detailed AID program, policy,

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and project criteria as applied to both ICIs and sub-borrowers under the lending component of this project. With respect to the Host Country contribution requirement, combined GOU and participating ICI and enterprise inputs to the project are calculated at 36% of total project cost (See Financial Plan, p. 51). The GOU request for assistance in the form of this project is attached as Annex G.

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PART II: BACKGROUND AND RATIONALE

A. Economic Setting

1. Historical Overview

Uganda has always enjoyed a wealth of readily accessible natural resources including favorable soils and climatic conditions for agricultural production, a rich mineral base to support the industrial sector, and ample water and forests for energy development. During the 1960's, the country had begun to exploit this potential, supported by an infrastructure which was well developed compared to most other Sub-Saharan African countries. As a result Uganda was self-sufficient in food and exported large quantities of coffee and cotton and to a lesser extent tea and tobacco.

In this period (1963-1970) per capita income rose at two percent per annum and the GDP grew at a rate of almost five percent. The latter outpaced the population growth rate at that time of 2.6 percent. Inflation was low and the country was able to maintain an excellent savings rate (averaging 13%)which permitted implementation of an ambitious investment program without undue pressure on domestic prices or the balance of payments. In the public sector, the GOU's budgetary position was sound; i.e., revenue increased faster than recurrent expenditure during the latter half of the 1960's and, together with non-bank domestic borrowing, helped to finance a significant proportion of development outlays.

The engine of growth was agriculture which provided the local and foreign surpluses needed for industrialization and development. The rich soils and good weather in Uganda give it a natural competitive advantage in most types of agriculture. Over 90% of the population derive their income directly from agricultural production which accounts for 75% of total domestic output and 95% of export earnings. Sixty percent of Government revenue is generated from agricultural activity.

After the 1971 Coup the situation quickly deteriorated. Under military rule large numbers of skilled people left the country; the parastatal sector became bloated with the addition of many abandoned or confiscated industries; and public sector professional standards were badly eroded. Lack of investment and maintenance, financial mismanagement, corruption and gross government interferance in the market mechanism characterized the period and contributed to the ongoing decline.

In addition to these largely self-imposed problems, the Ugandan economy was shaken by a series of external shocks; the sharp rise in petroleum prices after 1973, the breakup of the East African Community (EAC) in 1977, and the damage and looting which occured during the 1978-79 Liberation war. Consequently, throughout the decade of the 1970's, the economy declined at an ever increasing pace such that, following the war in 1979, it was on the verge of collapse. (For more detailed background, see Economic Analysis, Annex H.)

2. Uganda Today

Following the liberation war and the installation of the new government under President Obote, severe structural problems persisted; but in the economic policy sphere, the GOU (with IMF assistance) initiated a program of reforms in June 1981 which is addressing many of the most serious economic problems. The objectives of the program are to:

(1) increase prices and other incentives to agricultural producers;

(2) reduce smuggling and speculation;

(3) allow free market forces to operate by removing most price controls;

(4) establish an environment for increased investment and production.

In order to achieve these objectives the following measures were taken:

(1) a 90% devaluation of the Uganda shilling;

(2) four to sixfold increases in the producer prices for coffee, cotton, tea and tobacco;

(3) removal of most government price controls;

(4) rationalization of the tax structure;

(5) substantial increase in the price of petroleum and electricity rates;

(6) monetary and fiscal policy measures that hold down budget deficits, government borrowings and domestic credit expansion, and,

(7) increased interest rates that begin to reflect the real cost of money.

The impact of these new measures over the past four years plus continued policy reforms, including additional producer price increases, an auction system for foreign exchange allocation (Window 2), and the return by the GOU of some of its parastatal holdings to the private sector, have had a market positive impact on the economy. Government deficit financing has been reduced. There has been a noticeable diversion of supplies back into official channels, and the cost for most commodities has tended to fall below the pre-float open market prices. These policy changes are setting the stage for structural and institutional adjustments that should bring economic recovery and sustain development. Other positive signs include:

- five percent GDP growth during 1981 and 1982 which were sustained into 1983;

- 45 percent growth in export volume from 1980 to 1983;

- a nineteen fold increase in government revenue from 1981 to 1983 (0.8% to 6.3% of GDP);

- reduction of inflation from 100% in 1980-81 to 45% in 1982 to 30% in 1983.

The impact of the above measures would probably have been even more positive were it not for continuing internal security problems and the adverse world economic environment relative to Uganda's balance of trade during the period.

Despite this progress, overall levels of economic activity remain substantially below the peak levels attained in the early 1970's. Per capita GNP is still only two thirds of the 1970 level. The burden of this income lost falls most heavily on wage and salary earners, especially in the civil service. These public employees almost universally have to resort to secondary employment or illegal activities or both in order to survive.

A great deal, therefore, remains before the recovery effort can be considered solidified and characterized as a success. Nevertheless it is the USAID's belief that the potential for development, especially in the critical agriculture sector, is extraordinarily high due to the strong existing base in natural and human resources. It is felt that with the right mix of

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credit and technical assistance together with continuing normalization of the security situation, the economy, in the medium term future should be able to reach and probably outpace the level of development achieved in the 1960s.

3. The Agricultural Sector

Already there has been a marked increase in agricultural production and processing. The most dramatic increase are in cotton and coffee production (See Economic Annex.) Nearly all of the added production can be attributed to dramatic increases in producer prices. Although crop processing has continued to be a problem, it has increased substantially as evidenced by much higher processed crop exports. (See Agricultural Sector portion of Economic Analysis). Although there are no hard data on increased commercial sales, many shops in Kampala, Jinja and upcountry towns have reopened and are keeping surprisingly large inventories.

Realizing the key role agriculture must play in recovery, the GOU's near term objective for agricultural rehabilitation is "to restore agricultural productivity and to encourage structural adjustments in the sector that reflect Uganda's comparative advantage." This is being accomplished through the series of policy changes mentioned previously and through the restructuring of agricultural institutions. The national marketing boards, especially coffee and lint, will be reorganized and streamlined to operate on a commercial basis with effective cost controls linked to the volume of produce handled and the marketing services performed. One immediate change, now being implemented, is the divestiture of edible oil and soap factories by the Lint Marketing Board.

Rehabilitation of the cooperative structure is also key to agricultural recovery. At one time, the cooperative system in Uganda, which was considered by many to be the best in Africa, was the structural foundation of the country's highly productive agricultural sector. Uganda's agriculture is based on small holder mixed-farm production with cooperatives providing internal marketing and processing and for the last few years, most input supply. The Recovery Programme recommends a series of crop production and rehabilitation programs, but, in all cases, except for tea and sugar, cooperative support is the central institutional element. All cotton gins, most coffee hullers, and the (soon to be transferred) oil processing facilities are operated by private cooperatives. Finally, cooperatives operate a wide range of other rural enterprises (supply stores, maize mills, furniture manufacturers, piggeries, slaughter houses, etc.) which support or complement agricultural production. Thus, agricultural recovery in both the short and medium term will depend significantly on the rehabilitation of the cooperative services of input supply, crop processing and marketing.

Cooperatives are eligible to borrow under this project and should absorb a significant share of credit offered. The cooperative system is also being assisted by the ongoing Food Production Support project with commodity and technical assistance and will be the subject of a major new Cooperative Development project to be authorized in FY 1985.

4. The Financial Sector

a) Institutions

The country's financial system includes the Bank of Uganda (BOU) which is the central bank, seven commercial banks, two development banks, one post office savings bank, four other credit institutions, and several insurance companies. The Uganda Commercial Bank (UCB), evaluated in Annex J, is by far the largest. The remaining six commercial banks include five foreign-owned and a cooperative bank. The foreign-owned banks are Barclays, Bank of Baroda, the Libyan Arab Uganda Bank, Standard and Grindlays, (Evaluated in the Institutional Analysis, Annex J.)

Over the last decade commercial banking coverage declined sharply in Uganda in line with general economic deterioration, and the relative increase in subsistence activities. In 1970 Uganda had 290 bank branches. The current estimate is 110 branches, or one for every 116,000 people.

The two development banks include the Uganda Development Bank (UDB), (evaluated in Annex J.) and the East African Development Bank, owned jointly by Kenya, Tanzania and Uganda. A third institution - the Development Finance Company of Uganda (DFCU) - ceased operations in the mid-seventies and is yet to be reactivated.

The four credit institutions operate mainly in the areas of mortgage financing and consumer credit, but also carry out some of the functions of a commercial bank. Finally, the numerous insurance firms also include a wholly Government owned company.

b) Resource Mobilization and Credit Allocation

The seven commercial banks account for most of the resources mobilized and allocated through the country's financial

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system. Time and savings deposits mobilized by these banks increased from Uganda Shs. 562 million in December 1970 to Uganda Shs. 4,494 million ten years later. There has been no growth in savings in real terms, however, the increase actually reflecting the decline in the value of domestic currency along with GDP in general. It may also reflect significantly negative real interest rates in the latter part of the decade, discussed below and the disincentive effect of limited lending options on the willingness of the banks to mobilize savings.

Compared to savings mobilization, growth in domestic credit was more rapid over the same period, increasing from UShs. 1.5 billion in December 1970 to 21.5 billion 10 years later. This resulted primarily from increased GOU borrowing, particularly advances from the BOU, to finance its budget deficits. Claims of the GOU, accounting for only 39% of total credit in 1970, had reached 77% ten years later. The corresponding shrinkage in credit available to the private sector also reflected the effect of the general economic decline on private sector demand. In fact, before the introduction of the financial stabilization measures in June 1981, private demand for credit from the banking system was very small, and a number of banks were consequently refusing time deposits. These measures, negotiated with the IMF, included a limit on domestic credit and the relative share allocated to the GOU.

Since 1977 the BOU has pursued a policy of specifying ceilings for sectoral commercial credit allocations which are adjusted periodically. As a result of the IMF/GOU agreement, current ceilings (fixed in June 1981) include 30% each for agriculture and manufacturing, 15% for trade and commerce, 8.5% for construction, 5% for mining and 1.5% for local and urban authorities. At present, however, agriculture continues to absorb approximately 42% of commercial bank advances, mainly for seasonal cash and export crop marketing and input requirements.

Domestic credit availability does not appear to be a constraint relative to short term agricultural production and marketing operations, but is relative to longer term investment requirements, mainly due to creditworthiness problems such as outstanding debts, ownership disputes and lack of established feasibility. The lack of foreign exchange financing for investment in agricultural sector enterprises outside of the major cash export crops (toward which this project is directed) is a more serious problem. Commercial banks suffer from a continuing liquidity problem as so much money remains outside of the banking system altogether to support private trading activity. (See Financial Analysis, Annex I.)

c) Interest Rates

Current interest rate ceilings, set in October 1981 by agreement with the IMF, range from 8 to 12% for deposits and from 13 to 22% for lending. (The agricultural rate now stands at 17%.) Such rates are still negative in the Ugandan setting and do not limit demand. Inflation is currently running about 30% and dropping very slowly. Prices are stabilizing, however, and in the case of food, have actually declined by as much as 25% - reflecting increased production but low purchasing power of domestic consumers. This project will lend at the maximum legal rate possible to sub-borrowers in order to provide as much of a margin as possible in pursuit of viabile credit operations. Given the risk and cost associated with agricultural investment financing in Uganda, the rates should be much higher and currently act as a disincentive on the supply side. In order to seriously involve commercial banks in project associated lending, the widest possible margin will have to be offered.

d) Fiscal Policy

Fiscal policy reforms by the present government have brought about a dramatic reduction in domestic inflation over the past four years, i.e., from the 100 percent level in 1980-81 to 30% in 1983 as discussed above. The Government devalued in 1981 increasing the official rate from UShs. 7.3 to the dollar to 77.8. This was followed by further devaluations and the establishment of a second window where foreign exchange for the commercial sector could be obtained through weekly auctions. Market demand in large part now determines the rate for Window II, while Window I is still used for the purchase of essential commodities (e.g., oil and medical supplies). During the past year, exchange rates for Window I and II have moved closer together and the Government expects the two to eventually combine into a single system. There is still an unofficial street rate for foreign exchange at a fluctuating level somewhat higher than Window II (normally about 25%) reflecting a continuing gap through official channels, but the situation is not as severe as it is in many African countries where highly distorted rates are maintained through arbitrary controls. In this area, Uganda is one of the star performers amongst its neighbors.

5) The Public Sector

Public administration continues to be weak. The civil service is often described as inefficient, overstaffed and underpaid.

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External donors are encouraging the Government to concentrate financial resources on essential ministries, and postpone filling vacancies. The GOU is also increasing its reliance on market forces to guide allocation of resources for productive purposes, and the economy is responding. In 1983 the GOU passed the Expropriated Properties Act, setting up a mechanism to resolve ownership disputes of properties taken over by the former military government. Much of this property is still in the hands of parastatal institutions, however, which are experiencing serious problems with mismanagement and inadequate financial controls. Divestiture is being seriously contemplated for part of the parastatal sector, but it is a slow process.

There remain other areas where further changes in Government policy would improve the business environment. International donor agencies, and specifically the IMF, IBRD, and AID continue to encourage Government to abolish ex-factory price controls and exorbitant excise taxes on locally produced goods and to continue to review and adjust farm-gate prices for export crops. In this area, the USAID has made the case to the GOU relative to how present policy favors the importation of edible oil despite the comparative advantage of domestic production. Local retail prices could fall by 50%, for example, if local production could be encouraged by reducing the current sales tax on the ex-factory price of oil from the current level of 70% to 15%. Increased production resulting from such a move would result in considerable foreign exchange savings and increased employment from the rehabilitation of the oil industry. The Project is anticipated to lend in this area, if and when the issue is resolved.

6. Other Donor Activities

The GOU is determined not to recreate the economic situation that it inherited, in which an unsupportable burden of high-cost short-term debt had been acquired. As a result, Uganda's ability to attain the targets of its planned "Recovery Programme" is critically dependent on the level of concessionary assistance provided by the international community. The country, shows promise that such assistance can be effectively utilized over the medium term future, and its ability to absorb appears to be steadily increasing.

The new commitments of external financing required to implement the Revised Recovery Programme on schedule are summarized in Table I below. Commitment levels, including gap financing, are required to increase by 7 percent during 1984 and then to continue rising by about 4 percent per annum (below the projected rate of international inflation) over the remainder

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of the decade. Within the total, debt relief and private loans are expected to fall sharply in 1984, reflecting the reduction in current debt obligations and the unusually high level of supplier's credits committed in 1983. Other commitments of external assistance, therefore, are required to increase by 47 percent during 1984. Whether or not this can be achieved, at a time when many donors are tightening aid budgets, remains to be seen. Uganda's case for additional support is strong, however, based on its recent policy reform record and the obvious need for foreign exchange to rehabilitate its economy.

TABLE 1: COMMITMENT REQUIREMENTS[a/]
(in U.S.$ million at current prices)

	Average 1979-82	1983	1984	1985	1990
External Assistance[b/]	247	272	330	342	467
Multilateral	171	157	199	199	271
Bilateral	76	115	131	143	196
-DAC	(55)	(90)	(96)	(105)	(144)
-Other	(21)	(25)	(35)	(38)	(52)
Gap Financing[c/]	-	-	70	70	30
Other commitments	125	129	30	32	44
War related loans	43	-	-	-	-
Debt relief	61	79	15	16	22
Private loans	21	50	15	16	22
Total	372	401	430	444	541

a/ Excluding short-term loans
b/ Includes loans and grants
c/ Assumes that fast-disbursing assistance accounts for 80 percent of gap financing in 1984-85 and then falls to 50 percent by 1190. Fast-disbursing assistance is assumed to disburse 50 percent in year of commitment and 50 percent in subsequent year. The balance of gap financing is assumed to disburse 10 percent in year of commitment and 30 percent in each of the subsequent three years.

Source: World Bank, Uganda, Country Economic Memorandum, December 9, 1983

Even with the above commitment levels, net disbursements of loans and grants are still projected to fall in per capital real terms over the next seven years from their present level of U.S.$15 (compared, for example, to 1981 estimates of U.S.$27 in Kenya and U.S.$36 in Tanzania).

Other donor assistance specifically relevant to this project is described in more detail in the Institutional and Financial Analyses. In essence, assistance is concentrated in industrial rehabilitation and development through credits to the UDB which now has some $106 million ($30 from IDA) committed in this area, enough to saturate its absorptive capacity in the sector for the coming five to six years. Complementing these resources is what shows promise of being a highly effective package of long term technical assistance from the UNDP working in partnership with the IBRD, consisting six high quality expatriates functioning in line positions, including the assisting general managers for operations and finance.

Commitments on the agricultural side include an old line of credit from the Kuwait Fund destined for large scale ranching activity which the UDB is administering and which may be channeled to the Parastatal Livestock Development Agency. Another 70 million from the IBRD is directed to cash crop production and marketing through the 54 branches of the Uganda Commercial Bank in addition to $5 million specifically for industrial rehabilitation.

In summary, RPE project funds will be the only resources specifically available for "investment" (ie., actual improvements as opposed to maintenance/working seasonal requirements) in general agricultural enterprise of a non-specific cash export crop nature for either production or processing or both. Further and more important, RPE is principally directed toward the creation and development of absorptive capacity, the lack of which is the most serious gap of all at present. See Rationale section below.

B. Project Rationale

Given the above setting the rationale for this project in particular can be summarized as follows:

1. The Problem and Associated Constraints

The most serious problem facing Uganda today is severely debiliated productive capacity - across the board - capacity to meet its own consumption requirements and for export to generate urgently needed foreign exchange. Constraints associated with this generalized problem include:

a) Lack of investment capital given the past and current environments and associated risks; a continuing liquidity problem persists in financial systems as so much trade is carried on outside of official channels.

b) lack of sound delivery vehicles for credit and associated services; lending institions, especially in the public sector, are still reeling from the Amin years.

c) the lack of administrative and technical absorptive capacity of the producer group; the Asian entrepreneurial class was driven out under the Amin government and is only now beginning to dribble back in. During that period indigeneous Ugandans, lacking such skills, were thrust into management roles they were ill prepared for.

d) debilitated basic infrastructure, especially in the area of transportation;

e) continuing policy constraints in the areas of taxation, public sector enterprises and a still bloated bureaucracy and lingering price and exchange controls;

f) a persistent problem of corruption arising from the survival mentality fomented during the disastrous decade of the 1970s and;

g) a continuing security problem (See Issues above)

2. Resources

Against the above constraints should be weighed the following resources:

a) Natural resources in abundance especially for agricultural production in terms of land, soil and climate. Inexpensive hydro-electric energy from existing sources is also a vital resource for production in all sectors;

b) Human resources available at all levels. The population of Uganda includes an out of date but highly educated professional group in both the public and private sectors. At lower levels, farmers and workers are capable and trainable. Management skills are still lacking in a generalized sense, but the raw material is in place;

c) A comparative advantage in both agricultural and industrial production given the above factors. At the end of the 1960s Uganda stood head and shoulders above the rest of East Africa in these areas and could arrive there again given the required rehabilitation of previously existing productive capacity.

d) A basically positive policy framework for free market private enterprise development, despite the above constraints, relative to the rest of Africa.

e) Solid external donor support, spurred by the policy and natural environments. The donor community appears to be anxious to support a potential model. Uganda could "point the way."

f) Availability of concessional capital for rehabilitation of industry and commerce and to a lessor degree for agriculture.

2. The Gaps

The principal gap is clearly in the area of absorptive capacity for capital investment at all levels - lending, borrowing, managing, planning, analyzing, controlling etc., in sum, creditworthiness. The capital is either already there or waiting in wings. It is felt, on the basis of experience thus far, therefore, that if Uganda could only develop this capacity, given the other positive factors it has going for it, capital could be forthcoming in abundance from both donor and commercial sources.

4. Conclusion

In the USAID's analysis, the most critical need is to address the gap head on, i.e., attempt to deal directly with the absorptive capacity question. As it is already being addressed in industry, thanks to the IBRD and other donors, and within the agricultural sector in terms of basic production and marketing for the principal traditional export crops, coffee, cotton, tea etc. by other donors. What remains, essentially, is the capacity to productively utilize resources for private enterprise development throughout the sector.

To this end the project is directed, i.e., absorptive capacity of both the delivery system and the enterprise, with an emphasis on the latter. This, therefore, is an institution and system building project. The main effort is of a technical assistance and training nature. Regarding the capital inputs programmed in the project, although they will provide for a significant number of profitable and badly needed investments, they are even more critically needed for leverage and pump priming. Over its live the project should result in substantial mobilization of other capital resources which should mean that AID will be able to phase out of the investment area altogether in the future and focus on other critical needs.

C Relationship to Country Development Strategy Statement

As was correctly observed in the recent AID/Washington review of the Uganda CDSS update, The overall program is beginning to move toward a more traditional, institutional and system building approach, as opposed to the early emphasis on fast disbursing assistance for rehabilitation. This is particularly the case of this project.

As originally conceived, RPE was to be rapid disbursing. At that time, however, the factors limiting such an approach were not truly understood in the Ugandan context. What has been found in the design experience is that, despite the exciting potential in the country for accelerated development on the basis of existing natural and human resources, it is not so easy as originally contemplated. Systems and institutions existing in the 1960s were systematically gutted, or totally reconstituted in a different image. They are gradually rebuilding, but it is a long road.

An intelligent, relatively well educated and energetic people remain, but the 1970s took an enormous toll on the national psyche from which the country is only just beginning to recover. The level of distrust is high. A survival mentality persists. The normal performance incentives don't have the same impact as in other settings which have not been through such a trauma. Development objectives cannot be expected to receive the highest priority in a situation where for a high percentage of the population what is most important is to get from one day to the next and achieve a modicum of personal and economic security.

In terms of management, probably the most critical factor in the development of any economy, as mentioned in the last section, a very high percentage of the managers were driven out during the Amin years and are only now beginning to return. In the meantime, institutions and enterprises have failed or otherwise become moribund. Despite the undeniably high professinal level of many Makerere and foreign university trained Ugandans, there remains a severe management gap at middle and upper levels. The EHR cross-sectoral assessment proposed for later this year should give the USAID a much better understanding of this constraint.

In the meantime, it has been found through investigation and analysis that a project such as this just won't move rapidly. It will move at a pace commensurate with the environment, and this means a taxing, long term system building effort. Of the some 200 potential sub-projects reviewed as part of the design effort for this project, for example, not one was ready to finance, even if the funding had been there. Although better than half represented potentially viable investments, all required further analysis to determine feasibility and fundability. Targets of opportunity are out there in substantial numbers, but they will need time and technical assistance, not just capital, to get off the ground.

As mentined above, the real need for the capital component of this project is for pump priming and leverage to get the system going and to mobilize other resources. In a very real sense, this is risk capital, and should be looked upon as such, although every effort will be made to conserve it and make it grow.

Finally, the project is very much in line with Agency policy in terms of its private enterprise focus. The target group is one hundred percent private enterprise and this will be maintained through rigorous application of eligibility criteria. The fact that we are working with public sector institutions, in part, to reach intended beneficiaries, reflects a Ugandan reality for the timebeing. The alternatives chosen in terms of executing agencies are the only ones willing and capable of taking on the challenge the project presents. Eventually, however, it is expected, and will be encouraged, that resource management will gradually shift toward private intermediaries. The pace of this shift will depend entirely on the ability of this group to respond effectively to the opportunities presented by the project within the context of existing constraints. There is no pre-determined level allocated to public and private sector lenders, although illustrative levels have been established for purposes of analysis. Performance will be what counts and what brings reward in the form of profitable, expanded operations.

PART III THE PROJECT - DETAILED DESCRIPTION

A. Overview

The project is designed to address the principal gap identified in the problem analysis, i.e., the lack of absorptive capacity of both borrowers and lenders for productive investment in agricultural enterprise. This will be accomplished through provision of; a) technical assistance and training for improved managerial and technical capacity of both groups and b) start-up lending capital for priming of the systems to be strengthened and to enhance experience and capability necessary for self-sustained development in the future. In the long term, once sufficient creditworthiness is established (the key at both levels), other sources of capital should become accessible as has been demonstrated time and again in other settings.

The structure of the project (Figure 1) is built around the notion of separate but coordinated and mutually reinforcing packages aimed at the two key levels, credit intermediary and borrowing enterprise. Overall management and coordinating responsibility for the project will be officially lodged with the USAID's counterpart in the Bank of Uganda, the Director of the Development Finance Department. As a practical matter, however, the effort will be orchestrated and directed primarily through the U.S. contractor in collaboration with management of the lead Intermediate Credit Institution (ICI), the Uganda Development Bank. The project will also be carried out in a collaborative style with a World Bank/UNDP team, currently working with the lead ICI in critical line positions to strengthen industrial lending and overall management of the institution and its operating procedures. Beyond the sectoral difference between the World Bank and AID packages, in relative terms, the IBRD/UNDP group will focus more on lending operations while the AID effort will emphasize project development, appraisal and strengthening of the recipient enterprise.

One unique aspect of the above structure should be highlighted at this point in order to have an appreciation for the strategy behind the design of this project. This is the institutional separation of technical inputs for borrowers and the principal lender. As illustrated in Figure 1. sub-borrower assistance will be through the vehicle of a separate technical assistance (TA) entity, to eventually become totally independent, which will have no institutional relationship with the lender group. The rationale for this is two-fold. First, this allows the

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ICIs to focus on objective appraisal and financing rather than project development, not a traditional or natural banking function. Secondly, it provides a palatable and effective means of costing and charging for development services rendered which logically should not be part of the administrative cost of lending[1/]. In the long run, the TA entity should be able to sustain itself through user fees as the market for its services increases. It is also expected that the entity will eventually become the beneficiary of Ugandan investment capital, provided that it becomes independent as planned in the fifth year of the project. (See detailed description below).

B. The Approach and Project Phasing.

The approach for implementation of this project is a variation of phased and evolutionary ("rolling design") models with which AID has been experimenting for a number of years now. The idea behind the phasing, of course, is to provide a viable mechanism for mid-course corrections and design adjustments to respond to emerging factors and conditions which cannot be adequately predicted or analyzed at the outset. This is definitely the situation with this project, as it is with the development setting of Uganda at this time and for the foreseeable future.

Essentially, the first phase will allow for a period of systems development, limited lending, and the acquisition of the necessary experience and analytical foundation to proceed with confidence into a longer range development effort commencing in Phase II. Project phases, including a pre-implementation period, are projected as follows:

1. Pre-Implementation: June 1984 - December 1985: During this period, critical planning, preparation, and gearing-up activities will take place including; contractor recruitment and mobilization, the meeting of conditions precedent for disbursement, preparation of detailed work and procurement plans, etc. (See Implementation Plan.)

1/ Historically in AID and other donor financed ICI projects the approach has normally been to incorporate project development and lending assistance within the same institution, often within the same division. It has seldom worked. It is not cost effective and results in competing priorities. Promotion, design and development have a tendency to distort the appraisal function, and vice versa, when performed by the same unit or organization.

FIGURE I

PROJECT STRUCTURE

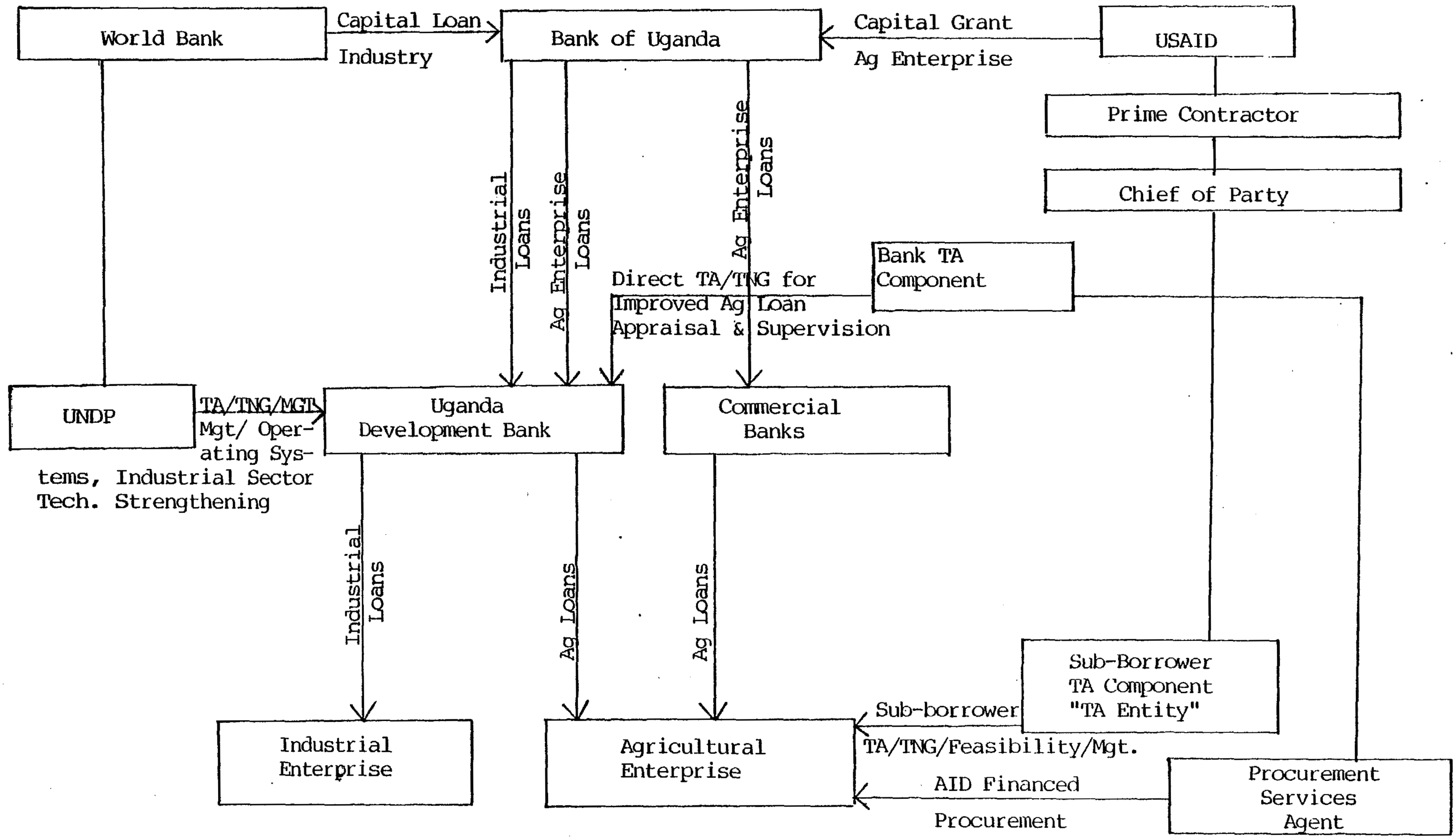

FIGURE 2

TECHNICAL ASSISTANCE STRUCTURE

Prime Contractor

Bank of Uganda Counterpart

Uganda Dev. Bank Counterpart

Chief of Party
Overall management, planning, monitoring, coordination, data management/analysis, etc.

USAID
Counterpart

Note: Independent auditing contract not shown here.

Institutional Strengthening Component

TA to Uganda Dev. Bank and possibly to Commercial Banks.

1 Long-term advisor

Various short-term advisors

In-country and participant training.

→ UDB
Commercial Banks

Sub-borrower Strengthening Component

Technical Assistance Entity (Semi-independent status)

To function as a business advisory service to target clientele.

Feasibility and management assistance.

3 Long-term advisors (Accounting, business/finance, agro-industry)

Various short-term advisors

→ Sub-borrowing
Ag Enterprise

Procurement Services Agent

All procurement financed by USAID.

US Agent with Ugandan/Kenyan affiliate.

→ Services to
Sub-borrower

2. Phase I: January 1986 - December 1988: This will be dedicated primarily to process, system, and institutional development and will receive the heaviest injection of technical assistance. The technical assistance entity will be developed during this phase and hopefully "spun off" as a viable enterprise in its own right by the end of the three year period. A number of studies, described below, will be carried out to provide the basis for evaluation of Phase I and detailed planning of Phase II. With respect to lending, the project will cover as complete a range as possible of possible project types (rehabilitation and/or expansion of existing enterprise and the creation of new ventures) in order to allow valid analytical determinations to be made with respect to areas of high and low payoff and where scarce concessional resources should be concentrated in Phase II.

3. Phase II - January 1989 - December 1991: During this period, lending to the target sector is expected to move into much gear on the basis of systems developed, experience gained, additional resources mobilized, and internal capitalization of intermediaries. External technical assistance and training activity will phase down and out prior to project termination, but the TA entity is to continue under Ugandan ownership and management with a staff of project trained personnel.

With respect to the implications of the above approach relative to authorization, full authorization is recommended now for life of project funding as; a) sufficient analysis and planning has taken place to allow for the timely and effective management of funds for technical assistance and training through Phase I; b) prior to the completion of Phase I, detailed plans and cost estimates will be developed and approved by AID for technical assistance and training activities projected for Phase II; and c) with respect to the credit component, criteria have been developed for ICI, sub-project, and sub-borrower eligibility to assure adequate compliance with AID policy, program and project criteria which will be further refined and negotiated (see Conditions and Covenants) during the pre-implementation period and again prior to the commencement of Phase II. Concerning obligations, however, these will be tranched in such a way that funding for Phase II will be contingent upon AID and GOU approval of detailed planning based on analyses and the evaluation to be carried out in the last year of Phase I.

Note; No actual lending is expected to take place under the project until the U.S. Contractor is on board and has been able to provide the necessary feasibility, planning and costing assistance for sub-project development as an ongoing activity. (The USAID may elect, however, to attempt to facilitate a select few, early priority sub-loans, but these would have to be evaluated independently by the Mission, probably with REDSO assistance, and other conditions and covenants would have to be met in terms of ICI agreements, criteria, etc. (See Conditions and Covenants.)

C. Goal Structure of Project.

1. Program Level Goal:

The program goal of the USAID strategy in the agricultural sector of Uganda is to provide a package of assistance interventions which will lead to rehabilitation, recovery and development of private (including cooperative) enterprise within the Agricultural sector resulting in improved income, employment and quality of life in general. As explained under the project rationale, the most significant constraint to pursuit of this objective for the foreseeable future appears to be the lack of medium to long term investment capital. The project as a whole, therefore, is directed toward the resolution of this limiting factor.

2. Project Goal

The goal of the project is to make available medium to long term financing for investment in high potential agricultural enterprise. The lending resources to be directly provided by the project do not come close to meeting valid investment needs in the sector. The objective, however, is to set up the distribution system and "prime the pump" so that resources can be effectively mobilized and absorbed downstream from other quarters. In this manner, AID funding will be utilized as leverage for capitalization and to lay the organizational and systemic groundwork for self-sustaining development to occur.

3. Project Purpose

The project purpose is to develop viable, self-sustaining systems, for the effective absorption of investment credit by agricultural enterprise. This is an institution and system building project - focussed on both borrowing enterprises and lenders - with an emphasis on the former. Although for purposes of programming criteria and requirements, it can be classified as an ICI project, it is really much more in the sense that it will work with all entities, at either the borrower or lender ends of the system, that qualify under basic criteria to assure that project objectives are effectively pursued. In essence, it is to improve absorptive capacity and managerial capability for the effective exploitation of both externally mobilized and locally available resources.

4. Conditions Expected at the End of the Project

The following conditions are defined in terms of the principal characteristics of the system that the project will strengthen or develop. Also included are qualitative objectives for resource mobilization and analytical elements of the project which will contribute in significant measure to realization of the self-sustaining aspect of the system as a whole. Relatively firm targets are established for Phase I, while those for Phase II must remain necessarily tentative until analytical exercises programmed for the last year of Phase I have been completed.

a) System Super-structure and Capitalization

The project aims to establish a viable, two tiered credit system for agricultural investment in terms of lending, ongoing capitalization and expansion. By the commencement of Phase I, the structure should be established although lending will not have commenced in any significant degree.

Phase I: By the end of Phase I, the system should be operating smoothly in terms of lending at both BOU and ICI levels, although only very modest capitalization or reflow activity will have taken place due to the grace periods built into both credits at both levels. Additional resource mobilization should be taking place on the basis of track records established.

Phase II: By the end of the project, substantial other donor resources for agricultural investment should also have been mobilized and disbursed through the systems established by the project. Expanded operations should be meeting demand accross the board. (See Financial and Economic Analyses.)

b) ICI Capability and Effective Participation.

The objective is to arrive at a set of lending institutions and programs capable of satisfying the need across the board for

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Investment financing in the agricultural enterprise sector. While as a matter of policy, the project has a bias toward private sector lenders, the project will work with any intermediary prepared to comply with established ICI and sub-project eligibility criteria (See Section 4 below.) The selection of the UDB as the lead ICI and the institution to receive the bulk of the lending resources under the project results more by default than intent, as it is the only public sector lender at this point that is; a) both willing and potentially qualified to serve in the capacity envisioned and b) responsive to the project's target clientel. Further, the opportunity for effective donor coordination to achieve project objectives is uniquely present in the UDB thanks to major capital and technical inputs in place from the combined World Bank (IDA) UNDP project which has compatible institutional objectives and an approach sympathetic to AID's. (See technical analyses) As the project progress, other lenders are expected to be incorporated.

<u>Phase I</u>: UDB and Grindlay's Bank effectively lending to all contemplated types of agricultural enterprise. Other banks will have experimented with some loans financed by the project on a pilot basis, i.e. Barclay's, Standard, and the Uganda Commercial Bank.

<u>Phase II</u>: Four or more major banks effectively lending for agricultural enterprise investment on a country-wide basis. An effective outreach capability will have been developed through branch operations or mobil units.

Note: In terms of the base line for the above objectives, at the time of final design, there was no institutional lending taking place in the agricultural sector with the exception of limited production credit for seasonal inputs and crop purchase through commercial banks.

c) <u>Volume of Lending</u>

<u>Phase I</u>: Cumulative total of Project Credit Extended will be at least \$6.0 million.

Annual Lending levels in the final year of Phase I will be \$3.0 million.

<u>Phase II</u>: Total of project credits extended: \$13.9 million.

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d) Viability/Efficiency of Lending

Phase I: Cost of lending to agricultural enterprise for capital received on concessional terms (AID Financed) will be established at a sustainable level within margins received.

Phase II: Cost of lending for capital received on both concessional and commercial basis will be reduced to what can be covered effectively by the spread. ICIs will be undergoing sustained expansion on basis of earnings from lending operations.

e) Resource Mobilization and Capitalization

Phase I: By the end of Phase I a track record will have been established plus demonstrated absorptive capacity of both borrowers and lenders such that additional major donor resources will be directed to the sector of on the order of $ 5 million per year projected for the commencement of Phase II.

Phase II: By the end of Phase II the needs of the assisted sector will be totally met from a combination of concessional and commercial sources of credit plus savings or retained earnings within the target community of enterprises and lenders (estimated to be on the order of $ 8 to 10 million per year by the end of the project).

f) Sub-borrower Strengthening and Enterprises Launched

Phase I: During Phase I the intention is to finance and assist at least one of each type of project contemplated at present in order to have a comprehensive basis for evaluation and planning for Phase II. Further, a core group of successful ongoing projects will have been established to serve as examples for replication and from which to draw experience and data. A total of at least 40 projects will have been financed of which about 50% should have completed the investment and be successfully operating.

Phase II: By the completion of the second year of Phase II, all project funds will have been drawndown and invested in viable projects in the target sector. By the end of the project, all project financed investments will have been completed. Of these a substantial number should represent additional investment opportunities for internal or other commercial sources of capital. Enterprise management within the sector will have been substantially improved.

g) The Technical Assistance Entity

From the beginning, the TA Entity will charge for services rendered to borrowers. Where necessary, costs of such assistance will be loan financed, initially at a subsidized level. The idea is to direct payments received to underwrite the growth and strengthening of the Uganda side of the operation and to develop the requisite skills to carry on with the same assistance on a commercially viable basis once the U.S. contractor pulls out. (See Section II,D,3 below for further detail.)

Phase I: By the end of Phase I the TA entity will be able to cover all local currency operating costs through fees received from sub-borrowers under the project. There will also be a core staff of five trained Ugandan professionals working full time in the areas of financial, socio-economic, and technical feasibility analysis.

Phase II: By the end of the project, the unit will be completely on its own as a viable firm or indigenous PVO dedicated to agricultural enterprise management and technical consulting available for the general public and for use by the donor community.

h) Lessons learned and analytical foundation developed for Expansion and Replication

Phase I: By a point in the middle of the last year of Phase I, the analytical foundation will have been developed for major other donor resource mobilization, and detailed planning for Phase II expansion of investment activity will have been completed.

Phase II: By the end of the project a fully documented analytical history together with a comprehensive final evaluation will have provided the basis for replication of successful elements of the project in other comparable countries of Africa in addition to serving as an invaluable instrument for public and private sector investment planning and resource mobilization upon termination of AID and other donor assistance to the target sector.

5. Purpose Level Assumptions

a) The project will receive strong policy level support from the GOU (Bank of Uganda, Ministries of Finance, Agriculture, and Cooperatives, and the Oversight Committee to be established.) There is reason to believe this will be the case due to reform measures implemented over the past three years.

b) Private banks will participate as anticipated in the project due to attractive lending margins offered. Grindlay's will be the first. Others should become involved once they observe successful participation by Grindlay's.

c) The IBRD/UNDP effort to improve operating systems at the UDB will be successful. The technical assistance team is very strong and operating in line positions. The Assistant General Manager is especially outstanding. (See UDB Institutional Analysis).

d) Target enterprises will be willing to borrow for technical services received.

e) The security situation in Uganda will gradually improve.

D. Detailed Activity Descriptions

The project is divided into five components corresponding to objectives related to; a) institution and system building, b) financing, and c) data collection, analysis, evaluation and planning. It should be borne in mind that implementation of these activities, for all intents and purposes, will commence in earnest at the beginning of Phase I in January 1986 as the first eighteen months of the project will be dedicated mainly to start up activities and detailed planning. The prime U.S. Contract is expected to be signed by the the end of June 1985, but a period of approximately six months of orientation, analysis, planning and mobilization is expected prior to commencement of serious project interventions. (See Administrative Arrangements and Implementation Plan.)

It should also be noted here that the U.S. Contractor will be responsible to a greater or lesser extent for all five components simultaneously, with different units and/or personnel (possibly sub-contracts or joint ventures) dedicated to different elements. The point is to have unified management to assure the complementarity and effective coordination of activity at all times. (See U.S. Contractor Section of Administrative Arrangements, PART V.)

1. Overall System Development and Capitalization

a) Outputs:

By the commencement of Phase I, all arrangements will have been made and agreements finalized for BOU lending to the Uganda Development Bank and Grindlay's. Agreements with other commercial banks are not expected until a year or more into Phase I, although they could come earlier. A proposed guarantee scheme for commercial lending to the agricultural sector will also be operational, and special accounts will have been established in the BOU for project associated disbursements and reflows. The system will be ready to commence project operations. Sub-project lending is expected to commence within six months of the commencement of Phase I by both the UDB and Grindlay's.

By the end of Phase I, the reflow account in the Bank of Uganda for the foreign exchange component of the lending activity will have accumulated to approximately $600,000 in local currency from interest payments. (Principal payments to the BOU are not programmed to start until the 11th year.) By the end of Phase II the balance of the account will have arrived at $2,900,000 with total outstanding loans amounting to approximately $13,900,000. In addition, over the life of the project, some $11.5 million in local currency will have been mobilized and invested from the local currency components of loans and equity contributions from sub-borrowers. Thus, the more important output will be achieved of capitalization of an ongoing source of lending capital for agricultural enterprise. This, when complemented by other donor assistance expected in Phase II and beyond capitalization at ICI and sub-borrower levels, should

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effectively meet demand for the indefinite future. Approximately 120 sub-projects are expected to be financed over the LOP. (See description of Financing Component, Section 4, below.)

b) Implementation

The official responsibility for achievement of pre-implementation phase targets will rest with the Bank of Uganda through its project manager, the Director of Development Finance. There will also be a high level GOU oversight committee. (See PART V.) There will be a need, however, for substantial USAID follow-up and assistance with most of the administrative and financial arrangements and other submissions required as conditions precedent. The USAID project manager will be responsible for this and will be assisted by one or more short term contractors (outside of the prime US contract) with respect to development, review, and approval of various required submissions. Approximately one year into the start-up phase, the U.S. Contractor will be available to assist with final administrative and financial arrangements through advance (pre-mobilization) consulting assistance.

With respect to main line implementation during Phase I, the Chief of Party (COP) of the prime contract will be responsible for overall management and coordination of project activities and will be responsible to his counterpart manager at the USAID. He will also relate directly to the Ugandan project manager in the BOU as well as to management personnel at the ICI level. As much authority as possible will be vested in the COP within legal and responsible limits in order to reduce the management burden of the USAID.

c) Inputs:

Inputs for this component, in advance of Phase I, will be limited to short term consulting assistance of no more than six months through personal services contracts with the USAID. Additional advance work carried out by the U.S. Contractor should come to no more than six person months. The intention is to achieve contractor mobilization to Uganda as early as possible after contract signing, now projected for June 1985.

2. ICI Strengthening and Capitalization

a) Outputs

(1) The UDB

Almost all technical assistance and training for ICIs under the project will be directed to the UDB through which 65% of project funds are expected to be channeled. Other ICIs may be provided with modest levels of short term assistance in the process of getting them involved with the project, and they will probably participate to a degree in some in-country training activity. At the present stage of project planning, however, there is no basis for describing institutional outputs outside of those targeted for the UDB. These are as follows:

- By the end of Phase I a consolidated (crops and livestock) agricultural division will be functioning as an effective integrated unit capable of adequately appraising almost all types of agricultural enterprise proposals anticipated in the Ugandan setting. As considerable agricultural technical expertise is already in place in the division, (including crop and livestock production and farm management), the basic technical ingredients to be added will be in the areas of financial and economic analysis plus planning for supervision and monitoring of sub-loans. Direct long term technical assistance to the UDB should be possible to conclude by the end of Phase I.

- By the end of Phase I sound loan processing and credit management procedures will have been fully developed, tested, revised, and formalized as part of official bank policy for the long term. In this area, the project will have to coordinate carefully with IDA and UNDP efforts to improve these functions throughout the bank.

- In terms of volume, the agricultural division will be capable of processing all applications in a timely period after receipt, i.e., two to four weeks, at an anticipated level of approximately eight per month by the end of Phase I.

- The quality of appraisal and supervision will be such by the end of Phase I that outstanding delinquent balances on loans processed by the Division will be held to less than 5% of the portfolio balance. (Does not apply to the UDB portfolio as a whole or to prior agricultural lending.)

- By the end of Phase I, the efficiency of UDB lending in average cost per loan will drop significantly and further yet during Phase II. Calculation of these targets will await detailed planning and analysis by the Contractor.

(2) Other ICIs

Grindlay's Bank should be participating actively in the project with a portfolio of outstanding loans to be target group of approximately $1,200,000. One or two other commercial banks will have experimented with project lending on a pilot basis by this time. By the end of Phase II there should be at least three commercial banks heavily involved in agricultural enterprise lending, both with project and other resources.

b) Implementation

A major condition precedent to disbursement under the project will be the consolidation of the existing crops and livestock departments of the bank into a single agricultural projects department. This will result in an office with a combined staff of about 20 technicians consisting primarily of production and farm management specialists. The reorganization is necessary for purposes of operational efficiency and because many of the projects to be appraised are of a mixed farming nature or otherwise overlap into desciplines represented in both departments. At present, the two are essentially moribund, lacking both access to project funding and the capability to adequately appraise the existing backlog of inadequate proposals, many of which could be suitable for RPE funding if the necessary feasibility and planning work could be carried out. (See Institutional and Economic Analyses.)

As early as possible after the signing of the U.S. Contract a short term development banking advisor with agricultural enterprise lending experience will be brought in to assist with the reorganization. The primary task will be to develop a rational structure in terms of the analytical and processing functions to be carried out, produce and secure bank approval of position descriptions, and develop and negotiate changes in personnel to bring skills into line with requirements of the project and the target sector, i.e., a focus on investment and agro-industry as opposed to straight production (especially seasonal production) implying a need for additional agricultural economics, marketing and processing expertise. This is expected to take up to three months.

For the long term, an agricultural finance advisor will be assigned to the division as early as possible under the U.S.

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Contract. The Advisor, working as counterpart to the Division Chief, will carry out a three year program of developing and upgrading appraisal capability within the Division in terms of economic and financial analysis, planning, funding, and monitoring and supervision requirements. The advisor will also work in collaboration with UNDP and World Bank advisors and other sections and officers of the bank (management, finance, accounting, supervision, etc.) in order to properly dovetale the functions of the Agricultural Department with other operating systems of the institution - both existing and in development. In the development of the new proposed Supervision and Monitoring Department for example, personnel are being drawn from the existing Crops and Livestock Departments, and project plans in the future will have to incorporate adequate follow-up measures to assure timely and effective implementation and repayment.

Another responsibility of the advisor critical to the project will be to assure rigorous application of both Bank and AID required sub-project eligibility criteria. The criteria will undoubtedly have to be adjusted over time in light of experience, but the advisor will be charged with making sure that AID program and policy criteria are properly addressed in the appraisal function. The same is true with respect to criteria related to project objectives, i.e., labor intensivity, import substitution etc. (See Section 4. below for more detail on criteria.)

The advisor will also be responsible (in collaboration with the UNDP team) for assessing additional short term technical consulting and training requirements for the Department and related activities in the Bank. Depending on the mix of projects to be addressed, there will be a need to bring in specialists from time to time to assist with particular specialized project appraisal needs and to produce guides, manuals, or models as instruments for improved analysis and planning. Domestic and international training plans will be developed by the advisor in consultation with Chief of Party and the Home Office of the Contractor. Such activities will include short courses such as those offered by the USDA in agricultural analysis, finance, management etc. Observation trips will also be arranged for visits to other banking operations and systems of particular relevance or utility such as in the Philippines and in other countries of Africa and perhaps Latin America where lessons and innovations can be captured from good and bad experiences in similar programs.

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Early in Phase I, a senior Ugandan agricultural finance specialist will either be recruited or selected from existing staff by the Bank who will also serve as counterpart to the advisor. He will be trained on the job by the advisor and eventually replace him, probably serving in the role of Deputy Chief of the Division.

The advisor will work closely with the external technical assistance group throughout the project to assure complementarity of purpose and activities. Initially, he or she will be charged with the task of developing referral procedures for projects in need of feasibility, planning, and management assistance. It will be a responsibility of the Department to assess the need for such assistance for all incoming proposals and make appropriate referrals to the external group for response and action. The Department will also determine funding requirements for such assistance and build these costs into loan plans where necessary.

In another area of referral, the advisor will coordinate with the Procurement Services Agent (PSA) element of the U.S. Contractor in order to incorporate adequate procurement plans into each project. It is currently envisioned most project procurement will take place outside of the Bank through the PSA.

There may be cases, however, where bank involvement would make sense due to well established connections and procedures for a particular commodity group. In consultation with the PSA and the USAID, the advisor will assure that AID procurement regulations (source/origin etc.) are observed. (See Annex ___, Waivers)

Finally, the advisor will be responsible for setting up a permanent data collection and processing system within the Department which will feed into the data management analytical component of the project as a whole (See section 5, below below.) This will be one of the first activities in order to capture base line data from the initial group of projects to be financed. A micro computer with appropriate software will be purchased for the Division for this purpose and also for project tracking and reporting along with a variety of other uses (word processing financial projections, etc.). Short term consulting assistance will advise on the initial establishment of the system.

The PP design analysis of the Bank concluded that it should be possible to complete the above activities and leave satisfactory systems and trained staff in place within the three year time frame of Phase I, upon the conclusion of which, long term services would cease. There will probably be a need for some short term inputs in Phase II however as follow-up to assure continuing proper utilization of systems, methods, and procedures established. The Phase I evaluation will provide the basis for additional technical assistance if necessary.

Note: Although both long and short term technical assistance for the institutional component will be focussed almost exclusively on the UDB, the principal advisor will coordinate and share information with other participating banks in order to make effective use of scarce resources, avoid duplication of effort, promote the concept of agricultural investment lending etc. In cases where a proposal is more appropriate for a commercial bank financing, for example, these will be referred accordingly. Such cases would be expected to require a lower level of funding over a shorter period with a relatively high projected rate of return and be proposed by a borrower who could meet private bank collateral requirements. Ideally, the UDB should strive to work with those projects which, for whatever reason, are not attractive for the private banking community. This concept will be pushed by both the UDB advisor and the technical assistance group in order to extend the project as much as possible into the commercial banking sphere and to make the most effective use of the relatively more costly services and facilities of the UDB.

c) Summary of Inputs - TA TO UDB

USAID	Project Years						
	1	2	3	4	5	6	7
Technical Assistance (PM)							
Banking Advisor		3					
Ag Finance Advisor		6	12	12	6		
Data Systems		2	2		2		
Other Short Term		2	3	3	2	2	2
Commodities							
1 Vehicle (fuel)		x					
1 Micro-Computer		x					
Office Furniture and equipment		x					

Training						
In-Country Seminars		x	x	x	x	
Short Courses in US or third Countries		x	x	x		
Observation Trips US and Third Countries		x	x	x		
GOU						
Senior Counterpart Ag. Appraisal			12	12	12	12
Office and Logistic Support	x	x	x	x	x	x

3. Sub-Borrower Strengthening (The Enterprises)

a) Outputs

(1) The Technical Assistance Entity

- By the commencement of Phase I, the entity will have been established and staffed with expatriate advisors by the US Contractor and an estimated core group of 5 Ugandan professionals in financial analysis, accounting, business management, agro-industry, marketing etc. It will be operational and providing assistance to initial sub-borrowers.

- By the end of Phase I, the entity will have been legalized as a Ugandan enterprise and able to act as a legitimate private consulting agency in the capacity of either a profit making or private and voluntary organization. By this time, all local costs of the entity will be covered on an ongoing basis by user fees and a capitalization process will have commenced leading to complete financial independence prior to the end of the project.

- By the end of Phase II, all US assistance will have been withdrawn and the entity will be totally independent as a viable enterprise. By this time the organization will have a direct hire staff of eight to nine professionals capable of covering all estimated types of management and technical consulting needs of the sector, with the exception of the largest of the industrial enterprises linked toagriculture. By then, however, there should be other firms capable of addressing the needs of this higher level group.

(2) Enterprises Strengthened

- o A minimum of 40 to enterprises will have been assisted by the end of Phase I in feasibility and project design assistance for financing proposals. An additional 20 - 25 enterprises will have received business management assistance associated with project financed investments, for some of which such assistance will be provided over an extended period of time to assure successful launching of the new operation. (Most but not all, of these will be from the same group that received proposal assistance.)(For an illustrative schedule of enterprises to be financed, see Financial Analysis, Annex I.) These numbers will have grown to 120 and 50 respectively by the end of Phase II.
- o By the end of Phase I it is estimated that 40% of the organizations assisted will be able to carry out their own analyses in the future for the development of additional financing proposals.
- o By the end of Phase I, 100 persons from these enterprises will have participated in management training, feasibility study and other short courses carried out by the technial assistance entity! An additional will have been sent for short courses in the United States or third countries and/or on observation travel.

b) Implementation

(1) Advance Work

As soon as possible after signing the technical assistance contract, an advance team, hopefully consisting of the Chief of Party and the business analyst, and the agro-business advisor (to serve in this component) will arrive for a period of up to two months to carry out detailed planning and make all arrangements for full contractor mobilization. (The Development Bank specialist may also participate to a degree). During that effort, the technical assistance entity will be organized and planned in detail, a location securred (probably a downtown

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Kampala set of offices) and initial Ugandan Staff recruited (Recruitment should not be difficult given the amount of underemployed and otherwise available professionals in the market with appropriate backgrounds.)

According to the implementation plan, it is currently envisioned that the office will be established and operating in January 1986, assuming that the above advance work is carried out on schedule.

(2) <u>Organization and creation of the "Ugandan" Entity</u>

In terms of organization, the initial staff of expatriate advisors will include, a) an agricultural/agro-business specialist to cover the agro-technical feasibility side of the operation, b) a business/financial analyst to provide project proposal and design assistance in the areas of financial analysis and projections, business and management planning, and c) an accountant to supervise the training of accounting staffs of ventures to be assisted, assist with financial analysis and initially manage the books of the entity itself.

Initially, five Ugandan professionals the above areas will be hired to serve as counterparts to the advisors. Within the first year, however, and on the basis of early experience with demand for services to be provided, it is expected that the Ugandan staff will be increased to between six and eight technicians in such areas as animal production and marketing, agricultural economics, agricultural engineering, agro-processing, etc. The operation will be supported throughout Phase I with short term consulting as needed in indicated technical areas depending on the mix of clientel to be assisted and in what order and magnitude.

As indicated earlier, the philosophy of the TA entity approach in the project is to establish a viable private enterprise in its own right to respond to latent demand in the Ugandan market for the services essential for agro-enterprise planning, investment and development. During the first year or more of the project, costs will be almost entirely covered by the project through the U.S. Contractor, and fees charged during this period will be modest and subsidized, the idea being to establish the practice and the concept.

Initially revenues received will be deposited into a special account maintained separately by the contractor and allowed to accumulate. At the same time, an organizational proposal will

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be developed for the incorporation of a private firm or PVO under Ugandan law which will be legally and administratively distinct from the Entity and a board of directors recruited. The entity will then be legalized or incorporated under Ugandan law and take over receipt and management of revenues received by the entity. A formal agreement or contract will be signed with the new organization committing it to work in tandem with the entity and under the overall direction of the expatriate Chief of the entity for the duration of Phase I of the project. The agreement will also provide for the exclusive dedication of fees received to local direct costs and capitalization of the firm or PVO. No dividends to directors or shareholders will be allowed.

Over time, as funds accumulate, the firm will start acquiring staff, first a manager and then appropriate technicians. Logically it will draw from the Entity as the two organizations will be working as one in any case during the first phase. By the end of Phase I the objective in one form or another (directly or indirectly) is to transfer all local personnel and related costs to the new organization with the foreign exchange and direct support costs of the advisors being the only remaining elements funded by the contract. Upon the conclusion of Phase I, all operational responsibility and control of this activity would be turned over to the Ugandan management of the operation and the long term advisors would be pulled out.

With respect to Phase II, the programming of external assistance will depend on the results of the analytical component of the project and the evaluation to be conducted early in the last year of Phase I. What is contemplated for Phase II at this point is that technical assistance requirements will be met entirely through short term consulting inputs - both for the TA entity and the Bank.

Note: The above scheme is of several options or formulas for achieving the same result, ie., the independent TA entity. Others will be analyzed during detailed advance planning by the Contractor.

During Phase I, the entity is expected to exclusively serve clients referred by banks participating in the project. In the case of the UDB, in the initial review of a proposal the Agricultural Division will make a determination first as to whether or not the investment has merit and should be considered seriously. Secondly, recommendations will be developed regarding the level and type of technical assistance required to fully develop the proposal in terms of required feasibility analyses, financial projections, planning etc. The client will

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then be advised that if the loan is to be approved, assistance must be secured to perform the indicated analyses and finalize the proposal in form acceptable to the bank. Then the client will be referrred to the entity. In the case of Private Banks, the same process will be followed. In both cases, individual loans will include provisions and funding for the reimbursement of technical services required for feasibility studies and proposal preparation.

When clients approach the TA entity for assistance during Phase I, to be accepted by the entity they must have a written referral from the Bank specifying that services are necessary and agreeing to fund them from the portion of the loan to be granted in local currency. The entity will then negotiate and sign an agreement with the client specifying exactly what will be done at what cost. From time to time in this process it may be necessary for the entity to return to the Bank for clarification on the nature and scope of the work to be done.

The entity will then carry out the indicated analyses providing as much technical assistance as possible to the client in the process. In the development of the proposal, the entity wil also assess the need for follow-up technical assistance in management, planning, technical areas etc., and make a written recommendation covering such services to the Bank along with the rationale. On receipt of the proposal, the bank will make its own determination as to whether follow-up services are required and if they should be funded. In the event the proposal is still not fundable, the Bank will provide instructions to the client and the entity as to what additional work is required. In the event that the proposal is rejected outright, the Bank will so inform the client and the TA entity in which case, at least during Phase I, the entity will not be reimbursed for its inputs. This is a contingency that the project will have to cover during the three year Phase I period.

(4) Phase II

As described elsewhere, upon the conclusion of Phase I, the technical assistance entity will commence operating totally independently of the U.S. Contractor. The idea is that it will essentially continue providing similar services with the same arrangements and understandings with the Banks as before, except that it will now be free to respond to requests from clients totally outside of the project and work out whatever arrangements it wants to for payment. It will also be free to do business with other donors, negotiate new arrangements with the Banking community or take any new direction that it desires. If it is to continue to receive technical assistance

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and payment from banks for services rendered under the project, however, it will have to comply with certain established groundrules and standards or it will loose clients, business and revenues associated with project. By this time, it will also probably have to compete with other firms expected to enter the market if growth within both industrial and agricultural sectors materializes as expected over the next four years or so.

Concerning the programming of Phase II technical resources, this is to come from the evaluation and planning to occur in the final year of Phase I. What is now expected is that the assistance will primarily take the form of relative specialized agro-technical consulting related to some of the larger possible projects of a major agro-industrial nature. Up to six months a year for the final three years of the project is provided for this purpose. This assistance can be channeled through the TA entity, the Banks or directly to the client enterprises, as most appropriate based on the evaluation and emerging needs, conditions and circumstances.

c) Summary of Inputs - TA Entity

USAID	Project Years 1	2	3	4	5	6	7
Technical Assistance (PM)							
Agro-Industrial Advisor (short term)		2					
Business/Financial Analyst (short term)		2					
Agro-Industrial Advisor (long term)		6	12	12	6		
Business/Financial Analyst (long term)		6	12	12	6		
Accountant		6	12	12	6		
Other Short Term Inputs			6	6	4	6	6
Commodities							
6 Vehicles		x					
2 Micro Computers Software		x					
Office Furniture and equipment		x					

<u>Training</u>				
In-country Seminars		x	x	x
Short Courses in U.S. or third countries		x	x	x
Observation Trips in U.S. and Third Countries		x	x	x
<u>Other Costs</u>				
Office Rent	x	x	x	x
Uganda Staff	x	x	x	x
Professionals				
Support Staff				
Transportation/Costs				
Other Operating Costs	x	x	x	x

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4. <u>Financing</u>.

a) <u>Outputs</u>.

(1) <u>Loans Made</u>:

Up to approximately 120 loans are expected to be made over the five year life of estimated project lending activity. The majority of these will fall between $50,000 and $100,000 in terms of the AID financed foreign exchange component in 1984 dollars. The average loan is calculated at approximately $85,000. In accordance with the projected disbursement schedule based on estimated absorptive capacity of lenders and sub-borrowers (See Institutional and economic Analyses) projected lending targets are as follows:

	Phase I			Phase II	
Year	1	2	3	4	5
Disbursements: ($000)	1,250	2,075	2,700	3,325	3,150
Loans Made:	20	33	43	53	50

(2) <u>Jobs Created</u>:

A total of some 2,000 jobs are expected to be created as a direct consequence of project lending based on an estimated average cost of per job of approximately $6,150.

(3) Sub-projects to be Financed:

An illustrative list of sub-projects to be financed under the project is as follows:

20 Dairy Farms
6 Hatcheries
40 Poultry Farms
10 Feed Mills
10 Fishing enterprises
20 Mixed Farms
xx Undetermined but substantial number of smaller
enterprises (mainly financed by the commercial
banks for new equipment)

Exactly what portion of these will be financed in Phase I or II is difficult to predict at this time. It is also certain that a variety of new possibilities will be developed during early years of the project for both rehabilitation and new enterprise.

In addition, the project expects to finance a relatively few larger enterprises long in need of rehabilitation such as the Wankoko poultry processing plant ($300,000 loan) and up to four oil mills (3 for rehabilitation and one new plant representing a total investment of up to $3.5 million). (See Appendices to Financial and Economic Analyses Annexes.)

b) Implementation.

(1) General

The $12.5 million (in non-inflated terms) to be provided by this project for lending will be in the form of a line of credit passed through the Bank of Uganda for onlending by the UDB and other participating ICIs on commercial terms to productive enterprises in the agricultural sector. Of the amount designated, and for purposes of analysis, some $8.5 million has been illustratively allocated to the UDB, with the remainder going to other, commercial, ICIs. Actual amounts, however, will depend entirely on the capability of the ICIs in question to demonstrate capacity to productively absorb the resources in the form of viable packages of loan requests in conformance with project lending criteria. It will also depend on willingness to participate and to bear the risks inherent in the medium to long term investment lending proposed. The UDB is

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already heavily committed, and Grindlay's has indicated that it is prepared to participate to an undetermined degree (See Institutional Analysis); but it remains to be seen if the other commercial banks will opt to participate. Indications are that they will, once they have observed expected successful performance of Grindlay's loans. (The manager of Grindlays has indicated to the USAID that once the bank is on board and lending, the others should follow suit.)

Host country contributions to the lending component of the project are expected to come to over the local currency equivalent of $11.5 million, consisting of the following elements:

- Up to US $ 5.0 million from the Bank of Uganda in the form of local currency refinancing of up to ____ % of rediscounted UDB sub-loans to project sub-borrowers. This could, in fact, be more or less depending on the level of UDB lending achieved over the life of the project.

- Up to $2.7 million, or approximately 50% of the value of foreign exchange costs, from participating commercial banks in accordance with local currency component requirements for most investments.

- Up to $4.0 million from sub-borrowing clients of the ICIs in accordance with equity contribution requirements, at least 20% of the 12.5 million grant plus the above local currency loan components.

  Total: $11.7 Million - rounded to $11.5.

In accordance with the structure of the project, it should be noted that the total of the combined contributions of the BOU and Commercial ICIs will roughly equal the same amount regardless of which of the ICI categories (UDB vs Commercial Banks) actually end up borrowing more or less. That is, to the degree that one increases, the other will decrease and vice versa.

In summary, the RPE line of credit will generate total direct investment lending of at least $24 million over the life of the project, not including additional lending for the same purposes to be generated from rollovers at the ICI level, estimated to add another $10 million by the end of the project for a total leveraged investment of $34 million.

(2) Terms and Conditions of Lending

Funds for sub-loans will pass through the Bank of Uganda to the UDB and participating commercial banks. The terms and conditions of lending by the BOU remain to be negotiated in final form but should provide adequate margins to the ICIs to enable them to cover expenses and earn reasonable profits. (In the case of the UDB, once projected project lending is outstanding, an annual income of up to $400,000/year will be available to cover portfolio administration costs.)

Initial terms proposed and also used for design analysis purposes have the BOU lending to the ICIs at a 6.5% rate of interest, over a 20 year term, with a ten year grace period on repayment of principal and interest to be paid annually from the first year. The long grace period allows the participating bank to build up internal reserves which will be relent for the same purposes. The objective is to develop the lending activity at the intermediate level and to make the loans sufficiently attractive so that participation will be as wide as possible. Despite the fact that this project is a grant, the BOU, in effect, will also bear the burdon of maintenance of value. That is to say, if there is a devaluation, the BOU will decapitalize to the same degree relative to the dollar in terms of the outstanding project financed portfolio. The ICIs in tern are expected to lend at between 15% and 17% (the legal maximum for agriculture) to sub-borrowing clients with terms of up to 8 years and grace periods as warranted by financed projects, but probably averaging in the vicinity of two years.

In line with AID policy criteria, an objective of the project is to foment a going rate or real cost approach to lending for development. In the case of Uganda, the project is hampered by legal maximums, as is the case in most countries. To the extent that other measures can be developed to protect the equity base of the lenders in terms of the cost of lending, delinquencies, the eroding effect of Uganda's improving but still relatively high rate of inflation, they will be studied for possible adoption.

Further, and in order to protect the capital resources of the project to the extent possible, maximum delinquency and default rates will be negotiated with the GOU with respect project loaned funds. If they fall above the specified level, further disbursements for the ICI in question will be halted. Such rates will be determined for both principal and interest obligations. The suggested initial formula at this point is ______% delinquency on outstanding balances due over 90 days of either principal or interest. In the event that a given ICI falls under this provision and it is envoked, it can, although won't necessarily, be revoked, once the ICI has recovered amounts due sufficiently to fall under the allowed maximum.

(3) Lending Criteria

Lending criteria (described further in Part III. E.) is still illustrative and will be refined during the detailed planning and negotiating stage of the project and submitted for approval by AID as a condition precedent to disbursement for the credit component. Described below are certain minimums, however, which will be preserved by covenant.

(3.1) ICI Eligibility

The ICI must be a legally chartered bank or financial institution authorized to operate in Uganda with an established program of lending to private enterprise. It must also be able to demonstrate adequate staff, operating procedures, and financial condition to satisfy AID as to its ability to lend responsibly under the terms of the project. Finally, it obviously must be prepared to abide by AID policy, program and project criteria as summarized below for the sub-borrower group, which, among other things, implies a solid analytical appraisal capability in terms of sub-project eligibility, feasibility and viability. In the case of the UDB, it has, in effect, been pre-qualified through analysis carried out during final design. (See Institutional Analysis) Further, technical assistance is being provided to the UDB, in part, so that it will be able to comply with established criteria, especially in terms of appraisal capability. Grindlay's and to a lessor extent the Uganda Commercial Bank,were also reviewed by the design team (See Institutional Analysis). Nevertheless, these lenders will have to present detailed evidence, satisfactory to the BOU and to AID, that they have the capability and the commitment to comply with criteria, norms, and standards required by the project.

(3.2) Sub-Project Selection

Borrowing enterprises must be Ugandan owned and controlled with their principal place of business in Uganda. Further, all project assisted enterprises (including cooperatives) must be in the private sector and be profit making ventures. In the case of cooperatives, PVOs, or otherwise non-profit making enterprises, they must be able to demonstrate that they are seeking to maximize their net returns and to capitalize for further investment and growth. All enterprises must be primarily operating in the agricultural sector, either in production or in processing or service activities directly linked (forward or backward) to agriculture. With respect to sub-projects, one of the following key conditions must be met; labour intensive (maximum of $6,000 per job created), have clear potential for import substitution or export and provide increased markets, inputs, or service for agricultural production based on locally available inputs. Further, the following AID program and policy criteria at a minimum will be met: a) adequate planning and costing [Section 611 a)], b) environmental soundness with protective or mitigating measures where necessary (See Environmental Analysis, Part IV___), c) financial soundness (projected rates of return), d) technical soundness (appropriateness of the technology employed), e) social soundness (equity considerations) and e) managerial competence to execute the project in accordance with the approved terms and plan of the loan.

With respect to any of these criteria, sub-borrowers may receive assistance, if necessary, from the technical assistance entity described earlier, either by choice or as required by the lending ICI in order to receive the loan. Sub-borrowers, of course, will be free to seek out any source of assistance they choose to meet the above criteria, but they must meet it in order to qualify.

It should also be noted here, that any loan for a total amount of over $200,000 of project funding will be directly approved by The AID mission director.

(4) Structure and Mechanism

A variety of details remain to be worked out during pre-implementain planning for the lending component. For the most part these will be spelled out in an operations manuel to be developed with contract assistance which will be negotiated and approved by AID and the Bank of Uganda. The manuel will spell out all project operating procedures and will be widely available for ICI, project, bank, and other personnel with a need to understand how the project works. In general, with respect to lending, the following is expected:

In order to participate, all ICIs must negotiate and sign an AID approved loan agreement with the Bank of Uganda. This will be a boiler plate document with all terms and contitions for lending and a line of credit stipulated. On a quarterly basis thereafter, each participating ICI will consolidate loan requests which it has approved, or expects to approve, in the period and present a global request for drawdown to the BOU. The BOU will then approve the drawdown and so advise the ICI and AID so that appropriate

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disbursement, executing and supporting arrangements may be made, either directly or through the US contractor. (Technical assistance, procurement, etc.)

With respect to sub-lending, ICIs will approve and negotiate individual sub-loans with client enterprises in accordance with established procedures. Each loan will have a detailed procurement list and plan (developed or assisted where necessary by the Procurement Services Agent) with a breakdown of what will be procurred off shore or locally (shelf item). Once the loan is signed, the PSA will proceed with procurement in accordance with procedures described in the the Procurement Plan (Part V, A.7.)

Interest on foreign exchange lent will be simultaneously calculated for both Sub-borrowers and ICIs based on outstanding balances from the time of sub-loan disbursement, on whatever schedule, until principal amounts outstanding have been paid. There will, in fact, be no direct disbursements in dollars within Uganda except when AID is required to change dollars for disbursements in local currency for shelf item procurement or to reimburse the Technical Assistance Entity for services rendered to sub-borrowers under authorized sub-loan agreements. With respect to local currency disbursements from counterpart sources, either the ICIs themselves or through the BOU's rediscount facility, interest will be calculated as required by the respective lender.

(5) Lending Component by Phase

During the pre-implementation phase, the operations manuel will be developed; criteria will be negotiated and approved; and detailed disbursement, procurement, tracking and other procedures will be worked out.

Lending activity during Phase I and II will depend completely on the ability, motivation and actions of the ICIs and sub-borrowers, and to a degree on the US contractor. It is not possible to predict at this point what will move first or in what order or magnitude. From final design, it is certain that a significant number of pre-qualified, viable projects are only awaiting finalization of feasibility and appraisal work prior to launching, however, and it is believed that lending will commence in volume in the first half of 1986. (See Implementation Plan.)

Note: For Inputs, see disbursement schedules and financial projections in Financial Analysis below.

5. Data Management, Analysis, Evaluation and Planning

a) Outputs

Phase I

- Base Line Information re sub-borrowers, sub-projects, ICIs and the technical assistance entity

- Periodic reporting of indicators showing progress or lack thereof from base line toward project objectives and targets.

- Detailed operational reporting for purposes of sub-project tracking, implementation monitoring, trouble shooting etc.

- Special analyses or studies for purposes of policy formulation, strategy development, activity planning, programming of human or financial resources, coordination, identification and sharing of innovation etc.

- Base material for the detailed planning of Phase II

- Useful material for capital resource mobilization from external donors and lenders as well as private capital markets.

Phase II

Hopefully, all of the above will continue to apply to Phase II in addition to a detailed final evaluation which will provide the basis for replication of models developed by the project in other settings and which will leave the Ugandan project community (BOU, ICIs, sub-borrowers, support entities) with a firm analytical basis for new and still more effective long range planning.

b) Implementation

By nature, this project is experimental. Systematic data collection and analysis will be critical to successful implementation throughout the project period. This component, therefore, will receive a very high priority by AID and the US contractor.

In addition to continuing analytical activity within the foremal structure of the project, there will be several special studies and surveys, described below, as well as two major external evaluations in the last years of Phases I and II.

The Data Collection component of the project will be contributed in its entirety by AID through the US Contractor. Management responsibility will likewise rest with the US contractor through Phase I with the exception of the external evaluations. Under current circumstances, it would not be possible for the GOU to justify committing scarce resources to such an effort, although counterpart institutions and personnel will be asked to participate and contribute on a systematic basis as part of their main line functions.

The major elements of this component are as follows:

(1) Data Management and Planning Office

A separate office will be established within the Technical Assistance Entity with a full time Ugandan data management expert in charge. Supporting him will be an average of two graduate assistants as necessary in statistics, agricultural economics, rural sociology, operations research etc, drawn from Makerere University or other Ugandan sources. The office will report directly to the Chief of Party. Advising the effort will be short term US consultants in data and information systems development and management and as necessary in finance, credit, rural sociology etc., in order to develop and maintain the system contemplated and carry out the studies indicated below.

Upon conclusion of Phase I, it is intended that the office will be taken over by the Ugandan Technical Assistance Entity and maintained throughout Phase II doing much the same work as in the first three years of the project. During Phase II AID will continue providing funding and consulting support as determined in detailed planning to occur late in Phase II. Upon conclusion of the project, it is hoped that activities and costs of the office will be maintained by the TA entity as a very useful arm in the ongoing conduct of its consulting services to enterprises, lenders, potential donors, etc.

During Phase I the Data Management Office will have four major functions as described below:

- Supervision and coordination of all studies to be conducted under the project (described below).

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- Development of an information system by means of which continuing feedback for planning and programming purposes will be directed to Project Management (BOU, AID, The US Contractor) and participating ICIs.

- The development of quarterly, annual and longer term work plans and reports for the project as a whole. The office will provide analytical "backstopping" for all major activities.

- Preparation of data and analytical material for the two major evaluations to be conducted of project performance and impact.

In addition to the studies detailed below, the office will be provided with funds ($150,000) which can be drawn on flexibly for other short studies, analyses, and planning exercises as may be required in the course of project development and implementation.

(2) Studies and Surveys

(2.1) Base Line Data:

This study will establish the base line for the project for use in subsequent evaluations and for a variety of other analytical and planning uses. It will be carried out within six months of the signing of the prime contract and will include, tentatively, the following elements:

- Credit Demand both for base line purposes as well as raw material for planning promotion, training, and technical assistance activities. The study will include both existing agricultural enterprise proposals in participating and potentially participating ICIs and unsolicited proposal potential in the field

- The status of project appraisal, approval, follow-up, and collection operations in the ICIs to be able to measure improvements in effectiveness and efficiency over time. The focus of this will be on the UDB.

- Profile of client enterprises in terms of the nature and activity of the enterprise itself, financial condition, size, management, plans for growth and expansion etc.

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(2.2) Constraints to Agricultural Enterprise Development.

Late in the second year of Phase II, after some experience has been gained with Project sponsored operations, the constraints study will be carried out to provide the analytical basis for redesign of project interventions in the last year of Phase II. This will also directly feed into the evaluation, and provide valuable insight into why the project is behaving as it is or experiencing a given set of difficulties. Tentatively, the study would cover the following aspects:

- Policy constraints - the edible oil tax, price fixing by parastatals, exchange controls, etc.
- Ownership and land tenure difficulties
- Managerial and technical skill levels in agricultural enterprise
- Savings, capital accumulation and investment options for successful enterprises
- Marketing barriers - domestically and for export
- Infrastructure constraints, especially transportation

Note: Any study of constraints to development in Uganda under present circumstances should take into account and/or analyze security and corruption problems. For obvious reasons, however, how these delicate areas would be approached would have to be thought through carefully and negotiated with the GOU.

(2.3) Alternative and informal credit systems - Internal Capital Markets

The study would look at other financing options for entreprises and draw conclusions about the relative merits of different alternatives for the client group as opposed to Project ICIs. It may be that different systems are worth consideration as possible vehicles for certain types of investment. Vehicles that would be considered would include credit cooperatives and other cooperative lending structures, money lenders, major companies in either supply or marketing etc.

(2.4) Women in Development

A study will be carried out early late in the first year of Phase I to determine how women participate in enterprises

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financed and what can be done to further their effective involvement in agricutural enterprise development. Again, conclusions from this study will serve as a basis for Project modifications in Phase II. Scopes of work for all these studies will be approved by AID prior to execution.

(3) Ongoing Data Collection

Prior to commencement of lending activity, the Data Management Office will develop systematic data collection, recording and reporting requirements from both ICIs and sub-borrowers. Separate files will also be established on each sub-project for the maintenance of time series data of particular importance for measuring project impact at the client level. Also for this purpose a computerized project tracking system will be established which will depend on systematic reporting of lending and borrowing entities. With sophisticated and easy to use software now available this should not be a particularly onerous task. The office will encourage the development of complementary and parallel systems in participating ICIs for improved follow-up activities, collections, etc.

The above system or systems will approved by AID prior to implementation.

(3) Evaluation

Major external project evaluations will be carried out in the third years of both Phases I and II. The first, among other things, will lead directly into a detailed design and planning exercise by participating agencies for Phase II. The second will provide a well documented basis for replication and/or use of experience gained in other programs in Uganda and other countries. Both should be very helpful in additional resource mobilization and for policy and strategy by AID and other donors.

Separate contracts will be utilized for each of these evaluations in order to maintain objectivity. In the case of Phase I, upon conclusion of the evaluation, the US contractor will work under AID's supervision and guidance in the execution of the planning exercise for Phase II.

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c) Summary of Inputs - Data Management

USAID Years	Project 1	2	3	4	5	6	7
Technical Assistance (PM)							
Chief of Party		6	12	12	6		
Short Term Consultants		3	4	4	4	2	
Training		x	x	x			
Short term in-country							
Commodities							
1 Vehicle.		x					
1 Micro Computer Software		x					
Office Furniture		x					
Other Costs							
Transportation							
Ugandan Staff							
Chief		6	12	12	6		
2 Research Assistants		12	24	24	12		
Special Fund for Study Purposes.		30	50	50	20		

The Chief of Party is pegged against this component of inputs as a matter of convenience. He or she will be administratively separate from any particular component of the project and will be devoted full time to overall management of the prime contract and the various activities under it. For obvious reasons, however, it would suit project purposes if the Chief could have some background and expertise in Data management and planning.

Note: This completes the project description. In addition to the inputs shown in the sections above, the following additional contributions are calculated into the final cost estimate in the following section.

Advance Work - Separate Contracts to assist USAID in "pre-prime" contract groundwork that must be carried out in first year and a half after authorization. (July 1984 - December 1985)

Administrative Arrangements Conditions Precedent etc.	6 PM
Invitational Travel to visit the National Development Bank of the Philippines - 4 persons, 2 weeks from the ICI group.	4 PM
International Executive Service Corps and other volunteer consulting services Spread over Phase I	6 PM

Separate Auditing contract with internationally recognized firm with local office which will audit ICI and Borrower Performance under the project periodically over Phase I (and Phase II if necessary) and report to the USAID.

E. Financial Plan and Cost Estimate.

Total project cost over the seven year and one half year project period (inflated at 10 % per annum) is estimated at just short of $51 million of which; a) AID will contribute $17.4 million for the lending component and $15.5 million in technical assistance related costs, b) the banking system (Bank of Uganda plus the ICIs) will contribute approximately $11 million, and c) sub-borrowing enterprises will put up an additional $6.9 million. AID, therefore, will finance 64% of total costs while the banks and sub-borrowers will finance 22% and 14% respectively.

Recurring cost is not expected to be an issue under this project as; a) sub-borrowers will gradually assume the cost of their own technical assistance through the process described in D.3. above; b) commercial banks will not participate in the first place unless they are convinced they can make a profit; and c) the UDB is already staffed to manage their portion of the lending activity, basically needing only an upgrading of skills and processes. (See Economic and Financial Analyses for the viability of the lending activity itself.)

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BUDGET TABLE 1

DETAILED EXPENDITURES BY PROJECT YEAR
($000)

Project Year	1	2	3	4	5	6	7		
	1984/85	1985/86	1988/87	1987/88	1988/89	1989/90	1990/91	Total	
AID FINANCED INPUTS									
Credit Line		1250	2075	2700	3325	3150		12500	(1)
Inflation - 10%		125	415	891	1529	1890		4850	
Sub-Total		1375	2490	3591	1890	4850		17350	
Long Term Tech. Asst.									
Chief of Party		85	165	165	85			500	(2)
Agrobusiness/Management		85	165	165	85	– –		500	(2)
Financial Analyst		85	165	165	85	–		500	(2)
Accounting Systems		85	165	165	85	–	–	500	(2)
Financial Analyst (UDB)		85	165	165	85	–	–	500	(2)
Short Term Tech. Asst.									
Banking Advisor		30				–		30	(3)
Data System Spec.	–	20	20	–	20			60	(4)
Agro-Industrial	–	25	–	–	–	–	–	25	(5)
Business Analyst	–	25	–	–	–	–	–	25	(5)
Other Int. and Local	75	62	162	162	125	125	100	812	(6)
Local Hire									
Professional Staff	–	90	140	200	200	–	–	630	(7)
Support Staff	–	20	50	60	60	–	–	190	(8)
Local Travel	–	80	100	120	80	–	–	380	(9)

	1984/85	1985/86	1988/87	1987/88	1988/89	1989/90	1990/91	Total
Commodities								
Vehicles	-	100	30	15	-	-	-	145 (10)
Office Equipment	-	50	20	5	-	-	-	75 (11)
Computers	-	40		-	-	-	-	40 (12)
Local Office Overhead	-	24	24	24	12	-	-	84 (13)
Training								
In-Country for ICI's	-	20	20	20	-	-	-	60 (14)
US & Third Country	-	40	60	80	60	-	-	240 (15)
In-Country Entrerenures	-		20	20	20	-	-	60 (16)
Observation Trip	-		13	-	-	-	-	12 (17)
Misc. and Start-Up	-	100	20	10	10	-	-	140 (18)
Contractor Overhead Rate = 85% (loans excl.)	-	893	1261	1301	851	106	85	4500 (19)
Procurement Service	-	50	50	50	50	-	-	200 (20)
Research Fund (Data Mgt)	-	30	50	50	20	-	-	150 (21)
External Audit	-		-100	100	100	100	-	400 (22)
Int. Volunteer Serv.	-	5	10	10	5	-	-	30 (23)
Evaluation	-	-		-	80	-	80	160 (24)
Sub-Total	75	2130	2975	3053	2119	331	265	23448
Provision for Inflation 10% compound annually		213	595	1007	975	199	204	3193 (25)
Sub-Total	75.00	2343	3570	4061	3093	530	469	14142
Contingency - 10% all TA	8	234	357	416	309	53	47	1414
Total - All TA	83	2578	3928	4467	3203	583	516	15556

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	1984/85	1985/86	1988/87	1987/88	1988/89	1989/90	1990/91	Total
COUNTERPART CONTRIBUTIONS:								
Bank Financed Inputs								
Local Funds Lending								
UDB	-	425	674	942	1231	1540	385	5196 (26)
Commercial Banks	-	200	417	552	696	452	183	2500 (26)
Sub-total		625	1091	1494	1927	1992	568	7696
Inflation 10% p.a. comp.	-	63	229	493	886	1215	437	3323 (27)
Sub-total incl. inflation	.00	688	1320	1987	2813	3207	1005	11019
Enterprise Fin. Inputs								
Enterprise Equity	-	375	633	839	105	1028	114	4039 (28)
TA Entity (Ugandan)	-	-	-	-	62	334	334	730 (29)
Sub-total		375	633	839	1112	1362	448	4769
Inflation 10% p.a. comp. (30)	-	38	133	277	512	831	345	2135
Sub-total incl. inflat.		413	766	1116	1624	2193	792	6904
TOTAL LOCAL CONTRIBUTION (31)	-	1100	2086	3103	4437	5401	1798	17923
TOTAL PROJECT COSTS	83	5053	8503	11161	12693	11023	2314	50829

BUDGET TABLE 2.

SUMMARY OF TOTAL PROJECT
COST BY FUNDING CATEGORY

	AID	BANK	ENTERPRISES	TOTAL
1. Technical Assistance				
Project Operations	4737		730	5467
Evaluations	160			160
Procurement	200			200
Audit	400			400
IVS	30			30
Research	150			150
2. Training				
In-Country	300			300.00
Overseas	73			73
3. Commodities	260			260
4. Misc. and Start-up	140			140
5. Contractor Overhead	4500			4500
6. Credit Line	12500	7696	4039	24253
Sub-total	23449	7696	4769	35914
Inflation 10% p.a. comp.	8044	3323.	2135	13501
Sub-total	31492	11019	6903	49415
Contingency 10% (TA only)	1414			1414
GRAND TOTAL PROJECT	32906	11019	6903	50830
Above % of Total	.64	.22	.14	1.00

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ASSUMPTIONS FOR THE PRE BUDGET
(Corresponds to notes on right margin of Table 1)

Note

(1) Combined drawdown of UDB and commercial banks based on projections from Tables 2 and 3 of Appendix 1, Annex E, Financial Analysis.

(2) Three years of long-term technical assistance starting in second year. Cost calculated per current person year estimates for Uganda. Breakdown of costs per person in Table___.

(3) Development Banker for 3-4 months to assist in reorganization of the Crops and Livestock Departments of the UDB. Will also assist in setting up procedures for on-lending by BOU and the ICI's.

(4) Computer consultant to establish information and analytical systems for UDB and Data Management Service. 2-3 months in each years 2, 3, and 5.

(5) These two short term consultants will work with Prime Contractor's start-up team during second half of 1985. Primarily involved in planning and design for long-term technical assistance team.

(6) In first year, 6 months of consultant working with AID mission finalizing agreements with GOU and various ICI's. Providing assistance to the mission on preparation of various documents for the project, preliminary planning, and other project related matters. These initial contracts will be directly with Mission and not through the Prime contractor. Cost estimated at $12,500 per month. Remaining short-term consultants will be supplied by prime contractor.

(7) Fully burdened costs of local hire professional staff estimated at $20,000 p.a. Salary and benefits competitive with top international commerical organizations operating in Uganda to discourage employees from taking secondary jobs.

(8) Secretaries, clerks, drivers, guards.

(9) Vehicle operation costs estimated at $10,000 p.a. per year based on $.50 per mile and 20,000 miles per year. Short-term technical assistance, local hire staff, and data management service transport cost included. Long-term technical assistance service transport cost included. Long-term technical assistance transport cost built into budgets for each position. Also includes provision of lodging while on safari. Road conditions in Uganda are very poor and repair and maintenance costs are high.

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(10) Estimated average cost of vehicle is $15,000. Vehicles will range from 4WD cross country vehicles, small 4WD vehicles, and station wagons. Eight vehicles ordered in 1985, followed by two additional in 1986, and one in 1987. Five vehicles for long-term technical assistance team, balance for local hire professional, short-term consultants, and data management office.

(11) Desks, file cabinets, photocopy equipment, typewriters, calculators, etc. for the Technical Assistance Entity.

(12) Two micro computers with appropriate software and printers. Estimated cost CIF $20,000 each.

(13) Local office rent, telephone and other communications, office supplies, local legal and audit costs.

(14) Short-term courses and special on-the-job training for UDB staff. Possible extension to commercial banks as appropriate. Emphasis on loan appraisal and supervision.

(15) Short-term courses for enterprise staff and senior staff. Accounting, planning, management information systems. Directed to improving efficiency and productivity.

(16) Short-term courses in US and observation travel.

(17) Visit by local officials to Phillipines Development Bank.

(18) In second year, $100,000 is for mobilization and other general expenses, with amounts in years 3-5 for other miscellaneous expenses.

(19) Prime contractors overhead rate. Calculated on all services being provided by the contractor.

(20) Permanent Service (PSA).

(21) Special research funds for studies on agricultural and business environment related to development and support for private sector. Research subjects selected or approved by AID mission.

(22) Quarterly audits of participating financial institutions relative to administration and disbursement of RPE funds. Also audits of clients (enterprise) to ensure that lending is complying with AID regulations.

(23) Expenses for volunteer international business advisors.

(24) Phase I and II Evaluation.

(25) Inflation is calculated at 10% per year compounded for the balance outstanding. No inflation for year 1984.

(26) Local currency requirements for lending. Based on estimated local currency requirement of $.50 for every $1.00 of foreign exchange. Based on drawdown schedule in line #7.

(27) Inflated at same rate as foreign exchange requirements with assumption that while inflation rate in Uganda is higher than 10% per year, a devaluation in the Uganda Shilling will adjust the inflation down to that of the 10% projected for foreign exchange.

(28) All clients obtaining loans under the RPE project will require a minimum of 4:1 debt/equity rations. Calculated on projected lending of both foreign exchange and local currency lending of the ICI's.

(29) Fees charged to enterprises for services from the Technical Assistance Entity. Increasing as the program becomes a local operation.

(30) Inflation calculated as described note (27).

(31) Contribution to project (including inflation factor) of ICI's and enterprises. Not calculated are ICI operating costs or primarily operating through banking institutions, GOU direct financial contribution will be minimal.

(32) Contingency calculated at 10% per year on all project costs.

BUDGET TABLE 3.

Cost for International Technical Assistance Personnel
(annual cost)

1.	Salary (Base)	50,000
2.	Post Differential (25% bse)	12,500
3.	Personal Benefits (15% base)	7,500
4.	Inter-Travel (4 persons RT by 1/3)	5,000
5.	Household Shipping (1/3 RT)	10,000
6.	Storage	4,000
7.	Medical Ins/Work. Comp. (6% base)	3,000
8.	Housing (est. $2,000 month)	24,000
9.	Education (2 x $8,000)	16,000
10.	R & R (5% base)	5,000
11.	Security	2,000
12.	Vehicle/Local Travel 800 miles/month $.50/mile	4,800
	Sub-total	143,600
13.	Contingency (15% sub total)	21,600
	TOTAL	165,400

Note: Does not include contractor overhead.

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TABLE

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8.	Housing (est.$2000 month)	24,000
9.	Education (2 x $ 8000)	16,000
10.	R & R (5% base)	5,000
11.	Vehicle/Local Travel 800 miles month $.50/mile	4,800
	Sub-total	143,800
13.	Contingency (15% sub total)	21,600
	TOTAL	165,400

Note: RT = round trip.

PART IV - PROJECT ANALYSES.

A. Summary and Conclusions.

As AID experience in the 1970s and early 1980s (especially in Latin America but to a degree in Africa) will testify, ICI projects are bound to be fraught with difficult financial, institutional, technical, and often political, issues. The RPE project is no exception.

There is, and can be, for example, only modest assurance of success on lending system objectives, ie., the UDB and other ICIs. System growth and capitalization goals may be out of line with the reality of what will happen to the Ugandan Shilling and the economy in general over the next few years as a result of unforeseen policy decisions. Institutionally, the UDB may be dragged down by its heritage of old, uncollectable loans, or by a salary scale so low that it will not be able to hold on to good people. (Key staff members are holding out at present because they see a "brighter day coming" thanks to the excellent management that has now been installed in the bank and faith that positive policy change and hard headed leadership will pave the way for the development of a viable institution over the next few years able to reward good performance and loyalty in the face of adversity.

There is much greater assurance, however, with respect to the target enterprise end of the system. From time spent in the field and analyses performed, the team is totally convinced of the demand side of the equation. The capacity to effectively absorb resources to be provided by the project and other sources is not in place, but that is what this project is all about: and AID will be in a position to provide and control inputs to an extremely receptive target group. The enterprises to be assisted have everything to gain and a lot to loose if they don't perform in terms of investments implying sacrifice to secure. (The loans themselves can be lost along with the equity contribution and the business itself in many cases if resources are not utilized effectively.

Further, in the past Ugandans have shown they can make it in the sphere in which the project will operate. They will be able to make it again, given time, assistance, and access to resources. The economics, as will be seen below, make sense. Comparative advantage on the production side is in place due to the countrys favorable climate, soils and other resources already described. Lacking only is capacity to analyze, package, and manage adequately to solicit and wisely utilize additional capital required for rehabilitation and solid growth.

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Finally, this is not the traditional AID ICI project focussed on the small farmer or the poorest of the poor. The target group is part of an entrepreneural class. It has demonstrated it is interested in more than mere survival - often the result of small farmer subsidized credit programs which do little more than provide for one more season's marginal production. This project is focussed on business development amongst a group of people who have already invested to a greater or lessor extent and, who by and large, are planning and striving for improvement - often to get back to where they were at an earlier time.

In conclusion, despite the unknowns, issues and constraints that must be faced, the design team is confident that this project will result in at least a partial success, ie., capacity to absorb will be developed - at least on the sub-borrower level - and rehabilitation, recovery and development of productive enterprise will take place.

B. Economic Analysis.

1. Introduction.

For several reasons, the design team determined that a standard benefit/cost analysis, with an internal rate of return calculation, should not be attempted for the project. Chief among these was that no mothodology could be effectively developed to adequately take into account the illustrative and changing nature of the sub-projects to be financed or to quantify either costs or benefits for over a hundred and some sub-projects. Rather than engage in excessive conjecture, therefore, the team chose to base the analysis on illustrative case examples, summarized below, and on overall economic conditions as observed and analyzed by the IBRD and others.

2. General Economic Situation.

Notwithstanding the serious political and security problems that continue to plague the Government of Uganda, the economy in general, and especially certain segments of the agricultural sector, are now experiencing relatively good rates of growth. Upon conclusion of the 1979 "War of liberation" however, the new government had inherited a devasted country caused by gross mismanagement during the Amin years and destruction during the war. Industrial capacity had been severely reduced; infrastructure was in disrepair; inflation was rampant; and the central government was almost bankrupt.

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In consultation with the IMF over the past 3 years the Government has adopted several key economic/fiscal reforms contributing to economic recovery, the most significant being; (1) the float of the Uganda Shilling from just over Shs. 7.6 to U.S. dollar to the present rate of USh. 210 (window 1) and USh. 330 (window 2), (2) significant increases in the farm gate price for export crops (Ref. Table 3) and (3) the removal of most price controls for export crops, consumer products. Likewise, the price of locally consumed food crops is governed by market conditions. The government also increased interest rate levels and established ceilings on domestic and government borrowing.

In terms of overall economic performance, the GDP rate of growth in real terms increased from 3.9% in 1982 to over 6.1% in 1982. Higher rates have been experienced in the subsistence sector compared to the monetary sector. Continued growth is expected in the near term, and the recent budget for 1983/84 generally favors continuation of monetary policies previously worked out in consultation with the IMF.

Market forces are expected to increase their influence in the economy, and more of the financing of imports should shift to Window II exchange rates. It has also been proposed that all new external debts incurred by government agencies should be financed at the Window II rate. The GOU now plans to increase the amount of foreign exchange available at Window II from $2 billion in 1982/83 to $3 billion in 1983/84. This will also help to reduce the potential risk of abuse from illegal or unauthorized purchase of dollars at the concessionary Window I rate. The RPE project will complement these positive economic policy measures and provide additional support to government efforts at rehabilitation and expansion of private enterprise in general.

3. <u>Sectoral Overviews</u>.

a) <u>Agriculture</u>.

Recovery in the agricultural sector continues to exceed previous expectations. Food crop production has been exceptionally good, but export crops are also doing well. Surplus maize was sent to Tanzania. Uganda is fortunate in that such a large portion of the country is suitable for crop production and livestock. Also, about 15% of the land area is freshwater rivers and lakes containing large stocks of fish.

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The major source of foreign exchange earnings for Uganda is the export of cash crops, of which coffee presently represents about 95%. Uganda has a current coffee quota set by ICO at 162,000 tons and expects to have this increased to 192,000 tons for the 1984 season. Coffee production in 1981/82 was 97,500 tons, 166,600 tons in 1982/83, and is projected to be 192,360 tons in the 1983/84 season. Uganda expects to be able to sell its surplus over quota profitably on the open market; although given the current oversupply of coffee on world markets, this may not be possible. It is expected, however, that with the rehabilitation of both large scale and small tea holdings in Western Uganda this crop will play a larger role in foreign exchange earnings in the future.

All four of Uganda's principal cash export crops (coffee, tea, cotton, and tobacco) still have an prices officially established by the government. The ratios of price increase for these crops from December 1980 to June of 1983 have all been about 10 to 1. This does not compare favorably, however, with the changes in the official exchange rates which have in the same period increased at ratios of 19.8 to 1 for Window 1 and 37 to 1 for Window 2. Nevertheless, the producers appear to be adequately motivated to increase production at prevailing prices, especially for coffee and tea. Calculation of estimated net returns on these crops together with the major food crops would, except for coffee, favor food crops, which do not have price controls and are more likely to respond to market conditions.

Cotton, previously Uganda's second most important cash crop, has not experienced the same rapid recovery found with coffee. The pre-season estimate for 1982/83 was for 200,000 bales, but the outcome was about 65,000. Much higher projections are being made for the 1983/84 season (est. 200,000), but due to the shortage of financing for cotton purchase, farmers are reluctant to release their crop, fearing default in payment by the cooperative buyers. With current ginning capacity of 200,000 bales per annum and a further planned development of 224,000 bales of ginning capacity being financed by World Bank and African Development Bank, there should be ample processing capacity if the cooperatives can secure financing for purchase. Further developments in cotton production and processing will provide additional cotton seed for oil extraction and cotton seed cake for the animal feed industry, a development of serious interest to this project. .

In conclusion, Uganda now has an excellent opportunity to rehabilitate and further develop its own agricultural

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production base and attempt to satisfy domestic consumer demand for such products as edible oils, poultry products, animal feeds, dairy products, and certain food crops such as sugar and rice. Recapturing markets and returning to former levels of production or increasing to even higher levels will require special attention to direct inputs and processing facilities, markets, and the managerial/technical skills required. The RPE project addresses many of these issues by focusing on the rehabilitation and/or expansion of productive activities that were previously well established in Uganda and for which there was effective consumer demand. RPE will complement current government policies directed toward encouraging the restoration of agricultural production and agro-industrial activities.

b) <u>Industry</u>.

Rehabilitation efforts in this sector have not been as spectacular to date as in agriculture. Reasons for this include: (1) physical plants were allowed to run down with inadequate repairs/replacement during 1970's, (2) management and technical expertise (often of Asian origin) was forced to leave, (3) deterioration of supporting infrastructure, and (4) shortage of raw materials and required foreign exchange.

Several international donor agencies, including the EEC, Islamic Development Bank, and IBRD have pledged funds to support rehabilitation efforts in the manufacturing sector, but progress has been slow due to administrative bottlenecks, disputes on property ownership, and security problems in major industrial areas. Reliable transportation continues to be scarce.

Whereas manufacturing's share of GDP in the monetary economy was 7.1% in 1970 and 6% in 1975, it dropped to about 3.5% for the period 1980-1982. The breakup of the East African Community further reduced the potential for regional African markets for manufactured goods from Uganda, and most manufacturing must now be oriented toward the Uganda domestic market alone. The reduction of import restrictions for manufactured and consumer goods will also require that locally manufactured products be competitive in price and quality with imported goods if they are to gain back a portion of the local market. Investments should first gravitate toward those activities where Uganda appears to have a superior comparative advantage, which now would be in the agricultural and agro-industrial areas such as sugar processing and oil extraction.

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4. The Project.

a) Overview.

The PID originally identified coffee and cotton as the major areas requiring financial support for rehabilitation efforts. During subsequent field investigations, however, it became apparent that these two commodities were being adequately supported by ADB, IBRD, and UK funds. Nevertheless, other appropriate agricultural production and processing areas were identified during field preparations for the Project Paper, which included; poultry hacheries, processing and production facilities; edible oil processing, animal feeds production, dairy production and processing, commercial fishing, and mixed farming.

All these project areas rely primarily on locally produced agricultural materials, or are engaged in direct agricultural production. They also tend to be labor intensive and job creating. Current market demand for planned project production comes from both regaining the previous market and from the natural increase in demand resulting from high population growth. Foreign exchange requirements are significant and essential, especially for capital equipment. The necessary investment capital has not been forthcoming, however, due to the ongoing liquidity problem, lack of external funding aimed at these areas, and lack of technical absorptive capacity of both credit intermediaries and the enterprises themselves. It is to these constraints, of course, that this project is directed.

b) Specific Sub-Project Activities.

Areas identified for RPE support are of an agricultural production and processing nature aimed at domestic consumption and sometimes import substitution. All activities were well developed at the time of the Amin takeover, some being primarily in the hands of Africans (fishing, farming, dairy), whereas most of the oil processing was owned and controlled by the Asian community.

During preparation of the project paper, a representative sample of the various loan categories were reviewed and site visits were made to several parts of the country. Of the loan applications submitted to the Uganda Development Bank (UDB) and reviewed by the PP team, none were adequately prepared and ready for appraisal. UDB senior management concurred. Preliminary costing and appraisals were made on several potential projects, but it was apparent that a considerable amount of preparatory work and analysis still remained before an adequate assessment of the applications could be made. The banking institutions have been reluctant to become involved in loan development of this nature, however, due to the risks inherent in such projects without adequate feasibility analyses, the lack of foreign exchange available for this area, and (according to the UDB) the fact that combining project development and appraisal functions would compromise objectivity. Cost and logistic constraints associated with feasibility work are also deterants.

For purposes of analysis, the PP team developed some representative models for the various types of loans likely to be included in the RPE project. These models provide illustrative examples of financial viability for selected enterprises. They do not substitute for what will ultimately be required by way of complete analysis of each loan application, but such analyses will only be possible when adequate technical assistance is available to assist clients in sound evaluation and planning of potential investments.

Undoubtedly there will be some changes in the profile of the agricultural lending activity during implementation, taken into account in project design, but the general focus of the effort in terms of level and nature should remain essentially valid. Changing economic conditions of the country will result in certain projects being more financially attractive than others, and undoubtedly there will be new enterprises identified during implementation. Examples follow:

<u>Poultry Production and Processing</u>

A well developed and integrated poultry production and marketing industry had previously existed in Uganda, and there is considerable interest being expressed by producers to re-establish it. Success in poultry production depends on well established feed sources, processing facilities, and adequate markets. An ample supply of day-old chicks is also required. A reasonable level of profitability can be attained if the producer has a regular market for his mature birds. With an 8,000 broiler throughput per annum, for example, breakeven would be at about 25% production. Annual profits are projected to be USh. 1.5 million giving an internal rate of return of 28.7% over 20 years on an investment of USh. 3.5 million (See Annex E., Appendix 2-A).

Although the market is in place in the urban areas around Kampala and Jinja, the capability to exploit it is presently lacking as the main processing cooperative, the Wankoko plant, is unable to operate and is in severe need of rehabilitation. A delay in processing mature broilers by as little as one week can seriously reduce the profitability of a broiler operation. The rehabilitation of the Wankoko plant, therefore, is a priority possibility for the project. The plant could be rehabilitated for USh. 100 million and would be profitable operating at half capacity. The internal rate of return would be 33%. (Annex E., Appendix 2-A).

With respect to Hatcheries, production is far below current demand in part due to inadequate equipment at existing facilities, and the shortage of foreign exchange for the importation of parent stock. Private hatcheries are planning expansion, however, as demand is such that customers are placed on waiting lists for day-old chicks. One hatchery analyzed for the PP is an operation could be made operational by the installation of a generator and the purchase of parent stock and drugs. Previous production was 4,000 chicks per week. The actual rearing of broilers and layers relies primarily on inputs available from within Uganda. An adequate building can be constructed of local materials, and the moderate climate keeps construction costs low. Medium-sized production units tend to be simple in construction, labor intensive and fit well in the high population density and small farming units around Kampala.

Dairy Production

Milk collection and marketing centers established by the parastatal Dairy Corporation are currently grossly under utilized, and prospects for reestablishment or previous processing levels appear limited. The Dairy Corporation currently pays the Government set price of USh. 20 per liter of milk delivered to the collection center, currently below the cost of production. The controlled price of milk has been increased to USh. 40, but is inadequate to encourage new investment. Even though the Dairy Corporation has a monopoly on the purchase and processing of milk for the formal market, the majority of milk now produced is sold locally through informal channels. The price of raw milk in the open market varies through the country from a low of USh. 20 per liter in the traditional production area of Mbarara to a high of USh. 100 in the Mbale area. Prices in Kampala and urban areas are generally between USh. 60-80 per liter in the open market.

A dairy farm located in an area of the country where there is sufficient market demand so that milk can be sold at USh. 80 per liter would experience a negative cash flow during the first (and possibly the second) year. The enterprise would be profitable, however, from the third year on, with a 12.9% internal rate of return on USh. 19 million investment. (Annex E, Appendix 2-B.) Dairy production should be encouraged in those parts of the country were it is a profitable agricultural activity such as around Kampala, Jinja, Mbale, and Ft. Portal. Prices in Lira, Soroti, and Gulu would also warrant investment.

Feed Mills

The lack of an adequate animal feeds industry responsive to the local market is considered by most livestock producers to be a critical constraint to increasing production and improving profitability. Demand for animal feeds is increasing due to expansion of poultry and dairy production. Ingredients for manufacturing animal feeds are increasingly available in Uganda, and the only required imported ingredient is the pre-mix concentrate. Existing feed milling facilities need to be decentralized, with scaled down capacity and using less complex milling machinery with lower capital and maintenance cost requirements. More labour intensive processing methods are warranted. Uganda also produces a surplus of cereal crops and agricultural by-products suitable for animal feed should be utilized. The current revival of cotton ginning and oil extraction will also restore cotton seed cake to the local market, an important protein source for animal feed.

Small scale feed mills (1-5 tons per hour) are low capital cost operations and energy is cheap. An illustrative model of a small feed mill derived from current market prices for inputs and capital equipment costs indicates that a mill can breakeven operating about 35% capacity on single shift. On an investment of USh. 20 million, if production increased to 67% of mill capacity by the third year and continued at that level, a 28.6% internal rate of return would be realized over 10 years. Because of the low capital cost to variable cost ratio, feedmills like this can breakeven on 800 tons per annum. (Annex D. Appendix 2-B.)

Oil Seed Processing

A recent consultant report for the USAID (Oil Seed Processing - Uganda, May, 1983) reviewed the current status of oil milling in Uganda and recommended consideration of selective investment in potentially viable operations. Most of the existing plant is low technology, labor intensive and designed for processing only cotton seed. There is a serious policy issue to be resolved, however, before any financing is provided for

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rehabilitation of oil seed milling capability. Oil production in Uganda is taxed at 70% for the domestic market which makes the resulting price higher than that for imported oil.

Estimated market demand for oil is only 25,000 tons per year at present due to high retail prices (Kampala price USh. 900 per kilogram). If total production reaches the government projected level of 300,000 tons of cotton seed per year, reserving some 50,000 tons for planting material, the remaining 250,000 tons would produce about 30,000 tons of oil. Consumer demand would increase substantially if only the retail price could be allowed to drop to its natural level.

Investment opportunities for RPE funds would potentially exist for the construction of a new facility at Gulu and rehabilitation of existing facilities at Soroti, Mbale, and Tororo. Most of rehabilitation work would be for replacement equipment and some building repairs. (See Annex D, Appendix 3 for net margin calculations on cottonseed oil processing and the internal rate of return for a proposed plant.)

C. Financial Analysis.

1. Introduction.

In the preparation of the Financial Analysis (See Annex E.), the design team reviewed both ICIs and clients with regard to capability to effectively utilize RPE funds and attempted to estimated how the project would affect viability at both levels. Much of this analysis is included in the economic and institutional sections which were prepared together with the financial. This section in particular concentrates on background and hypothetical financial soundness by means of a set of financial projections included in Annex E, Appendix I, tables 1-3. The three analyses should be read together.

2. Background.

Uganda had a previous history of a well developed banking sector during both the pre- and post-independence period up through the 1970s. Several international commercial banks, including Standard, Barclays, Grindlays and the Bank of Baroda, maintained full services through much of the country. The cooperative Bank of Uganda (UCB) also provided commercial banking services for its clients. The commercial banks catered to agricultural clientele besides their usual industrial and trade accounts.

When the GOU formed the Uganda Commercial Bank (UCB), much of the branch network of the commercial banks was taken over, and the UCB became the dominant bank together with the Cooperative Bank in rural areas. The overseas commercial banks now limit most of thier activity to Kampala, although they have retained some of their agricultural clients. The GOU is now encouraging the commercial banks to consider reestablishing branch banks. Grindlays is considering the reopening of a Jinja branch.

Recent upheavals in the financial environment of Uganda (brought about in part by the float of the Uganda shilling) have had a profound effect on the financial sector and the banking system in the country. Banks now generally face a severe liquidity crisis. Bankers attribute this partially to delays in payments from the government to various suppliers. Another factor is that outside major urban areas, the commercial banking system is not operating efficiently and most trading must be carried out on a cash basis requiring large quantities of physical cash to be available for business transactions. Recent increases in interests have not produced a noticeable increase in deposits and the situation will most likely continue if interest rates remain negative in real terms relative to the current rates of inflation.

Interest rates have been increasing relative to the rate of inflation since 1980 with the most favorable rate going to the agricultural sector (currently at 17% - still below inflation now running at about 30%), but the liquidity problem continues as so much money remains outside the system to support commercial trade.

3. Financial Soundness.

For purposes of analysis and financial projections (see Annex E, Appendix 1, Tables 1-3) the ICIs are expected to borrow the $12.5 million provided by the credit component of the project from the BOU in the form of long (20-year) term loans with ten year grace periods on principal and annual interest payments at 6.5%. In the case of the ICIs, their loans to sub-borrowers have been calculated with eight year terms and a one year grace period at 15% interest. Of the $12.5 million total, $8.0 million is expected to be channeled through the UDB.

Local contributions to the project are projected to be:

$5 million   from UDB loans rediscounted by the BOU

2.7 million from commercial bank counter part lending contributions in local currency

4.0 million from sub-borrower equity investment (minimum 25% contribution on the two amounts above plus the $ 12.5 million.

$11.5 million total in local currency.

Thus the RPE line of credit should leverage total funds for investment of about $24 million. An additional amount will be internally generated at the ICI level as principal payments to the BOU do not start until the tenth year, whereas clients will be repaying in accordance with much shorter grace periods. Under the above terms, over $3.0 million will be available for relending (for similar purposes - a covenant) from client principal and interest payments earned in excess of administrative costs, estimated to be approximately 4.25% of outstanding balance of the project portfolio. (See Annex E, Appendix 1, Table 2.)

In strictly financial terms, because the funds are initially in grant form and the BOU will assume responsibility for maintenance of value against the dollar, the financial soundness of the project can be assured by adjustments of the spread in interest rates of funds from the BOU to the ICIs and also on the rates, terms, and conditions of lending by ICIs to the client group. Smaller loans that have higher administrative costs can and should have larger spreads. This should also be done for loans that are considered to be of higher risk by their nature.

In the case of the UDB, by relending principal repayments and approximately 50% of its proposed 8.5 point spread, it could increase the total amount of its project loan fund to $11.3 million from the $8.5 million received by year 10. The amount available for lending would then start to decline as principal repayments are made to the BOU. When the total loan has been repaid to the BOU in year 20, the UDB would still have generated an additional $6.9 million in local currency as a result of the project. Similar results would be found in the other ICIs.

In the case of the Bank of Uganda, under these terms, interest payments will amount to about $2.0 million in year 4 and $4.0 million in year 6. By the end of the project, payments to the fund by all ICIs will total over $20 million.

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These calculations, of course, assume relatively low administrative and delinquency costs 4.25% at the ICI level. This is the case in the private commercial ICIs. In the case of the UDB, as can be seen in the Institutional Analysis, delinquency rates at present are horrendous. This is why between the IBRD/UNDP group and this project, so much technical assistance is going into the bank, and there are reasons to expect that the performance on the project portfolio will be relatively good - mainly based on the client group. Also most of the UDB's problems can be traced to mismanagement and unsound lending policies during the 1970s and the following period of upheaval. On the administrative cost question, the additional cost to the UDB of administering this project will be relatively minor as the institutional structure is in place and, if anything, will shrink over time through improved efficiency. Nevertheless, if deliquency or default rates approach unacceptable levels on the project portfolio (to be negotiated) disbursements will be cut off.

D. Institutional Analysis.

The institutional analysis, attached as Annex F, covers the Uganda Development Bank in depth, and to a lessor extent, Grindlays and the Uganda Commercia Bank. With the exception of the UDB, which has (in part) been pre-qualified, the other ICIs will have to undergo more comprehensive additional analysis in order to qualify for project lending. (See Criteria, Section E below, and Conditions and Covenants.) This section deals with the UDB only, as it currently stands to receive the bulk of lending resources provided by the project, despite the fact that every effort will be made to promote utilization of other, commercial alternatives. These will take time to develop, however, and can be considered during detailed planning and analysis activities of the Pre-Implementation phase.

1. The Uganda Development Bank.

a) Background.

The Uganda Development Bank (UDB) was estaolished in 1972 with an input of SH 100 million from the GOU. It was to assist in the development of asgriculture, industry, tourism, housing and commerce through the provision of short and long term loans, equity and other share investments in addition to managerial and technical assistance. It was also to administer a credit guarantee fund consisting of contributions from the GOU and other banks, for assisting marginal borrowers in raising funds from banks and credit institutions.

UDB's inception coincided with the mass exodus in 1972 of non-Ugandan citizens, and the allocation of their trading and small manufacturing business to new owners without the requisite business experience. The new owners were unable to obtain financing from commercial banks because they were largely unknown, and the UDB was requested by the government to fill the gap. At its commencement, therefore, the UDB started playing a non-developmental role as a short term commercial lender in addition to its decreed function as a multisector development bank. This along with mismanagement and other problems associated with the Amin era and the looting and destruction which occured during the Liberation war, seriously undermined the quality of the UDB loan portfolio and resulted in the lingering financial problems still being faced today.

The GOU is now attempting to build the UDB back into its major development bank with a substantial role in investment financing in Key sectors. In the future the UDB will concentrate on medium and long term development lending for commercial agriculture, medium and large industries, transport and tourism. Its role in lending to commerce and small industries has been discontinued. In productive sectors, mainly the industrial, however, it has run into a major obstacle related to continuing questions of ownership of client enterprises, and many rehabilitation loans are stil waiting for Government resolution of these disputes. This is much less of a problem in the agricultural sector.

b) <u>Structure</u>.

Appendix 6 of Annex F shows the newly created organizational structure of the UDB.

The Board of Directors is appointed by the Minister of Finance and consists of up to sevem members including the Governor of the Central Bank and the Secretary of the Treasury as permanent ex-officio members. The decree establishing the UDB stipulates that Board members whould have experience in banking and financial matters. This has been broadly interpreted, however, and a number come from bolitical backgrounds without the requisite experience. With this in mind, among other questions, AID will reserve the right to approve all loans in excess of $200,000 being financed under the project.

As part of the reorganization plan sponsored by the IBRD/UNDP project, six senior positions at the bank will be filled by expatriate personnel, as follows:

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			Department
1.	Assistant General Manager		Operations
2.	Assistant General Manager	(vacant)	Finance
3.	Chief Accountant	(vacant)	Accounts
4.	Industrial Engineer		Industry
5.	Financial Analyst		Industry
6.	Industrial Economist		Industry

The assistant general manager for operations is particularly stong and will be the chief UDB counterpart for this project. The presence of the UNDP team and the solid and businesslike capability of the assistant general manager were significant factors in the selection of the UDB as the principal ICI for the project.

In April 1984, the UDB had 58 professional staff, assigned as follows:

	Total
General Manager's Office	4
Internal Auditor	2
Operations	
Crops	6
Industry	11
Livestock	16
Research (not operational)	
Secretariat	5
Finance and Administration	
Accounts	4
Admin & Personnel	6
Supervision	4
Total	58

The above staff is broken down within individual departments in Annex F, Appendix 6.

In addition to the expatriate assistance provided by the UNDP, there is to be a program of externalf fellowships for staff training including introductory livestock, agricultural, and industrial projects courses lasting from four to six weeks for about 20 newly recruited professional personnel. Provision has also been made for sending about 12 UDB employees to eight to nine week development banking seminars in Europe.

Given the above, adequate measures have been developed to deal with staff constraints related to industrial lending. By UDB's own assessment, however, and based on a review of pending agricultural loan applications, both the Crops and Livestock Departments require considerable strengtnening, especially in financial and project analysis skills. The newly formed Department of Supervision and Recovery is also critical to successful operations and likewise requires strengthening. UDB has requested assistance in both of these areas. It is felt that both needs can be met with the TA package offered by the project, ie., one long term agricultural finance specialist and various short term consultants, in addition to two other credit specialists to be supplied by the German Government for livestock and crop production.

To further improve on the structure for project appraisal, the design team recommended that the Livestock and Crops Departments be combined into one Agricultural Department as many of the pending applications are for mixed farms and other agro-industrial activities where there is clearly overlap between the two areas and related disciplines. (See Project Description, III, D. 2., for the technical assistance plan and basic scope of services.)

c) Policies.

The UDB limits its exposure per project to the lowest of:

- 80% of the project's cost
- 20% of the UDB's net worth

The bank also has the policy of not accepting any foreign exchange risk, yet the matter is not clear with respect to certain existing credits (EEC, IDA, OPEC) between the UDB and the BOU. The issue of where the foreign exchange risk is lodged is critical and requires resolution as commitments of foreign lines of credit may soon reach $130 million (Annex F, Appendix 4). Depending on the economic sector in question and GOU pricing policies, devaluation of the shilling could substantially increase local currency debt service cost on such loans.

Under the RPE project, clients will repay loans in local currency based on the prevailing exchange rate at the time of their drawdown with no foreign exchange exposure being passed to the sub-borrower.

d) Processing and Procedures.

Some 14 steps have been identified in processing a loan application in the UDB, all of which is handled in the bank's head office. (Annex F contains complete description.) All loans eventually go to the Board of Directors for final approval. The total process takes about six months provided that proposals are not turned back for further work.

It is believed that with technical assistance and training as proposed for agricultural project appraisal and processing the process can be improved and streamlined to a degree. This will be one of the principal tasks of the short term Development Banker to arrive early in the project. Also, lower order loans or ones that become routine should not have to bo to the Board for approval.

Concerning supervision, quarterly visits are called for to each borrower. In practice, however, this has not been possible because of the security situation and transport difficulties. Clients around Kampala have tended to be adequately supervised while those in more distant areas receive almost no visits. In the future, assuming improvements in security and transport and with a strengthened supervision and monitoring staff (this project will contribute on the agricultural side) supervision should improve substantially. Further, part of the burden for this in more complex cases can be assumed by the Technical Assistance Entity to be established by the project. Where necessary, certain loans can include financing for this type of follow-up project management consulting assistance.

e) Financial Condition

(1) Prior Record

Annex F, Appendix 1 is a summary of UDB's income and expenditure statements from 1978 through the first quarter of 1984. Appendix 2 shows the balance sheets for the same period. The UDB incurred losses each year from 1978 through 1983, with a cumulative loss at 31 December 1983 of Sh 729 million. (Total share capital at the time was Sh 1,143 million.) Outstanding loans during the period has grown substantially from Sh 125 million to Sh 2,358 million, most of which took place during 1983 when the UDB began heavily utilizing foreign lines of credit. The growth in borrowings increased from Sh 9 million in 1980 to 3,241 in 1983. Appendix 3 is a historical statement of sources and application of funds.

It should be pointed out that a 70% provision for bad debts was made in 1980 which represented a potential write off of Sh 90 million, out of a total possible of Sh 134 million. Yet current experience indicates that this provision is probably excessive. Loans put on UDB's books prior to the float of the shilling can now be repaid with greatly devalued shillings, and these borrowers are voluntarily clearing old debts in order to be eligible for new loans.

As with other institutions in Uganda, the UDB suffered from the chaos of the 1971 to 1988 period. Accounting standards were poor during this period and resulted in "qualified" audits for 1980 and 1981. A primary reason for the qualifications was that the UDB could not produce a list of individual loan balances showing specific allocations for bad debts. The accounts department is now actively working on the problem.

(2) Present Position and Projections.

The draft audit for 1983 has been completed by Price Waterhouse (attached as Appendix 5) and is being reviewed by the UDB. The most noteworthy elements are as follows:

- A 16 fold increase in foreign borrowings over two years.

- A net loss for the year (1983) of Sh 473 million compared to a loss of Sh 110 million for 1982. (Significant increases in administrative expenses account in part for this. UDB is now maintaining a much larger staff than before anticipating greatly increased lending, especially in agriculture.) Another part of the loss resulted from a Sh 74 million loss in the Ranch Rehabilitation Program due to stolen goods, death of cattle, and an apparent foreign exchange loss. Finally, under the EEC line of credit, the UDB is not permitted to pass exchange risks on to the borrower. This resulted in a SH 193 loss in 1983.

- UDB's operational efficiency improved during the year and it is making progress in solving various problems and the implementation of imporoved systems.

- Concerning income, it is worth noting how the UDB accounts for interest income. The bank accrues interest only on loans guaranteed by the GOU. On other loans it accounts for interest income only when the money is actually received. The 1983 interest income from loans was SH 176 million which contained at least SH 144 million of accrued income on GOU guaranteed loans.

Appendix 4 of the financial annex shows the approximate position of UDB Industrial Department at 31 Dec, 1984 with respect to foreign lines of credit. Even with the external assistance received from the UNDP group (expatriate engineer and economist) it is not likely that the Department could responsibly administer any more credit beyond the $106 now available.

In agriculture, on the other hand, there is only one foreign line of credit - ADB II, Ranch Rehabilitation Project, for 10 million units of account (approximately $13 million) which is available to the livestock Department. This has now been almost fully disbursed, and the workload in the department is drastically reduced. No lines of credit are available to the Crops Department. These two departments now have a significant excess of staff, some of whom will be transferred to the new Supervision and Recovery Department. The RPE credit can easily be staffed from existing personnel. The constraint, rather, is in types and levels of skill on board.

An issue of considerable importance to the successful implementation of UDB's loan program is its ability to mobilize local currency. The best use of foreign lines of credit is for the importation of needed foreign goods, such as factory equipment. Yet the importation of such equipment is only part of a typical rehabilitation loan package. The installation and utilization of such equipment reuires local construction, working capital, and other uses of local currency.

In most cases the loan package from the UDB will have to include the local currency portion as well as the foreign currency. Recent estimates indicate that for every $1 of foreign eschange lent $.50 of local currency may also be required. The Industrial Department currently has foreign lines of credit totalling $106 million which theoretically would require as much as Sh 17 billion in local currency. The combined savings of all the commercial banks in Uganda, however, does not total 17 billion. Currently there is no excess liquidity in the system, in part due to reasons explained earlier under the financial analysis. There probably is, however, a fair amount of unrecorded liquidity in rural areas.

A condition to the IDA loan was that UDB share capital be increased by the government at a rate of Sh 100 million a year for three years. This has not been met. The IDA credit also provided that the first $10 million of the $30 million credit disbursed would be converted to equity in the UDB. UDB now has about $15 million worth of projects to be financed by the credit almost ready go move.

Eventually, principal and interest payments from UDB loans will be sufficient to provide the shillings needed to implement new projects planned. Yet due to the grace periods provided for in most UDB loans these loan repayments will not be significant in the initial years. For these reasons, it is necessary to secure the local currency part for the project through the proposed rediscount facility provided by the BOU. The liquidity is just not in the system to begin with.

(3) Loan Recoveries

UDB's success as an ICI will depend on its ability to properly appraise and supervise loans and keep defaults to reasonable minimums. Considerable effort is now underway in upgrading and streamlining UDB operations. The past gives little indication of what UDB's performance is likely to be in the future as the bank is going through a period of substantial transformation.

Nevertheless, current information at UDB indicates that all the changes and upgrading that has been taking place at the bank has not yet resulted in an improvement in loan recoveries. Because of grace periods, very little of UDB's loans have any principal due, yet interest is to be paid. Taking into account that about 82% of 1983 interest income was accrued, but not collected and the uncollected interest (Sh 133 million) on other loans (not guarangeed by the GOU) this percentage increases to 90%.

UDB financial performance for the first quarter of 1984 also indicates poor recoveries. During the quarter UDB expected loan recoveries (principally from interest and delinquent loans) of Sh 339 million. Actual recoveries were less than Sh 5 million.

The Supervision an Recoveries Department needs to be substantially improved before UDB will be a viable self-sustaining institution. The strengthening process is still underway. If UDB can not improve its recovery rate, funds currently planned for onlending through UDB should be channeled through other ICI's The Project Loan Agreement with the BOU should stipulate certain performance targets in terms of delinquency and default rates permitted which if exceeded would result in suspension of disbursements.

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2. Other ICIs

Much more limited analyses were carried out on Grindlays bank and the Uganda Commercial Bank (See Annex F) Summaries are not included here as much more complete analyses will have to be made before any loans are channeled through these or any other banks outside of the UDB. It is worth noting, however, that both these banks offer real possibilities, especially Grindlays early in the program, and commercial bank participation will be encouraged to the extent possible.

3. Conclusion.

The selection of UDB as the principal ICI, despite various negative financial performance indicators above, was based on the following factors:

- o The Cooperative Development could not be utilized due to a conclusions regarding its financial condition.

- o The UDB is the only public sector institution with the mandate and the structure to work with the AID selected target enterprise group - ie., small to medium agriculturally based enterprise with a need for investment as opposed to commercial, shorter term lending.

- o The IBRD/UNDP team at the UDB, in this case, is a real plus in terms of the positive impact it can have on overall management and systems improvement. AID can have more impact at lower cost working with this group due to the greater concentration of effort resulting from the combined effort.

- o The Uganda Commercial Bank is a possibility, is being promoted by the Government, and will be considered as a potential lender under the project. It is now, however, geared for the type of lending contemplated, being focussed primarily on short term commercial credit. There are also unresolved financial and absorptive capacity questions with this bank.

With respect to the other commercial banks, chiefly Grindlays, the USAID is very interested in having them participate. None at this point would be willing to take the lead, however. They will wait and see and make their own determinations on the basis of detailed packages once they have been firmed up and become available. Such a role for the commercial banks would almost certainly not be acceptable to the GOU either, at least not initially.

E Lending Criteria.

Lending criteria is still illustrative and will be refined during the detailed planning and negotiating stage of the project and submitted for approval by AID as a part of a condition precedent to disbursement for the credit component. Described below are certain minimums, however.

1. ICI Eligibility

- The ICI must be a legally chartered bank or financial institution authorized to operate in Uganda with an established program of lending to private enterprise.

- The ICI must be able to demonstrate adequate staff, operating procedures, and financial condition to satisfy AID as to its ability to lend responsibly under the terms of the project.

- The ICI must be prepared to abide by AID policy, program and project criteria as summarized below for the sub-borrower group, which, among other things, implies a solid analytical appraisal capability in terms of sub-project eligibility, feasibility and viability.

Note that in the case of the UDB, it has, in effect, been partially pre-qualified through analysis carried out during final design. Further, technical assistance is being provided to the UDB, in part, so that it will be able to comply with established criteria, especially in terms of appraisal capability. Other lenders will have to present detailed evidence, satisfactory to the BOU and to AID, that they have the capability and the commitment to comply with criteria, norms, and standards required by the project.

2. Sub-Borrower Eligibility.

- Borrowing enterprises must be Ugandan owned and controlled with their principal place of business in Uganda.

- All project assisted enterprises (including cooperatives) must be in the private sector and be profit making ventures. In the case of cooperatives, PVOs, or otherwise non-profit making enterprises, they must be able to demonstrate that they are seeking to maximize net returns and to capitalize for further investment and growth.

- All enterprises must primarily operate in the agricultural sector, either in production or processing or service activities directly linked (forward or backward) to agriculture.

3. .Sub-projects Eligibility.

One of the following key conditions must be met:

- Labour intensive (maximum of $6,000 per job created),
- Have clear potential for import substitution or export,
- Provide increased markets, inputs, or service for agricultural production based on locally available inputs.

4. AID Program/Policy Criteria.

the following AID program and policy criteria at a minimum will be met:

- adequate planning and costing [Section 611 a)],
- environmental soundness with protective or mitigating measures where necessary (See Environmental Analysis, following section).
- financial soundness - adequate projected rates of return,
- technical soundness - appropriate technology to be employed),
- social soundness - adequate consideration of equity concerns, and
- managerial competence to execute the project in accordance with the approved terms and plan of the loan.

With respect to any of these criteria, sub-borrowers may receive assistance, if necessary, from the technical assistance entity described earlier, either by choice or as required by the lending ICI in order to receive the loan. Sub-borrowers, of course, will be free to seek out any source of assistance they choose to meet the above criteria, but they must meet it in order to qualify.

It should also be noted here, that any loan for a total amount of over $200,000 of project funding will be directly approved by The AID mission director.

E. Environmental Considerations

1. General Environmental Categories

In general, small-scale industries in developing countries do not have severe environmental impacts, simply because of their small size. However, exceptions exist in the form of larger agro-industries where amounts of organic waste are produced in excess of the capacity of the local sewerage system. Exceptions also occur when a small enterprise produces toxic, obnoxious or contaminating compounds that could pose health threats or degrade the environment. Thus a small electroplating plant, tannery or textile plant could be considered a very small industry but could still have far-reaching negative impacts on the local environment.

In order to assure that the environmental effects of all activities to be financed by this project are thoroughly reviewed in accordance with their potential for environmental harm, and to assure that activities which have significant potential for harm are identified (regardless of the size of the activity in monetary terms), a system for classification of loan applications is proposed below which provides ascending levels of environmental review depending on size of activity and potential for environmental harm. In the present project, prior to evaluating any loan against the RPE criterion for "environmental soundness", the ICI and/or the USAID-funded technical services team should assess which category the loan will fall into. The general categories are briefly described below and should be easy to apply. However, if any doubt exists, either the USAID or the Prime Contractor advisory group can call on the services of the in-country Environmental Advisory Committee (as described in Attachment I of the IEE in the PID).

Class I Enterprises.

Those enterprises which are small-scale enterprises producing non-toxic substances (e.g. chicken hatcheries, small dairy farms, farm input and equipment supply, etc.) Rehabilitation of these enterprises in most cases will involve repair or replacement of parts for existing equipment with average investment per enterprise anticipated to be in the $25,000 range.

Class II Enterprises

Any enterprise (especially agro-industries) producing large amounts of organic waste or organic effluents capable of exceeding the capacity of local sewage treatment plants, would be classified as Class II. Several small and large Class II agro-industries have already been assesssed for organic waste production and effluent loads. This assessment was carried out earlier by the Envrionmental Advisory Committee (see Attachment IV of IEE in PID). This assessment showed that most of these agro-industries will be producing organic wastes that can be treated by rehabilitation of present waste pits or digging new or larger oxidation ponds in order to treat the larger quantities of wastewater expected.

Class III Enterprises

Small or large enterprises where toxic wastes or industrial effluents are expected (as opposed to the mostly organic wastes typical of agro-industries) should be included in Class III. A good example of Class III would be the EMCO industrial site mentioned in the EAC Assessment (Attachment IV of IEE in PID). This enterprise will be producing a mixed industrial-agricultural effluent which will need a proper wastewater treatment facility. Practical guidelines, such as the UN/ESCAP Guidelines for industrial pollution control in tropical countries will be available for use in preparation of environmental assessments. These ESCAP guidelines are available with the EAC for: fertilizer, sugar, distilling, starch producing, electroplating, tanning and fish processing industries. Guidelines will be available later for other industries, and will be kept on file with the EAC.

2. Environmental Review Procedures

a) Class I Activities

The Regional Environmental Officer (REO) will be sent copies of all loan application which are placed into Class I by the implementing ICI's. The REO will screen these applications to determine the appropriateness of the classification of the activity and to identify any activity which, regardless of classification, may have a significant adverse effect on the environment. No special environmental analysis would be required with loan applications for Class I activities and no environmental assessment of the activity would be undertaken, unless the application reflects an aspect of the activity that is likely to have significant adverse effect on the

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environment. In the latter case, the ICI involved will be advised to reclassify the loan application for environmental review purposes and it would then be processed as indicated below.

b) <u>Class II Activities</u>

Loan applications for Class II activities will be required to include an enrironmental review (ER) along with plans especially for treatment of waste. Where the loan applicant cannot carry out such an (ER), the technical services team will call on the services of the EAC. (<u>Note</u>: an environmental review (ER) differs considerably from the environmental assessment (EA) called for in Class III activities. An ER is a brief review of the most obvious environmental impacts (usually waste disposal) along with practical suggestions as to how the impacts can be resolved. Several good examples can be seen in Attachment IV of the IEE in the PID).

The REO will review such applications to insure that they are adequate in respect to the provision of waste treatment facilities and that no other aspect of the activity is likely to have a significant adverse impact on the environment. For loan applications in Class II, which require financing under $200,000 (i.e. below the AID approval level), the environmental section of the loan application (the ER) will be reviewed by the REO who will provide recommendations for modifying the activity, if need be. The environmental review section for Class I activities that require loans of $200,000 and over will be reviewed and approved by the Mission Director as part of the AID loan approval process with advice, as required, from the REO. Loan provisions will provide for periodic monitoring specialists, such as might be provided by the technical assistance contractor or the EAC, evaluation by GOU and AID and a requirement to correct any deficiencies discovered as the result of such monitoring or evaluation. Sanctions, will also be included, such as non-compliance penalties, suspension of loan disbursement, or loan repayment acceleration for failure to put adequate waste treatment facilities into operation.

c) <u>Class III Activities</u>

In loan applications for Class III activities (regardless of funding level) the applicant will be required to include detailed plans for an adequate waste disposal plant based upon an environmental assessment (EA). This will be included with the application. (<u>Note</u>: An environmental assessment (EA) is a detailed study, usually undertaken by consulting companies and follows the detailed instructions set down in Reg 16 (Section 216.6), a copy of which is on file with the EAC). The environmental aspects of the design, operation and monitoring program for this plant will be reviewed and approved by the Mission Director as part of the AID loan approval process. It is expected that all loans for activities in this class will exceed $200,000 and therefore will be subject to AID approval. Later agreements would be required to contain the same special provisions regarding monitoring and rectification of deficiences as provided for in the case of Class II activities. The effluents in the case of both Class II and III must meet those standards set by the Uganda Water and Sewerage Corporation prior to start-up.

d) Pesticide Activities

Any loan application where pesticide use is contemplated, (regardless of amount or category) will have to include a risk-benefit analysis as called for in Reg. 16 (Section 216.3b). A copy of Reg 16 which will be on file with the EAC. This analysis will be reviewed in the same manner as prescribed above for review of the other environmental aspects of the loan application.

e) In all of the above activities the Environmental Advisory Committee (EAC) in Kampala at Makerere University will be available to assist the ICIs and the technical service team in:

(1) reviewing all loan applications;

(2) assigning applications to their proper environmental class;

(3) carrying out environmental reviews (ER's) for Class II loans where necessary;

(4) advising applicants on availability of consulting firms capable of carrying out environmental assessments (EA's) for Class III loan applications; and

(5) possibly participating in the preparation of EA's where practical.

3. Funding.

Funding and and consulting time is available for the provision of services to assit the ICI applicants and the technical assistance advisory team to review the environmental aspects of loan applications submitted.

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4. Covenants and Conditions

It is recommended that the following covenants and conditions precedent to disbursement be included in the Project Grant Agreement:

a) A Project Grant Agreement covenant requiring that the Government of Uganda require the implementating credit institutions to develop procedures for making sub-loans under the project that include the environmental analysis and review procedures outlined above;

b) A condition precedent to disbursement providing that AID funds will not be disbursed to an implementing credit institution or a loan applicant for a loan or loan-financed activity under the project until the environmental analysis and review procedures outlined above are completed;

c) The Government will covenant an agreement to require implementing credit institutions to include the following conditions/covenants in each sub-loan agreement :

(1) With respect to all Class II and Class III activities, a covenant whereby the borrower agrees that production operations will not commence until adequate facilities for organic and toxic waste treatment are in place and whereby the borrower agrees to a right of inspection by the representatives of the lender, GOU, or AID to insure compliance with, and the adequacy of, any environmental design requirements or environmental protection facilities agreed to as part of the loan approval process.

(2) In the case of large industrial operations which will receive loan funds in increments, a condition precedent to receipt of subsequent increments of loan funding requiring evidence that satisfactory progress has been made on installation of waste treatment facilities and verification (by initial monitoring) that the design of the facilities is adequate.

5. Summary.

A negative determination is proposed here for Class I activities. The threshold decision for Classes II and III will be deferred and will be made by the Mission Director at the time of approval of the loan application.

Note: This section on environmental considerations was prepared for inclusion in the Project Paper by REO (Gaudet) and RLA (Scott), REDSO/ESA.

G. Social Soundness.

The full social soundness analysis, found in Annex G, reviewed the two principal components of the project, ie., ICI strengthening and enterprise development. A number of real and potential constraints are pointed out and means of addressing them noted or recommended to improve the project's sociocultural feasibility. Presented here are the main conclusions only.

1. With respect to the ICI (UDB) component, a combination of strategies was recommended, including; a) the placement of a long term expatriate technical assistance team outside the bank to support bank clients (sub-borrowers from the project), b) direct technical assistance and training to the UDB in critical areas to increase effectiveness and outreach, with particular emphasis on training for middle and junior level staff to address problems of staff inadequacy and low morale. c) a sensitive approach, full explanation and gradually introduction of changes in organization and procedures to minimize resistance.

2. Important points of the lending loan component included; a) encouragement of competition in industry. b) pursuit of a bias for employment generation through labor intensive agricultural and industrial development loan criteria, c) an on-the-job management training program to build up a cadre of Ugandan managers, d) Attention to greater geographic dispersion of loans for political as well as economic reasons, and e) the building of self-interest in the financial viability of enterprises through the broadening of boards of directors where possible and by encouraging investment by entrepreneurs, employees and/or cooperatives in their respective firms.

Note: This Social Soundness Analysis in Annex G. was based on the original draft written for the RPE Project a year ago when the principal ICI was to be the Cooperative Development Bank (CDB). Subsequently, the target enterprise mix of the project likewise evolved to a degree from the original, heavily export oriented, somewhat higher economic level group. The greater beneficiary population, however, remains fairly similar to the original, although, there is now a greater emphasis on somewhat more dispersed directly productive agricultural enterprises rather than the primarily agro-industrial cash export crop processing level as was initially proposed. If anything, the social soundness of the project, in terms of its equity and spread effect, would appear to have improved under the new design.

PART V: IMPLEMENTATION ARRANGEMENTS.

A. Administrative Arrangements.

1. Government of Uganda.

a) Grantee and Executing Agency.

The Ministry of Finance is the designated grantee for this project and will sign the Grant Agreement on behalf of the Government of Uganda. The Bank of Uganda (central bank of the country) will be nominated as the official implementing agency.

b) Policy Direction and Mechanisms for Oversight and Supervision.

To accomodate the need for national oversight and a vehicle for policy level intervention when necessary, it was decided that a high level, inter-agency project committee should be established which would meet periodically to review progress, provide policy guidance, and deal with major actions and difficulties as they arise. The committee, to be organized by the Ministry of Finance and chaired by the Bank of Uganda, is to consist of the following representatives or their designees:

Governor of the Bank of Uganda - Chairperson

Permanent Secretary, Ministry of Finance - Member

Permanent Secretary, Ministry of Planning - Member

Representative of the national Chamber of Commerce - Member

Representative of the Uganda Development Bank - member

Representative of the Commercial Banks - Member

USAID Mission Director - Member

Bank of Uganda Project Manager - Ex-officio Member

The committee is expected to meet quarterly, although it may be convened for extraordinary sessions as warranted by the Governor of the BOU. Tentative terms of reference for the committee include:

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- Review and set overall policy direction for the project relative to national plans and priorities.

- Review and approve annual and longer term plans for the project including the overall plans for Phases I and II.

- Review quarterly progress reports prepared by project management, and respond, where necessary, to situations requiring actions at this level. Project representatives may make special presentations where warranted or called for by the committee.

- Facilitate inter-agency coordination where necessary for effective execution of project activities.

- Facilitate public/private sector understanding and collaboration (government ministries, ICIs, and the Sub-borrower group).

- Formulate new policies and take other actions to further effective pursuit of project objectives and enhance impact.

- Consider strategies to mobilize additional resources for project related lending or other activities

- Resolve disputes, where necessary and appropriate, between participating agencies or groups

- Respond to unforseseen problems or constraints which may arise.

Another vehicle for oversight will be quarterly audits performed under contract to the USAID which will provide independent audit coverage of all project lending operations including both ICI and sub-borrower performance and compliance with project criteria and requirements. Audit reports will be provided to the Bank of Uganda and the USAID and shared as appropriate with other participating entities.

c) <u>Project Management and Administration</u>.

Project management responsibility will be officially rest with the Director of the Department of Development Finance (a non-voting member of the oversight committee), or his designee, who will have full delegated authority to act in behalf of the BOU on project related matters including the signing of

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official documents. The Project Manager will be directly responsible for:

- overall supervision and monitoring of project activity for the Bank of Uganda,

- general liason with his counterpart project manager in the USAID on all project related matters,

- the preparation and submission of necessary documentation such as that required to satisfy conditions precedent and covenants,

- agreement on terms of reference for project contracts and participation in contractor selection procedings,
- review of periodic ICI and prime contractor reports and action requests and in turn reporting to the BOU, the USAID, and/or the oversight committee as necessary with respect to actions taken or required in response,

- approval, management and monitoring of BOU loans to project ICIs in accordance with the terms of loan agreements,

- the timely provision of counterpart local currency resource commitments to the Uganda Development Bank through the vehicle of the BOU's rediscount facility, and,

- other duties and actions as required to further successful project implementation.

It is expected that the BOU project manager will be heavily involved in project actions during the 18-month start up phase of the effort. Once the prime contractor is on board, however, and systems are in place and operating, the need for such heavy involvement should diminish substantially. The project is designed in such a way as to place as much responsibility as possible at the level of the prime contractor and participating ICIs for greater efficiency and reduced burden on both the central government and the USAID. Such functions as the certification of invoices for payment, referral of sub-borrowers to the technical assistance entity, etc., will take place at the lower level. The project manager will receive periodic audit reports of project operations and may raise issues and intervene at any time in response to identified questions or problems.

2. The Intermediate Credit Institutions.

a) The ICIs as a group.

The ICIs as a group will each be responsible for management of ongoing project related operations in accordance with the terms of loan agreements signed with the BOU and such other instructions as will be issued from time to time by the BOU and the USAID. All will apply established sub-borrower and sub-project criteria, report quarterly to the BOU and the USAID (using negotiated formats), refer clients where necessary to the technical assistance entity, refer sub-loans for approval by the USAID when required (over $200,000), provide copies of all sub-project proposals to the Prime Contractor and the USAID to meet environmental review requirements (see IV, G.), and generally be responsible for effective communication and coordination of activity with involved agencies including participation through a selected representative on the oversight committee described earlier.

With respect to the disbursement of sub-loans, the foreign exchange component of each loan will be referred to the Procurement Services Agency in accordance with procedures described in the procurement plan, (Section C below), while the local currency component will be handled in line with current operating procedures of the Bank in question as modified by BOU loan agreements. Obviously, the two lines of credit should dovetale in terms of timing, terms etc., which will be adequately described in sub-loan agreements.

b) The Uganda Development Bank.

In addition to the above, the UDB as the lead ICI under the project and a major recipient of technical assistance, will have a variety of additional responsibilities.

The project manager and chief liason on the part of the UDB will be the Assistant General Manager for Projects and Operations, a position currently filled with the highly regarded expatriate chief of the IBRD/UNDP team, who will coordinate on an ongoing basis with project managers for the BOU, the USAID, and the Chief of Party for the prime contract. He will be responsible for compliance with project conditions and covenants on the part of the UDB and for approval and support of technical assistance and training initiatives provided by the project. In addition he will review and agree on terms of reference for contract advisors, studies and training activities, manage the sub-loan review and approval

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process while assuring compliance with project lending criteria, submit original loan requests, drawndown requests, and local currency rediscount requests to the BOU on the basis of approved sub-loans, provide quarterly reports to the USAID and the BOU in accordance with established formats etc. Many of the tasks, of course, will be delegated, but he will be the person responsible. Finally, he will serve as primary liason with the project for the IBRD/UNDP team and the IDA industrial development project in general.

At the working level, the counterpart of the AID contract advisor will be the Chief of the newly created Agricultural Department who will report to the above Assistant General Manager. He will be responsible for appraisal of all sub-loan proposals to be funded by the project through the UDB, the adequate application of project criteria to each, referral of clients where warranted and in collaboration with the advisor to the Technical Assistance Entity, and for implementation of approved appraisal procedures developed by the project. In collaboration with the Assistant General Manager, he will also assist in general liason and coordination with other departments of the bank in pursuit of project objectives.

3. The USAID.

a). General.

Due to USAID staff limitations, as described below, the project will be implemented as much as possible through the prime contractor. The USAID role, with the exception of the initial start up period, will be limited as much as possible to required approvals of loans and other major actions to be accomplished by the Contractor and participating agencies. All procurement (sub-project financing), for example, will be handled through the PSA element of the Prime Contract. AID will also have the monitoring tool of quarterly audit reports in addition to other quarterly reports from ICIs and the Prime Contractor. Nevertheless, additional ongoing project management duties will include:

- liason and coordination with BOU project management and participating ICIs,
- general administration, and provision of policy guidance to the Prime Contractor,
- financial management including the approval and monitoring of expenditures,

- periodic site visits to sub-projects,
- coordination of project activity with the rest of the USAID's portfolio in Uganda and program planning and development activity in general.

In addition to the above duties, existing delegations of authority place with REDSO/ESA the responsibility for providing financial, legal, contracting, engineering, environmental and commodity assistance and approvals. REDSO will play an important role in this case with respect to sub-loan approvals when there are engineering and or/environmental factors to be considered. Other sub-loans may be referred for REDSO review or assistance as necessary depending on the nature of the sub-project. AID's Regional Financial Management Center (RFMC) in Nairobi will act as controller for the project and process project related payments.

During the initial pre-implementation phase of the project, despite structural attempts to minimize the management burden, there will be substantial demands placed on the small USAID staff. For this reason, an additional six person months of pre-Prime Contract consulting assistance has been built into the project to assist with establishment of administrative arrangements and the meeting of conditions precedent. The question of USAID capacity to manage the project is further treated below.

b) USAID Capacity Analysis.

For reasons beyond its control the USAID must operate with a serious direct hire staff constraint, ie., one project officer responsible for the entire portfolio, one agricultural project manager already tied up with two other major ongoing projects, a program officer, an assistant program officer for evaluation, and an agricultural economist in addition to a minimum of administrative support personnel.

With the commencement of implementation of this project, the Mission will have four active bilateral projects including; Food Production Support (617-0102), Manpower for Agricultural Development (617-0103) and Oral Rehydration Therapy (617-0113). The first two of these represent traditional AID management commitments, similar to this project. The ORT burden, however, should be modest as the project will be implemented almost entirely through UNICEF with the USAID's input limited to funding, procurement of a single commodity, and relatively minor participation in certain study and evaluation elements.

With respect to management of this project, for the first six months, approximately, the USAID will dedicate the majority of the time of its US direct hire project officer to the effort. A local hire Ugandan assistant project manager (currently working in the agricultural division of the USAID) will gradually phase into assuming more and more of the administrative burden of the project on an ongoing basis; while the US project officer, of necessity, will have to turn more to responding to other generalized demands of portfolio management and the development of new project initiatives. It is worth noting here that the Foreign Service National to be involved is an economist with a banking background. He was previously employed by the Bank of Uganda as purchasing manager and currency officer and is knowledgeable of the institution's internal operations. The USAID will shortly hire another FSN project manager to replace the above employee with his previous work in the agricultural division.

4. Prime Contractor Considerations.

Given the responsibility to be vested in the Prime Contractor, the contract element of the project will be the most crucial factor impacting on implementation accross the board. This cannot be over emphasized. Contractor solicitation and selection, therefore, will receive priority attention by the USAID from commencement of the project.

a) Contract Structure.

Chief of Party

Project Appraisal ICI Strengthening

Sub-Borrower Strengthening

Procurement services

There will be four principal components of the Prime Contract as follows:

(1) The Chief of Party (COP): The COP will be overall manager of prime contract activities. He will be administratively separate from the other units and without specific technical duties in order to allow time to adequately administer overall operations (a very substantial task in itself) in addition to being

able to retain objectivity with regard to elements of the contract which may well have competing interests and priorities. He or she should have substantial experience in executive management positions in third world (preferably Africa) settings. A background in finance, banking and credit systems development, agriculture and agro-industry, and data and information systems would all be very helpful; but the single most important factor will be demonstrated executive capability and judgement.

(2) Project Appraisal and ICI strengthening: A major unit of the contract will be dedicated to technical assistance and training for the Uganda Development Bank for the strengthening of its project appraisal, approval and monitoring capability. This will involve one long term advisor and various short term consultants. (See Project Description, Section III, D. 2.) This component will also coordinate with other ICIs to assure that project lending criteria are satisfied.

(3) The Technical Assistance Entity and Sub-borrower Strengthening: This will be the most heavily loaded component as it represents the true thrust of the project. Three long term advisors will work with a contract hired Ugandan staff of professionals to provided critically needed technical feasibility and management services support to agricultural enterprise clients of the credit system being developed. (See Project Description, Section III, D.3.) A very important element of this component will be design and execution of a scheme for the development and eventual spin off of the Ugandan side of the entity as a viable enterprise in its own right.

(4) Procurement Services Agent (PSA): All procurement (both off shore and locally in Uganda and Kenya) under the financing component of the project (up to $12.5 million in sub-loan financed equipment, materials and spare parts) is to be channeled through the PSA element of the Prime Contract. As such this unit will be of critical importance to project execution and will need to consist of a US operation linked (contractually or otherwise) with a similar firm or arm with offices in Kampala and Nairobi. The PSA is expected (although not required) to be a joint venturer or sub-contractor to the Prime. The USAID recommends a minority set aside firm for this element. (See Procurement Plan and Waiver section below.)

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b) Contract Mode, Solicitation and Selection.

For various reasons an AID direct mode of contracting is to be utilized for the Prime Contract utilizing standard unrestricted AID procedures for technical services contract solicitation. The USAID is interested in the widest and most open competition possible for this contract due to its demanding nature and critical importance to the project. The one exception is that the USAID urges that a firm registered with AID's Office of Business Relations (small and disadvantaged businesses) be considered as a joint venturer or sub-contractor for the Procurement Services element.

The request for proposals (RFP) will allow bidders to bid alone, or as a consortium, joint venture, or a single contractor with specified sub-contractor(s). Overall management of the contract will be awarded to a single contractor. The contract will be awarded for up to three and one half years, to be renewed for two to three additional years, based upon the major evaluation to be conducted in the first half of the last year of Phase II, ie., 1988. The RFTP will cover in detail the functional areas required for Phase I activities and will clearly outline the need for Phase II follow-on work.

As the REDSO/ESA contracting officer staff appears to be fully committed on other priority actions during the period when procurement and negotiations for this contract are expected to take place, the process will probably have to be managed by the Office of Contract Management (SER/CM/ROD/AFR) in AID/Washington. Regarding selection, however, an RFP evaluation committee will be formed consisting of representatives from the USAID, the GOU (probably one each from the BOU and the ICI group) and one or more appropriate staff persons from AID/Washington and/or REDSO/ESA. Depending on availability and timing, the chairperson will probably be either the USAID's project officer or a representative of the East Africa Projects Division (AFR/PD/EAP) of AID/W. Following initial review of the proposals and establishment of a competitive range, some of the members of the panel may visit the sites of selected finalists. Bidders will also be encouraged to visit Uganda prior to submitting proposals in order to adequately take into account the operating environment and constraints which they would have to face during implementation. Upon receipt of best and final offers from these firms, contractor selection will be made.

5) Other Contracts

Two other contracts will be executed during implementation of this project as follows:

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a) Auditing.

An auditing contract will be solicited from amongst those qualified firms which have or could have a permanent presence in Kenya and/or Uganda. The selected firm is to operate in a form totally independent of the Prime Contractor or participating agencies and will report solely to the USAID. The terms of reference will include quarterly auditing of project lending activity with corresponding reports to USAID project management. These reports will be shared with the Bank of Uganda and other project agencies as appropriate.

The contractor will audit for compliance with accepted national and international standards of financial performance as well as satisfaction of project criteria as specified in Implementation Letters issued by the USAID and in loan agreements at both the ICI and sub-borrower levels.

Solicitation and award of this contract is expected to be managed by the REDSO/ESA Contracting Officer staff, as this will be a less taxing and time consuming exercise than the one discussed above for the Prime Contract. Also, proposals are expected primarily from firms already located in Kenya and East Africa.

b) Evaluation Contract

Separate contracts will be let for evaluations in the last years of both Phases I and II. (See Evaluation Plan, Section D below.) Each contract is expected to run approximately six weeks with up to four specialists on each team. Procurement is expected to be handled by REDSO/ESA.

6. Disbursement Procedures.

In terms of implementation vehicles under the project, there are basically two major elements, namely; a) the provision of technical assistance and services, and b) the procurement of commodities under the credit/financing component. With this in mind and in accordance with payment verification policy guidance issued in December 1983, proposed payment procedures are as follows:

a) Technical Assistance:

The direct payment (direct reimbursement) procedure will be utilized for all technical services under the project including both the Prime Contract and smaller contracts for auditing, evaluation and pre-implementation assistance services. There will also be a small amount of funding set aside, approximately $30,000, for international volunteer services associated with sub-project studies such as from the International Executive Service Corps. An additional small amount may be used for observation travel during the first year of the project for a group of UDB officials to visit the National Development Bank of the Philippines.

b) Commodity Procurement.

As explained earlier and below in the procurement plan, a Procurement Services Agent (PSA) under the Prime Contract will be responsible for all procurement under the credit component of the project. The financing of the agent's fee will be by direct letter of commitment. For U.S. and code 935 procurement, however, FM/BFD will issue a bank letter of commitment with the PSA as approved applicant. The PSA will instruct the designated bank to issue Letters of Credit to suppliers to whom awards have been made. In the case of Kenya and Uganda procurement, direct letters of commitment will be issued or awarded, semi-annually, by RFMC to cover estimated procurement required for the coming six month period. This will coincide with proposed semi-annual requests for drawdown by ICIs under the project from the Bank of Uganda. (See project description, Section III, D. 4., The Financing Component.) A summary Table is shown below (format drawn from referenced policy guidance):

Methods of Implementation and Financing

Implementation Method	Method of Financing	Approximate Amount ($000 - Non inflated)
TA - Pre-Implementation Services	Direct Payment	75
TA - Prime Contract	Direct Payment	10,385
TA - Audit Contract	Direct Payment	400
TA - Evaluation	Direct Payment	160
TA - Volunteer Services	Direct Payment	30
Commodity Procurement	Direct L/Com Bank L/Com	12,500 "

Note: With respect to Commodity Procurement, it is not possible at this point to determine how much will be by direct and how much by bank L/Com. This will depend on the mix of off shore and shelf item procurement in country. See Section III. E., Financial Plan, for inflated costs plus contingencies.

5. Procurement Plan - Commodities.

a) Items to be Procured.

Likely procurement requirements will be for items such as food processing machinery, animal stock, building materials and machinery equipment related to agricultural service industries such as feed milling and bagging. Equipment, materials and spare parts will be purchased for the rehabilitation of such agricultural and agro-industrial enterprises as dairy farms, hatcheries, poultry farms, feed mills etc. The source of individual items will vary depending on the availability of supplies from the local market (including Kenya). Precise details and specifications for both local and US procurements will be developed by the Procurement Services Agent (PSA) to be contracted by the project and who will provide all necessary purchasing services under it, including items such as vehicles in support of the technical assistance side of the effort.

b) Responsible Entities

The Grantee and the USAID both prefer to have a non-GOU Agency directly responsible for all procurement activities. Also, because of limited procurement experience and the lack of existing services of this nature to support clients, the ICIs (UDB and Grindlay's thus far) would prefer not to be directly involved in the project procurement function. With this in mind, and due to limited staff resources within the USAID, it is proposed that all procurement be accomplished by a PSA under the prime contract. (See Annex C for draft scope of work of PSA)

c) Source and Origin.

As Uganda qualifies as a Relatively Least Developed Country (RLDC), the officially authorized source and origin for all project goods and services will be the US, Code 941, and the cooperating country. A major exception to this is warranted by project circumstances, however, as noted in the Waiver section below.

d) Methods of Procurement

The procurement of commodities will be accomplished under the policies set forth in Chapter 19 of Handbook One, Supplement B. Kenya will be regarded as a local cost source under the

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extended shelf items rule. Except for motor vehicles, it is not anticipated that any items discussed in Chapter 4, Section C of Handbook one, Supplement B, "restricted Commodities" will be financed under this project. Specific waivers will be requested for any vehicles not covered by the blanket waiver for light vehicles which has been requested for projects in Uganda.

Most procurements under the lending activity of the project will be for over $5,000 but less than $100,000 in value. The PSA acting for and together with private sector sub-borrowers will be expected to follow good commercial business practices and use informal (negotiated) procurement methods for these purchases. Specifically, proforma invoices will be obtained from a reasonable number of prospective sources prior to procurement implementation. In addition, local procurements will be consistent with Ugandan laws and practice. For individual procurements exceeding $100,000, formal competitive bidding procedures will be followed, with the USAID retaining its right to approve the issuance of IFBs and related contract awards.

e) Waivers

A blanket waiver request to allow the purchase by sub-borrowers of items of Geographic Code 935 source and origin of up to $17.35 million is included in Annex C, Waivers. This is due to a design team estimate that up to 120 sub-borrowers under the project for the most part will be rural based and dispersed with little access to procurement information on commodities other than those normally available in the vicinity of the enterprise. Likewise, maintenance and repair services will only be available for equipment normally in use in the area, and few, if any, of the commodities likely to be imported by sub-borrowers are currently imported by Uganda from the United States. Visits to rural areas by USAID personnel confirm the general non-availability of US equipment and spare parts in these areas. (See Waiver Request for more detailed justification.)

In addition, Annex C includes a request for a certificate of non-availability of US shipping. This will exclude from cargo preference rules any shipment of commodities not originating in the United States. Also included is a request to allow shipping costs of up to $3.0 million to be financed on Code 935 vessels.

f) Schedule and Delivery.

It is planned that major procurement under this program will not be initiated until the Prime Contractor and the PSA are on board, at least one year into project implementation. If any sub-loans can somehow be approved before then, the USAID will assume direct procurement responsibility in accordance with above provisions and project lending criteria.

Off shore suppliers will be required to provide all risk marine insurance in the amount of 120 percent of commodities and similar insurance for inland freight.

B. Implementation Plan.

1. Pre-Implementation.

The critical path for start up of this project follows the line for procurement of the Prime Contract, as it is not expected to be possible under the proposed structure of the project and lending criteria to be able to commence the financing activity until the Prime is on board and functioning. It should be noted here that the USAID is anxious to make a very few early loans to enterprises currently in critical need. Possibly these can be realized through short term pre-prime contract assistance from alternative sources. Conditions precedent will still have to be met, however, projects appraised, additional feasibility work carried out, procurement services arranged etc.; and it is expected that by the time these loans are ready to move the Prime Contract may be about ready to commence in any case.

For ease of presentation, the plan for procurement of the prime contractor is presented first. Then other start-up activities are shown. Phase I and II are then presented in very limited detail in order to avoid engaging in excessive fiction. Detailed planning remains to be carried out on the basis of agreements to be reached among participating agencies and contractors as shown below. The plan is assumed to commence with the signing of the Grant Agreement, anticipated to be in mid July 1984, given that the PP will not arrive in Washington until the end of the first week in June and it will need to go to the Administratore for approval.

a) The Prime Contractor.

o Preparation of PIO/T with complete scope of work is carried with REDSO/ESA and/or short term contract assistance assistance. (Substantial analytical and drafting task) and forwarded to AID/W. (USAID project officer returns to post o/a July 15.)

Target: Aug 15, 1984

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- RFP is prepared and issued by AID/W as soon after end of fiscal year as possible. (No new contract actions will be accepted this fiscal year.)

  Target: October 30, 1984

- Proposals received in AID/W. Sixty days will be allowed.

  Target: December 30, 1984

- RFP evaluation committee convenes in Washington.

  Target: January 15, 1985

- Evaluation committee completes review and establishes competitive range.

  Target: January 30, 1985

- Panel completes visits to highest ranked contenders and agrees on final ranking.

  Target: February 15, 1985

- Contracts office commences negotiations with highest ranked contender.

  Target: February 28, 1985

- Contract signed by AID/W. (Note that negotiations for this contract will be a substantial task given its multifacited nature and the fact that it will probably envolve two or more sub-contractors or joint venturers.)

  Target: May 30, 1985

- Contingency factor: 30 days. Revise contract signing date.

  New Target: June 30, 1985

- Initial short-term group consulting group from Prime Contractor for detailed planning and contract implementation arrangements arrives in Uganda

  Target: August 1, 1985

- Planning and implementation arrangements complete. This is expected to involve several different trips of various long and short term people over a period of about four months while contractor is gearing up for full mobilization. During this period the contractor will be simultaneously working on; a) housing and office arrangements, procurement for the resident team effort (vehicles, furnature, office equipment computers, etc.) and other administrative aspects of its own mobilization and b) groundwork (initial studies and surveys, development of detailed work plans, recruitment of Ugandan staff etc.) on the Technical Assistance Entity, UDB, Data Management and financing/procurement components. (Substantial pre-mobilization funding has been provided for such an effort and the RFTP should indicate that this will be expected in order to minimize delays and be able to make a January 1, 1986 target for commencement of Phase I in earnest.)

Target: November 30, 1985

- o Full mobilization. Contractor is on board for the duration in Kampala and systems are operating.

Target: December 31, 1985

b) Other Pre-Implementation Activities.

(1) Conditions Precedent - TA.

Beyond routine conditions such as names and specimen signatures, important conditions precedent which must be met before the signing of the Prime Contract include; establishment of the high level project oversight committee along with its groundrules, the consolidation of the Crops and Livestock Departments within the UDB, and a statement from the GOU that it is in accord with the establishment of the administratively separate Technical Assistance Entity and the plan for its eventual independence. The meeting of these conditions, with the assistance of the USAID project officer and short term assistance as necessary from pre-prime contract consultants and REDSO, is expected to require approximately six months from the date of the grant agreement. Three extra months are added here for likely slippage.

Target: April 30, 1985

(2) Conditions Precedent - Lending.

These conditions will be somewhat more taxing than those for technical assistance, but for a substantial portion of the period when these are being developed, Prime Contractor personnel will be on hand to assist. The principal ones are; a) the development and approval of an operating procedures manuel for the project which will incorporate complete ICI, sub-borrower, and sub-project criteria, plus guidelines and procedures for lending operations at both ICI and sub-borrower levels, and b) a minimum of one completed loan agreement between the BOU and an ICI (probably the UDB). It is expected that these will be completed within 12 to 17 months of the signing of loan agreement depending on the level and quality of effort made by the BOU and participating ICIs, follow-up work by the USAID and the timing and effort of the Prime Contractor. In any case, they are not expected to drag into the Phase I operating period.

Target: December 31, 1985

(3) <u>Other Pre-implementation Activities</u>.

Other activities during this period include: selection and award of the auditing contract which must take place in advance of any actual lending activity, observation travel of ICI officials to the Philippines, and possibly initial advisory services either by international volunteer experts such as from the International Executive Service Corps or short term consultants brought in by the USAID to try and get a few loans off the ground early. The timing and feasibility of these possible initiatives will depend on initial planning and negotiating by the USAID and on availability of staff time.

2. <u>Project Operations - Phases I and II</u>.

a) <u>Phase I</u>

On the basis of the advance work discussed above, it is assumed that Phase I (officially commencing on January 1, 1986) will start with all systems in place and operating. That is, sub-project appraisal will commence in earnest at least in the UDB, the Technical Assistance entity will start providing feasibility study and management assistance to sub-borrowing entities and initial data collection work will be underway. On this basis, the project loans are expected to be approved within three months. (Note that the average time from application until loan approval in the UDB is six months, but a number of asnticipated sub-project loans are already in the system, and it is expected that some advance work can be done on these. In the case of the commercial banks, the process is much more rapid. Grindlay's is expected to commence lending immediately.)

By the end of the first quarter of the last year of Phase I, or March 30 1988, the data management component of the project will have completed a thorough analysis of project operations up to that point (See III, D. 5.) plus all special studies, and have a package of comprenensive material ready for the forthcoming independent evaluation.

The Phase I evaluation will commence in April, 1988 and be completed by the end of June. On the basis of the findings of that evaluation, the redesign and detailed planning exercise for Phase II will be carried out over the following three month period, primarily by the Data Management Office with inputs as needed from other elements of the contract, the USAID and participating agencies. This exercise will culminate in the production of a major Project Paper supplement, to be approved by the USAID, with REDSO/ESA's concurrence for the funding of Phase II.

b) <u>Phase II</u>.

No attempt is made here to project timing and execution of Phase II activities as these will depend entirely on the results of the above analytical efforts. See Phase II elements of the project description for overall targets and tentative descriptions. A major evaluation will likewise take place in the last year of Phase II in 1991 which will hopefully lead to the replication of valuable experience in other settings and ongoing international resource mobilization for Ugandan agricultural enterprise.

C Evaluation Arrangements and Plan

Ongoing evaluation activities are an integral and critical part of this project through the Data Management Component. The success of the project in terms of its ability to adjust to emerging conditions and lessons observed hinges on sound data collection and analysis over time. The ability of credit systems strengthened to mobilize additional lending capital will depend in substantial measure on adequate analysis and evaluation of problems, progress, impact etc.

The Data Management Component is described in Section III, D. 5. of the Project Description. As mentioned in the preceeding section, separate and independent evaluations are to occur early in the final years of Phases I and II - 1988 and 1991 respectively.

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For purposes of implementation, the most important evaluation will obviously be the one at the end of Phase I, as detailed planning for the remainder of the project will draw from it. It should be of unusually high quality given the magnitude of quality of effort that will be directed to preparaing data for it, including time series data on lending, institutional strengthening, and the client group in addition to a number of special studies that will feed into the mix to be considered. It will also consider contractor and USAID performance in implementing the project and make recommendations on both. The final product will include a comprehensive set of analytically support recommendations for project redesign and implementation for Phase II.

The final evaluation will consider the entire project with an emphasis on Phase II and result in a well documented basis for replication and/or use of experience gained in other programs in Uganda and other countries. It should also be very useful in additional resource mobilization.

The evaluations are expected (and have been budgeted) to be carried out by teams of three people (finance, agro-industry, and social science or some similar mix) over a period of approximately two months each.

D. Proposed Conditions and Covenants.

In addition to standard conditions precedent and covenants the USAID plans to include the following in substance in the agreement to be signed with the Ministry of Finance:

1. Conditions Precedent.

a.) General and Prior to First Disbursement for Technical Assistance.

The Grantee will furnish, or cause to be furnished, in form and substance satisfactory to USAID, evidence of:

(1) The establishment of high level, inter-agency project committee to provide for national oversight of the project's execution and to serve as a vehicle for policy level intervention when necessary. The evidence submitted should provide terms of reference and operating procedures for the committee.

(2) The establishment, or intention to establish within a satisfactory time period, of a consolidated agricultural

projects appraisal department within the Uganda Development Bank which will draw from the existing crops and livestock departments. ("Intention" may suffice, as short term consulting assistance from a development banking expert is programmed to assist the UDB in the regoranization plan, structure, operating procedures, etc. .)

(3) Government approval of the plan to establish an independent technical assistance entity by the end of Phase I. The evidence should indicate approval of the concept and the substance of the proposed plan for arriving at the independent enterprise. The evidence should also indicate approval of the initial establishment of the technical assistance entity under Prime Contractor.

b) <u>Prior to First Disbursement for Lending</u>.

The Grantee will furnish, or cause to be furnished, in form and substance satisfactory to USAID, evidence of:

(1) An established rediscount facility in the Bank of Uganda, to be utilized by project ICIs, Particularly the Uganda Development Bank, for securring the local currency counterpart contributions required for the sub-lending program. Terms, conditions, and operating procedures for access and drawdowns from this facility should detailed.

(2) The establishment of a special account for repayments by ICIs of Project loans which are to be relent for purposes in accord with project criteria in general. (Note: Possibly this should be a covenant. Reflows during the project period will be interest only, but will be substantial nevertheless. It is not expected that the condition can be inforced beyond the project period for lack of monitoring capability once project has terminated. This same condition should be stipulated for ICIs in the case of sub-loan reflows.

(3) The development of an officially approved operations manuel for the lending component of the project including credit policy and regulations and lending criteria for ICIs, sub-borrowers, and sub-projects. This will also include procedures for complying with AID's environmental regulations and for referring proposed sub-loans to AID for approval with respect to AID's, project, program, policy and legal requirements. (Note: USAID will probably need to provide direct and consulting assistance to the Grantee to meet this condition, which will be possible both prior to

and once the Prime Contract has been signed.) (Also, please see the conditions and covenants stipulated above under the Environmental Considerations, PART III, F)

(4) Signed loan agreements with ICI's to participate in the lending activity. (Once a loan agreement is signed with one ICI, lending may commence through that particular ICI. New loans may be signed over the live of the project, each to be approved by AID, as each new ICI applies to participate in project lending activity. The loan agreements will stipulate compliance with project lending criteria and provide for terms and conditions acceptable to AID.)

(5) Acceptance of negotiated ongoing maximum levels of delinquency and default rates at both ICI and sub-borrower levels of over a stipulated period in age, over the life of the project. It will be further accepted that if such rates exceed the agreed upon levels (in either or both the ICI in question and the sub-borrower group) disbursements for lending through that ICI stopped until the BOU and the USAID are satisfied that the rates have dropped below the levels in question and that adequate measures have been taken to avoid future occurrences of the problem.

(6) Statement that imported commodities will be exempted from import duties and inspection fees etc. (With respect to shelf items of over $5,000, import duties and fees will have to be removed somehow, or reimbursed to the project.)

c) <u>Proir to Phase II Disbursements</u>.

Prior to Phase II disbursements for either Technical Assistance or Lending, the Grantee and the USAID will agreed on detailed plans and costs for Phase II project execution on the basis of the findings of the comprehensive evaluation to be carried out in the last year of Phase I.

2 <u>Covenants</u>.

The grantee will covenant that, unless AID otherwise agrees in writing, it will:

(1) Assure that proposed sub-loans for an amount exceeding $200,000 in USAID financed costs will be submitted to the USAID for approval prior to disbursement.

(2) Assure that the USAID receives copies of all sub-loan proposals in general for purposes of information and monitoring.

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(3) Absorb the maintainance of value risk (devaluation) associated with project lending, ie., all project loans will be denominated in local currency at the time of commitment or disbursement.

(4) Attempt to reach agreement with commercial ICIs interested in participating in the project with respect to a combination of interest rates and a possible local currency credit guarantee scheme which will allow such ICIs to project a satisfactory return to their participation at an acceptable risk.

(Note: A credit scheme is being developed by the Bank of Uganda to encourage commercial lending for agricultural development. At the moment, the amounts to be covered are so low that it would not serve the interests of this project in particular. The commercial banks, on the other hand, have indicated that they will require a guarantee on that portion of their sub-loans not to be covered by sub-borrower contributions of "local cover." Finally, the design team is not convinced of the utility of the guarantee scheme, believing that a sound way to handle the risk question is through lending rates which adequately take risk into account with the establishment of appropriate reserves by the lender etc. In any case, it is believed that the commercial banks will participate without a guarantee if they are allowed to borrow and charge at rates commensurate with the risk and project a reasonable profit; hence covenant proposed above.)

(5) Make its best efforts to:

- resolve the edible oil ex-factory tax question in a manner condusive to the development of the local industry and production for the Uganda market.
- resolve disputes over ownership of private enterprises soliciting credit for sub-projects under the project.
- provide and maintain qualified counterpart personnel on a timely basis in the UDB.

E. Negotiating Status of Project

At the time of PP preparation the project had been discussed with the Government, particularly with the Department of Development Finance of the Bank of Uganda, for over a year.

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Detailed discussions have also been carried out over a number of months with the principal ICI, the Uganda Development Bank. Discussions at a somewhat less intense level have also been carried out with Grindlay's and to a lessor degree still with other ICIs.

As the Project Paper was prepared in final in Nairobi in order to use REDSO production facilities and confer with appropriate experts, and as the deadline for authorization was fast approaching, it was not possible to return to Uganda and negotiate the project in final form. This will be carried out by the USAID Director, with assistance from REDSO, once the final version of the paper has been received on June 6, 1984. This should allow time for possible problems to surface prior to authorization which is not expected to take place until close to the end of June 1984. Major difficulties are not expected to occur, however, as the Bank of Uganda is on board with the structure, concept, approach and basic modus operandi of the project. A Government Request for Assistance is attached as Annex F to this paper.

REHABILITATION OF PRODUCTIVE ENTERPRISES

ANNEXES

A. Logical Framework
B. Project Checklists
C. Waivers
D. Economic Analysis
E. Financial Analysis
F. Institutional Analysis
G. Social Soundness Analysis
H. Government Request for Assistance

USAID UGANDA

JUNE 1984

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ANNEX A

LOGICAL FRAMEWORK

I. Goal Structure of Project.

A. Program Level Goal:

Provide a package of assistance interventions which will lead to rehabilitation, recovery and development of private (including cooperative) enterprise within the Agricultural sector resulting in improved income, employment and quality of life in general.

B. Project Goal

Make available medium to long term financing for investment in high potential agricultural enterprise.

C. Project Purpose

Develop viable, self-sustaining systems, for the effective absorption of investment credit by agricultural enterprise, in essence, to improve absorptive capacity and managerial capability for the effective exploitation of both externally mobilized and locally available resources.

D. Conditions Expected at the End of the Project

1. System Super-structure and Capitalization

The project aims to establish a viable, two tiered credit system for agricultural investment in terms of lending, ongoing capitalization and expansion. By the commencement of Phase I, the structure should be established although lending will not have commenced in any significant degree.

Phase I: By the end of Phase I, the system should be operating smoothly in terms of lending at both BOU and ICI levels, although only very modest capitalization or reflow activity will have taken place due to the grace periods built into both credits at both levels. Additional resource mobilization should be taking place on the basis of track records established.

Phase II: By the end of the project, substantial other donor resources for agricultural investment should also have been mobilized and disbursed through the systems established by the project. Expanded operations should be meeting demand accross the board.

2. <u>ICI Capability and Effective Participation</u>.

The objective is to arrive at a set of lending institutions and programs capable of satisfying the need across the board for investment financing in the agricultural enterprise sector.

<u>Phase I</u>: UDB and Grindlay's Bank effectively lending to all contemplated types of agricultural enterprise. Other banks will have experimented with some loans financed by the project on a pilot basis, i.e. Barclay's, Standard, and the Uganda Commercial Bank.

<u>Phase II</u>: Four or more major banks effectively lending for agricultural enterprise investment on a country-wide basis. An effective outreach capability will have been developed through branch operations or mobil units.

3. <u>Volume of Lending</u>

<u>Phase I</u>: Cumulative total of Project Credit Extended will be at least $6.0 million.

Annual Lending levels in the final year of Phase I will be $3.0 million.

<u>Phase II</u>: Total of project credits extended: $13.9 million.

4. <u>Viability/Efficiency of Lending</u>

<u>Phase I</u>: Cost of lending to agricultural enterprise for capital received on concessional terms (AID Financed) will be established at a sustainable level within margins received.

<u>Phase II</u>: Cost of lending for capital received on both concessional and commercial basis will be reduced to what can be covered effectively by the spread. ICIs will be undergoing sustained expansion on basis of earnings from lending operations.

5. <u>Resource Mobilization and Capitalization</u>

<u>Phase I</u>: By the end of Phase I a track record will have been established plus demonstrated absorptive capacity of

both borrowers and lenders such that additional major donor resources will be directed to the sector of on the order of $ 5 million per year projected for the commencement of Phase II.

Phase II: By the end of Phase II the needs of the assisted sector will be totally met from a combination of concessional and commercial sources of credit plus savings or retained earnings within the target community of enterprises and lenders (estimated to be on the order of $ 8 to 10 million per year by the end of the project).

6. Sub-borrower Strengthening and Enterprises Launched

Phase I: During Phase I at least one of each type of project contemplated will have been financed and assisted. A core group of successful ongoing projects will have been established to serve as examples for replication and from which to draw experience and data. A total of at least 40 projects will have been financed of which about 50% should have completed the investment and be successfully operating.

Phase II: By the completion of the second year of Phase II, all project funds will have been drawndown and invested in viable projects in the target sector. By the end of the project, all project financed investments will have been completed. Of these a substantial number should represent additional investment opportunities for internal or other commercial sources of capital. Enterprise management within the sector will have been substantially improved.

7. The Technical Assistance Entity

Phase I: By the end of Phase I the TA entity will be able to cover all local currency operating costs through fees received from sub-borrowers under the project. There will also be a core staff of five trained Ugandan professionals working full time in the areas of financial socio-economic and technical feasibility analysis.

Phase II: By the end of the project, the unit will be completely on its own as a viable firm or indigenous PVO dedicated to agricultural enterprise management and technical consulting available for the general public and for use by the donor community.

8. Lessons learned and analytical foundation developed for Expansion and Replication

Phase I: By a point in the middle of the last year of Phase I, the analytical foundation will have been developed for major other donor resource mobilization, and detailed planning for Phase II expansion of investment activity will have been completed.

Phase II: By the end of the project a fully documented analytical history together with a comprehensive final evaluation will have provided the basis for replication of successful elements of the project in other comparable countries of Africa in addition to serving as an invaluable instrument for public and private sector investment planning and resource mobilization upon termination of AID and other donor assistance to the target sector.

E. Purpose Level Assumptions

1. The project will receive strong policy level support from the GOU (Bank of Uganda, Ministries of Finance, Agriculture, and Cooperatives, and the Oversight Committee to be established.) There is reason to believe this will be the case due to reform measures implemented over the past three years.

2. Private banks will participate as anticipated in the project due to attractive lending margins offered. Grindlay's will be the first. Others should become involved once they observe successful participation by Grindlay's.

3. The IBRD/UNDP effort to improve operating systems at the UDB will be successful. The technical assistance team is very strong and operating in line positions. The Assistant General Manager is especially outstanding. (See UDB Institutional Analysis).

4. Target enterprises will be willing to borrow for technical services received.

5. The security situation in Uganda will gradually improve.

II. Outputs of Project.

A. Overall System Development and Capitalization

By the commencement of Phase I, all arrangements will have been made and agreements finalized for BOU lending to the Uganda Development Bank and Grindlay's. Agreements with other commercial banks are not expected until a year or more into Phase I, although they could come earlier. A proposed guarantee scheme for commercial lending to the agricultural sector will also be operational, and special accounts will have been established in the BOU for project associated disbursements and reflows. The system will be ready to commence project operations. Sub-project lending is expected to commence within six months of the commencement of Phase I by both the UDB and Grindlay's.

By the end of Phase I, the reflow account in the Bank of Uganda for the foreign exchange component of the lending activity will have accumulated to approximately $600,000 in local currency from interest payments. (Principal payments to the BOU are not programmed to start until the 11th year.) By the end of Phase II the balance of the account will have arrived at $2,900,000 with total outstanding loans amounting to approximately $13,900,000. In addition, over the life of the project, some $11.5 million in local currency will have been mobilized and invested from the local currency components of loans and equity contributions from sub-borrowers. Thus, the more important output will be achieved of capitalization of an ongoing source of lending capital for agricultural enterprise. This, when complemented by other donor assistance expected in Phase II and beyond capitalization at ICI and sub-borrower levels, should effectively meet demand for the indefinite future. Approximately 120 projects are expected to be financed over the LOP. (See description of Financing Component, Section 4, below.)

B. ICI Strengthening and Capitalization

1. The UDB

Almost all technical assistance and training for ICIs under the project will be directed to the UDB through which 65% of project funds are expected to be channeled. Other ICIs may be provided with modest levels of short term assistance in the process of getting them involved with the project, and they will probably participate to a degree in some in-country training activity. At the present stage of project planning, however, there is no basis for describing institutional outputs outside of those targeted for the UDB. These are as follows:

By the end of Phase I a consolidated (crops and livestock) agricultural division will be functioning as an effective integrated unit capable of adequately appraising almost all types of agricultural enterprise proposals anticipated in the Ugandan setting.

By the end of Phase I sound loan processing and credit management procedures will have been fully developed, tested, revised, and formalized as part of official bank policy for the long term. In this area, the project will have to coordinate carefully with IDA and UNDP efforts to improve these functions throughout the bank.

In terms of volume, the agricultural division will be capable of processing all applications in a timely period after receipt, i.e., two to four weeks, at an anticipated level of approximately eight per month by the end of Phase I.

The quality of appraisal and supervision will be such by the end of Phase I that outstanding delinquent balances on loans processed by the Division will be held to less than 5% of the portfolio balance. (Does not apply to the UDB portfolio as a whole.)

By the end of Phase I, the efficiency of UDB lending in average cost per loan will drop significantly and further yet during Phase II. Calculation of these targets will await detailed planning and analysis by the Contractor.

2. Other ICIs

Grindlay's Bank should be participating actively in the project with a portfolio of outstanding loans to be target group of approximately $1,200,000. One or two other commercial banks will have experimented with project lending on a pilot basis by this time. By the end of Phase II there should be at least three commercial banks heavily involved in agricultural enterprise lending, both with project and other resources.

C. Sub-Borrower Strengthening (The Enterprises)

1. The Technical Assistance Entity

By the commencement of Phase I, the entity will have been established and staffed with expatriate advisors by the US Contractor and an estimated core group of 5 Ugandan professionals in financial analysis, accounting, business management, agro-industry, marketing etc. It will be operational and providing assistance to initial sub-borrowers.

By the end of Phase I, the entity will have been legalized as a Ugandan enterprise and able to act as a legitimate private consulting agency in the capacity of either a profit making or private and voluntary organization. By this time, all local costs of the entity will be covered on an ongoing basis by user fees and a capitalization process will have commenced leading to complete financial independence prior to the end of the project.

By the end of Phase II, all US assistance will have been withdrawn and the entity will be totally independent as a viable enterprise. By this time the organization will have a direct hire staff of eight to nine professionals capable of covering all estimated types of management and technical consulting needs of the sector, with the exception of the largest of the industrial enterprises linked to agriculture. By then, however, there should be other firms capable of addressing the needs of this higher level group.

2. Enterprises Strengthened

A minimum of 40 to enterprises will have been assisted by the end of Phase I in feasibility and project design assistance for financing proposals. An additional 20 - 25 enterprises will have received business management assistance associated with project financed investments, for some of which such assistance will be provided over an extended period of time to assure successful launching of the new operation. (Most but not all, of these will be from the same group that received proposal assistance.)

By the end of Phase I it is estimated that 40% of the organizations assisted will be able to carry out their own analyses in the future for the development of additional financing proposals.

By the end of Phase I, 100 persons from these enterprises will have participated in management training, feasibility study and other short courses carried out by the technial assistance entity! An additional will have been sent for short courses in the United States or third countries and/or on observation travel.

D. Financing.

1. Loans Made:

Up to approximately 200 loans are expected to be made over the five year life of estimated project lending activity. The majority of these will fall between $50,000 and $100,000 in terms of the AID financed foreign exchange component in 1984 dollars. The average loan is calculated at approximately $85,000. In accordance with the projected disbursement schedule based on estimated absorptive capacity of lenders and sub-borrowers (See Institutional and economic Analyses) projected lending targets are as follows:

	Phase I			Phase II	
Year	1	2	3	4	5
Disbursements: ($000)	1,250	2,075	2,700	3,325	3,150
Loans Made:	20	33	43	53	50

2. Jobs Created:

A total of some 2,000 jobs are expected to be created as a direct consequence of project lending based on an estimated average cost of per job of approximately $6,150.

3. Sub-projects to be Financed:

An illustrative list of sub-projects to be financed under the project is as follows:

20 Dairy Farms
6 Hatcheries
40 Poultry Farms
10 Feed Mills
10 Fishing enterprises
20 Mixed Farms
xx Undetermined but substantial number of smaller enterprises (mainly financed by the commercial banks for new equipment)

Exactly what portion of these will be financed in Phase I or II is difficult to predict at this time. It is also certain that a variety of new possibilities will be developed during early years of the project for both rehabilitation and new enterprise.

In addition, the project expects to finance a relatively few larger enterprises long in need of rehabilitation such as the Wankoko poultry processing plant ($300,000 loan) and up to four oil mills (3 for rehabilitation and one new plant representing a total investment of up to $3.5 million). (See Appendices to Financial and Economic Analyses Annexes.)

E. Data Management, Analysis, Evaluation and Planning

1. Phase I

Base Line Information re sub-borrowers, sub-projects, ICIs and the technical assistance entity

Periodic reporting of indicators showing progress or lack thereof from base line toward project objectives and targets.

Detailed operational reporting for purposes of sub-project tracking, implementation monitoring, trouble shooting etc.

Special analyses or studies for purposes of policy formulation, strategy development, activity planning, programming of human or financial resources, coordination, identification and sharing of innovation etc.

Base material for the detailed planning of Phase II

Useful material for capital resource mobilization from external donors and lenders as well as private capital markets.

2. Phase II

Hopefully, all of the above will continue to apply to Phase II in addition to a detailed final evaluation which will provide the basis for replication of models developed by the project in other settings and which will leave the Ugandan project community (BOU, CIs, sub-borrowers, support entities) with a firm analytical basis for new and still more effective long range planning.

III. Inputs.

See corresponding sections of Project Description and Financial Plan.

IV. Means of Verification

See Data Management section of Project Description - III.D.5.

Annex B

PROJECT ASSISTANCE

Revised for FY 84 2/21/84

5C(1) - COUNTRY CHECKLIST

Listed below are statutory criteria applicable generally to FAA funds, and criteria applicable to individual fund sources: Development Assistance and Economic Support Fund.

A. GENERAL CRITERIA FOR COUNTRY ELIGIBILITY

1. FAA Sec. 481; FY 1984 Continuing Resolution. Has it been determined or certified to the Congress by the President that the government of the recipient country has failed to take adequate measures or steps to prevent narcotic and psychotropic drugs or other controlled substances (as listed in the schedules in section 202 of the Comprehensive Drug Abuse and Prevention Control Act of 1971) which are cultivated, produced or, processed illicitly, in whole or in part, in such country or transported through such country, from being sold illegally within the jurisdiction of such country to United States Government personnel or their dependents or from entering the United States unlawfully?

NO

2. FAA Sec. 620(c). If assistance is to a government, is the government liable as debtor or unconditional guarantor on any debt to a U.S. citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) the debt is not denied or contested by such government?

NO

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3. FAA Sec. 620(e)(1). If assistance is to a government, has it (including government agencies or subdivisions) taken any taken which has the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property of citizens or entities U.S. beneficially owned by them without taking steps to discharge its obligations toward such citizens or entities? — NO

4. FAA Sec. 532(c), 620(a), 620(f), 620D; FY 1982 Appropriation Act Secs. 512 and 513. Is recipient country a Communist country? Will assistance be provided to Angola, Cambodia, Cuba, Laos, Vietnam, Syria, Libya, Iraq, or South Yemen? Will assistance be provided to Afghanistan or Mozambique without a waiver? — NO

5. ISDCA of 1981 Secs. 724, 727, 728 and 730. For specific restrictions on assistance to Nicaragua, see Sec. 724 of the ISDCA of 1981. For specific restrictions on assistance to El Salvador, see Secs. 727, 728 and 730 of the ISDCA of 1981. — NA

6. FAA Sec. 620(j). Has the country permitted, or failed to take adequate measures to prevent, the damage or destruction by mob action of U.S. property? — NO

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

Yes, this project will only fund agricultural enterprises

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

Yes, title has to be free before loans are made

c. FAA Sec. 660. To provide training or advice or provide any financial support for police, prisons, or other law enforcement forces, except for narcotics programs?

YES

d. FAA Sec. 662. For CIA activities?

YES

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

YES

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f. FY 1982 Appropriation Act, Sec. 503. To pay pensions, annuities, retirement pay, or adjusted service compensation for military personnel?	YES
g. FY 1982 Appropriation Act, Sec. 505. To pay U.N. assessments, arrearages for dues?	YES
h. FY 1982 Appropriation Act, Sec. 506. To carry out provisions of FAA section 209(d) (Transfer of FAA funds to multilateral organizations for lending)?	YES
i. FY 1982 Appropriation Act, Sec. 510. To finance the export of nuclear equipment, fuel, or technology or to train foreign nationals in nuclear fields?	YES
j. FY 1982 Appropriation Act, Sec. 511. To aid the efforts of the government of such country to represss the legitimate rights of the population of such country contrary to the Universal Declaration of Human Rights?	YES
k. FY 1982 Appropriation Act, Sec. 515. To be used for publicity or propaganda purposes within U.S. not authorized by Congress?	YES

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ANNEX C

WAIVERS

Attached are:

Annex C-1:	Draft Request for a waiver of US Source/origin requirements from AID Geographic Code 941 to Code 935 for commodity procurement under the Lending Component of the project.
Annex C-2:	Draft Request for a waiver of US Source/Origin requirements from AID Geographic Code 941 to Code 935 for shipping of commodities procured to Uganda.
Annex C-3:	Draft Request for a Determination that US flag carriers are not available for shipments from non-US sources to Uganda.
Annex C-4:	Draft Scope of Work for Proposed Procurement Services ASgent under the Prime Contract.

ANNEX C-1

DRAFT ACTION MEMORANDUM FOR THE ADMINISTRATOR

SUBJECT: Source/Origin Waiver Request - Commodities

Problem: Your approval is requested for a waiver of U.S. source/origin requirements from A.I.D. Geographic Code 941 to A.I.D. Geographic Code 935 for the procurement of approximately $17,350,000 of equipment, materials, and spare parts by intermediate credit institution sub-borrowers under the Rehabilitation of Productive Enterprises Project (617-0104).

a) Cooperating Country: Uganda

b) Nature of Funding: Grant

c) Description of Goods: Equipment, materials, and spare parts for private agricultural production, processing and service enterprises

d) Approximate Value: Up to $17,350,000

e) Probable Origin: Europe or Japan: (A.I.D. Geographic Code 935)

f) Probable Sources: Kenya, Europe, Japan, Uganda

Background: The goal of the Rehabilitation of Productive Enterprises (RPE) Project is to make available medium to long term financing for investment for agriculturally based enterprises in Uganda. Achievement of this goal will directly contribute to USAID and Government of Uganda (GOU) strategic objectives of rehabilitation and development of the agricultural sector resulting in improved income and employment for Uganda's rural population. Project objectives will be attained through the provision of credit and technical assistance to intermediate credit institutions active in Uganda who will in turn relend to benefiting enterprises. Additional technical assistance and training will be provided to participating enterprises through a separate entity to be established for this purpose. A total of $17.35 million in medium to long term funds will be provided by AID through the Central Bank of Uganda to intermediate lending institutions for on-lending to enterprises to be assisted at prevailing rates of interest. Agricultural production and processing ventures are the most likely to borrow under the project.

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Since the project will be implemented through intermediate credit institutions and loan decisions will not be made prior to project authorization, no specific list of required commodities can be established. However, studies carried out during project design do allow broad estimates of the procurement requirements.

USAID estimates that some 120 sub-borrowers will wish to procure up to approximately $17.35 million of equipment, materials and spare parts of Code 935 but non-Code 941 origin. Likely reprocurement requirements are for items such as food processing machinery, animal stock, building materials and machinery and equipment related to agriculture service industries such as feed milling and bagging. The project sub-borrowers for the most part will be rural based and dispersed with little access to procurement information on commodities other than those normally available to the vicinity of the enterprise. Likewise, maintenance and repair services are available only for equipment normally in use in the area. Uganda imports from the U.S., including items financed by military and aid programs, account for less than 3.0 percent of total Ugandan imports. Few, if any, of the commodities likely to be imported by sub-borrowers under the project are currently imported by Uganda from the United States. Visits to rural areas by USAID personnel confirm the general non-availability of U.S. equipment, machinery, and spare parts in these areas.

Discussion: Given the likely procurement needs of project sub-borrowers, application of U.S. source and origin requirements to sub-borrowers procurement would have negative project implementation implications for sub-borrowers, intermediate credit institutions, and A.I.D., with little tangible benefit to U.S. exporters. Application of normal source and origin requirements are likely to reduce significantly the participation of sub-borrowers in the project for the following reasons:

- Needed goods of U.S. and developing country (Code 941) source and origin are not normally available to the rural sub-borrowers from locally known and accepted commercial suppliers. To the extent that appropriate commodities could be made available, substantial additional time and cost would be required to obtain these commodities. Sub-borrowers paying market interest rates are unlikely to be willing to incur these additional costs.

- Maintenance and repair of Code 941 commodities, if not already available and generally used locally, will be

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difficult, if not impossible, and certainly more costly to the sub-borrower. Even if the sub-borrower is willing to incur additional maintenance and repair costs, the risk of having to shut down operations for an indefinite period of time because of the lack of spare parts may well incline the potential sub-borrower away from the project.

The following considerations make a Code 941 procurement requirement undesirable from A.I.D.'s point of view as well:

- Because of the difficulty small, rural borrowers would have in procuring and maintaining Code 941 commodities, a Code 941 requirement would significantly bias the project's lending toward larger, urban-based sub-borrowers, which would be undesirable from both social and economic perspectives.

- Because of the difficulty in repairing and maintaining equipment not routinely available in the vicinity of the investment, project-assisted investments would be less sustainable than would otherwise be the case, thus weakening the potential long-term impact of the project.

- Given the nature of U.S. exports to Uganda, most commodities required by the project would need a waiver in any case. Granting such waivers on a case by case basis would place a severe and unnecessary burden on sub-borrowers, the intermediate credit institution and AID, without significantly altering the composition of the total import list.

- As was demonstrated by the Impact Evaluation of the Entente Fund African Enterprises Project 1/, a Code 941 procurement requirement for lending to rural private enterprises through a number of credit intermediaries is difficult or impossible to monitor and implement in the African context. The referenced project was unable to meet even a 15% Code 941 requirement. The impact evaluation concluded that the Code 941 requirement was an impractical and unworkable condition of the Entente Fund loan and strongly urged that remaining Code 941 requirements be waived.

The conclusion of the AID project design team following project feasibility analysis, was that application of a Code 941

1/ "Assisting Small Business in Francophone Africa". The Entente Fund African Enterprises Program, AID Project Import Evaluation No. 40, December, 1982.

source/origin requirement to the Rehabilitation of Productive Enterprises project would make the project unfeasible. It would discourage sub-borrowers from borrowing, reduce the long-term impact of the sub-loans, be difficult or impossible for A.I.D. to monitor in full accordance with its responsibilities, and have little positive impact on U.S. exports to Uganda in any case.

This waiver authority will also be used for the purchase of "shelf items". Shelf items are defined (Chapter 18, Section A4 of Handbook One, Supplement B), as items that are normally imported and kept in stock, in the form in which imported, for sale to meet a general demand in the country for the item; they are not goods which have been specifically imported for use in an AID-financed project. Inasmuch as the value of imported items is greatly enhanced if they can be made immediately available to the sub-borrower, it is important that items previously imported and on hand in Uganda (and in Kenya, under the "extended" shelf item rule) be also made accessible to the sub-borrower.

It is estimated that the total demand for shelf items will approach $5,500,000. Also, many of the items of capital equipment required will exceed $5,000 in value. Thus the existing limits on purchases of shelf items of Code 935 origin, $5,000 per item and $250,000 for total project, are not sufficient to provide the items required by sub-borrower under the project.

It will, however, be stipulated in our agreement with the Uganda Development Bank that no loan funds provided by USAID will be used to finance duties and/or sales taxes for any items valued at over $5,000.

USAID does, nevertheless, recognize the legitimate interests and concerns of U.S. private enterprises which the source and origin requirements were designed to protect. Consequently the following provisions have been included in the project design to permit full and fair U.S. participation in the supply of project-financed commodities where appropriate:

- Early in project implementation, a notice will be published in the Commerce Business Daily describing the project, identifying the kinds of procurement likely to be required under the project, and providing the contact point for project procurement (Procurement Services Agent sub-contractor or division of primary contractor).

  Early in the loan approval process any import requirements of project sub-borrowers will be referred to the Procurement Services Agent who will assist potential sub-borrowers in the identification and procurement of U.S. commodities.

- Sub-loan agreement with sub-borrowers will include a stipulation that preference be given to the procurement of commodities from the United States and other Code 941 countries, in that order, where appropriate.

USAID believes that the above measurers will yield a commodity procurement origin mix which closely resembles that which could be expected under more restrictive conditions, without unduly damaging project implementation.

Primary Justification: The criteria relied upon to support the waiver, per Handbook 1, Supplement B, Chapter 5, Section 5B4a, are as follows:

(2) The commodities are not available from the authorized source: Given the extreme difficulty which would be encountered by project sub-borrowers in maintaining and repairing a large proportion of Code 941 origin machinery and spare parts in rural areas of Uganda, such commodities have been considered to be unavailable.

(7) Such other circumstances as are determined to be critical to the success of the project: Given the determination that the project would not be feasible from the point of view of sub-borrowers or AID if Code 941 source and origin requirements were applied, waiving of such requirements has been considered in the best interests of the project.

Recommendation: Based on the above justification it is recommended that you determine that exclusion of procurement of goods originating from free world countries other than the cooperating country and the less developed countries included in AID Geographic Code 941 will seriously impede the attainment of U.S. foreign policy objectives and the objectives of the foreign assistance program in Uganda.

APPROVED: ______________

DISAPPROVED: ______________

DATE: ______________

Drafted:REDSO:ALaemmerzahl:dlm
Clearance:REDSO:KHansen (draft)
doc. 0901J

ANNEX C-2

DRAFT ACTION MEMORANDUM FOR THE ASSISTANT ADMINISTRATOR FOR MANAGEMENT

SUBJECT: Request for Source/Origin Waiver - Shipping

Problem: Your approval is required for a waiver of Source/Origin requirements from A.I.D. Geographic Code 941 to A.I.D. Geographic Code 935 for the provision of approximately $4,000,000 worth of shipping costs under the Rehabilitation of Private Enterprise Project (617-0104):

a)	Cooperating Country:	Uganda
b)	Nature of Fundings:	Grant
c)	Description of Commodity Related Services:	Ocean shipping
d)	Approximate Value:	Less than $3 million
e)	Origin:	A.I.D Geographic Code 935
f)	Probable Sources:	Greece, U.K., Denmark, Japan (major shipping flags).

Background: Annex C-1 requests a waiver of the source/origin requirements for commodities from USAID Geographic Code 941 to Code 935. Annex C-2 requests a determination of non-availability of U.S. flag carriers. If the above waiver and determination are granted, the availability of Code 941 shipping on the major anticipated routes (Europe-Mombasa and Japan-Mombasa) is not adequate to permit efficient project implementation. REDSO has only been able to identify one 941 flag shipping line providing services on these routes without transshipment. Furthermore, many of the items to be financed under this project will already be on the shelf in Uganda and Kenya. Inasmuch as Code 935 (non-941) vessels perform the majority of freight services from Europe and Japan to East Africa, mostly of these shelf items will have been shipped on 935 vessels. The administrative burden of requesting waivers to permit the financing of the freight portion of the cost of these items will be a burden for available staff and result in further delays making the program less acceptable to sub-borrowers.

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Justification: According to Handbook One, Supplement B, Chapter 7, Section B4a(5), a waiver expanding flag eligibility requirements may be authorized which eligible vessels do not provide liner service from the shipment's source to the destination country. Although Uganda is landlocked and does not have a port of its own, Mombasa is the usual port of entry. Inasmuch as liner service is not adequate from the anticipated major source countries to Mombasa, this waiver is justified.

Recommendation: That you certify that the interests of the United States are best served by permitting financing of transportation services on ocean vessels under flag registry of free world countries other than the cooperating country and countries included in Code 941.

APPROVED: ____________

DISAPPROVED: ____________

DATE: ____________

Drafted:REDSO:Alaemmerzahl:dlm
Clearance:REDSO:EDragon (draft)
doc. 0901J

ANNEX C-3

DRAFT ACTION MEMORANDUM FOR THE ASSISTANT ADMINISTRATOR FOR MANAGEMENT

SUBJECT: Determination of Non-Availability of U.S. Flag Carriers

Problem: Your approval is requested to determine that U.S. flag carriers are not available for shipments from non-U.S. sources to Uganda under the Rehabilitation of Productive Enterprise Project.

Discussion: The goal of the Rehabilitation of Productive Enterprises (RPE) Project is to make available medium to long term financing for investment for agriculturally based enterprises in Uganda. Achievement of this goal will directly contribute to USAID and Government of Uganda (GOU) strategic objectives of rehabilitation and development of the agricultural sector resulting in improved income and employment for Uganda's rural population. Project objectives will be attained through the provision of credit and technical assistance to intermediate credit institutions active in Uganda who will in turn relend to benefiting enterprises. Additional technical assistance and training will be provided to participating enterprises through a separate entity to be established for this purpose. A total of $17.35 million in medium to long term funds will be provided by AID through the Central Bank of Uganda to intermediate lending institutions for on-lending to enterprises to be assisted at market rates of interest. Local resources based agricultural production and processing ventures are the most likely to borrow under the project.

Since the project will be implemented through intermediate credit institutions, and loan decisions will not be made prior to project authorization, no specific list of required commodities can be established. However, studies carried out during project design do allow broad estimates of procurement requirements. USAID estimates that some 120 sub-borrowers will wish to procure approximately $17.35 million of equipment, materials and spare parts for agribusiness and other rural private enterprises of Code 935 but non-Code 941 origin. This procurement will be both off-the-shelf and off-shore. However, there is no regular U.S. flag liner service from non-U.S. source countries to Mombasa, the usual port of entry for commodities consigned to Uganda. Further, there is no regular U.S. liner service to Kenya from other than Gulf and East Coast Sources. Therefore you are requested to determine, per Chapter 7, Section 7D5b(3) of Handbook 15 and per Chapter 10, Section 10A4 of Supplement B, Handbook 1, that U.S. flag vessels are not available for intended procurement from non-U.S. Gulf and East Coast Sources, thereby relieving project sub-borrowers of the obligation to ship at least 50 percent of commodities from these sources financed by the project on U.S. flag carriers.

This request is being made on a blanket, rather than a case-by-case basis because of the large number of individual transactions which will take place under the project. To try to make the determination on a case-by-case basis would impose undue delays in the procurement process which would be unacceptable to private sector sub-borrowers and banks. It would also impose an enormous USAID project management burden.

Recommendation: That you determine that U.S. flag shipping is not available for the intended procurement from non-U.S. Gulf and East Coast Sources in accordance with your authorities under the cited provision of Chapter 10, Supplement b, Handbook 1.

APPROVED: ________________

DISAPPROVED: ________________

DATE: ________________

Drafted:REDSO:ALaemmerzahl:dlm
Clearance:REDSO:EDragon (draft)
doc. 0901J

ANNEX C-4

SCOPE OF WORK - PROCUREMENT SERVICES AGENT (PSA)

The PSA will be required to:

1. Have a corresponding relationship with a similar eligible (941) firm that has offices in both Kampala and Nairobi.

2. Assist sub-borrowers with drawing up specifications for required commodities.

3. At the request of the sub-borrower and in accordance with the sub-borrowers requirements for timely delivery, locate among the eligible sources, the most appropriate and inexpensive sources of supply for the required commodity. Solicit at least three proformas from such sources. Assist in the reviews and evaluation of quotations.

4. Ensure that the commodity to be financed does not include any non-935 components, and ensure that shipping is not accomplished on any non-935 vessel.

5. Document and show justification in cases where awards were made on any basis other than lowest price.

6. Bring to USAID's attention any situations where "sole source procurement (procurement negotiated with only one source of supply) appears to be required. Obtain USAID's approval, in accordance with AID Handbook One, Supplement B, Section 4 before proceeding with procurement. Requests for sole source authorization in excess of $25,000 must be referred to AID/W.

7. Prepare the initial announcement in Commerce Business Daily and AID/Export Opportunities Bullentin describing the project, identifying in the kinds of procurement likely to be required under the project, and act as the contact point for project procurement.

8. When required or considered desirable, advertising the availability of Requests for Quotations in eligible source countries. Assisting in drawing up Invitations for Bids and advertising cases where formal competitive procedures are required.

9. Acting as the "approved applicant" named in the bank L/Comm and ordering letters of credit to be issued to offshore supplies. Instructing the Uganda Development Bank and other participating ICIs to issue purchase orders covering local cost purchases.

10. Consolidate procurement, whenever convenient, for the same or similar items by various sub-borrowers for the sake of simplified administration, lower prices, and lower shipping costs.

11. Determine when quotations should be C.I.F. Kampala, or F.A.S. port of source country. Arrange for shipping for all items not quoted on a C.I.F. Kampala basis. Make recommendations on expeditious and inexpensive shipping alternatives (air freight, rail vs. road, etc.)

12. Maintaining a record of the usage of waiver authorities provide under the project.

13. Be responsible for enforcing AID Marking requirements.

14. Be responsible for the proper receipt an clearance of incoming project commodities. The PSA will arrange for the inspection as necessary, of imported commodities prior to the export from the supplying country. In addition inspection of incoming shipments must be made and receiving documents will be annotated with comments on evidence of or possible damage losses. The PSA will assist the sub-borrower in initiating claims against shippers and/or insurance companies.

15. In all other respects, be guided by the provisions of Chapter 19 of AID Handbook One, Supplement B.

Drafted:SMO:ALaemmerzahl:dlm

ECONOMIC ANALYSIS

I. Background

Notwithstanding the serious political and security problems that continue to plague the Government of Uganda, the economy in general, and especially certain segments of the agricultural sector, are now experiencing relatively good rates of growth. Upon conclusion of the 1979 "War of liberation" however, the new government had inherited a devasted country caused by gross mismanagement during the Amin years and destruction during the war. Industrial capacity had been severely reduced, infrastructure was in disrepair, inflation was rampant, and the central government was almost bankrupt.

In consultation with the IMF over the past 3 years the Government has adopted several key economic/fiscal reforms contributing to economic recovery, the most significant being; (1) the float of the Uganda Shilling from just over Shs. 7.6 to U.S. dollar to the present rate of USh. 210 (window 1) and USh. 330 (window 2), (2) significant increases in the farm gate price for export crops (Ref. Table 3) and (3) the removal of most price controls for export crops, consumer products. Likewise, the price of locally consumed food crops is governed by market conditions. The government also increased interest rate levels and established ceilings on domestic and government borrowing.

Table 1: Exchange Rate Comparisons
(in USh. per U.S. dollar)

At the end of	Official Rates Window one	Window Two	Unofficial Rates
June 1980	7.3	-	8.0
June 1981	77.8	-	200.0
June 1982	96.7	-	300.0
June 1983	150.0	280.0	350.0
November 1983	210.0	330.0	400.0

Sources: IMF, International Financial Statistics
IBRD

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The new government had originally prepared a long term recovery plan, A Ten Year Program of Action, but it proved to be overly ambitious as it was based on significantly larger amounts of foreign aid than could be expected to be forthcoming, especially in view of the internal security problems the government was facing. A revised plan covering a shorter time period was presented in May 1982, the Recovery Programme: 1982-1984 which included proposals for policy and institutional reform as well as a project specific investment plan for 1982/83 and 1983/84. The focus of the plan was to rehabilitate the private productive sectors of the economy, and allow for open market forces to stimulate increased food production. Expenditure of funds for this rehabilitation effort were projected to be $240 million during 1983/84. Only about $150 million was actually available, however. Inadequate Government implementation and administrative capability was also cited as a primary constraint to increased utilization of available funds.

Consequently, following a review of performance in 1983, a Revised Recovery Program was published in October which took account of the resource constraints and implementation experience encountered in the first year of the plan and incorporated 1984/1985.

In terms of overall economic performance, the GDP rate of growth in real terms increased from 3.9% in 1982 to over 6.1% in 1982. Higher rates have been experienced in the subsistence sector compared to the monetary sector. Continued growth is expected in the near term, and the recent budget for 1983/84 generally favors continuation of monetary policies previously worked out in consultation with the IMF. Market forces are expected to increase their influence in the economy, and the more of the financing of imports will shift to Window II exchange rates. It has also been proposed that all new external debts incurred by government agencies should be financed at the Window II rate.

The GOU now plans to increase the amount of foreign exchange available at Window II from $2 billion in 1982/83 to $3 billion in 1983/84. This will also help to reduce the potential risk of abuse from illegal or unauthorized purchase of dollars at the concessionary Window I rate.

The RPE project will complement the current economic policies of the GOU and provide additional support to government efforts at rehabilitation and expansion of productive enterprises in the private sector through the granting of investment loans for the procurement of capital equipment, materials and spare parts and the provision of complementary technical and managerial assistance and training geared specifically to the agricultural sector.

For additional information and data on general economic performance, see the IBRD Country Economic Memorandum for Uganda dated December 1983.

II. Sectoral Overviews.

A. Agriculture

Recovery in the agricultural sector continues to exceed previous expectations. Food crop production has been exceptionally good, but export crops are also doing well. Surplus maize has recently been sent to Tanzania. Uganda is fortunate in that such a large portion of the country is suitable for crop production and livestock rearing. In addition, about 15% of the land area is freshwater rivers and lakes containing large stocks of fish. Estimated land usage in 1980 is given in Table 2 below.

Table 2-Land Use

	(000 hectares)
Arable land-seasonal crops	3,900
Under Permanent crop	1,351
Permanent Pastures	5,000
Forest land	2,759
Other land (semi-arid)	6,961
Total land area	19,971
Inland water	3,633
Total area	23,604

(Source: FAO estimates in Europa, Africa South of Sahara, 1980)

Eighty-four percent of Uganda is a plateau (elevation 900 to 1500 meters) with rainfall between 900 to 1600 millimeters annually. The rain pattern is generally bi-modal allowing two cropping seasons per year. Moderate population density (average 70 people per sq. km.) provides adequate agricultural land for current and near term needs. Estimated total population in 1982 was 13.5 million with an annual population growth rate estimated at between 3% and 4%.

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The major source of foreign exchange earnings for Uganda is the export of cash crops, of which coffee presently represents about 95% according to the 1982-83 GOU Budget Report. Uganda has a current coffee quota set by ICO at 162,000 tons and expects to have this increased to 192,000 tons for the 1984 season. Coffee production in 1981/82 was 97,500 tons, 166,600 tons in 1982/83, and is projected to be 192,360 tons in the 1983/84 season. This increase has come about from the rehabilitation of existing coffee trees and coffee processing factories rather than from new acreage. Uganda expects to be able to sell its surplus over quota profitably on the open market; although given the current oversupply of coffee on world markets, and a recent USDA estimation that the 1983/84 world coffee crop will increase 16% over the previous year, this may not be possible. unless demand for Robusta coffee continues to be high. It is expected that with the rehabilitation of both large scale and small tea holdings in Western Uganda, however, this crop will play a larger role in foreign exchange earnings in the future, especially now given the current rapid increase in world tea prices.

Table 3: Producer Price Changes

	1980	1981		1982		1983
Crop (USh/kg.)	Dec.	June	Dec.	June	Dec.	June
Coffee	7.0	20.0	35.0	50.0	50.0	80.0
Tea	2.6	4.0	6.0	10.0	10.0	25.0
Cotton	6.0	15.0	30.0	40.0	40.0	60.0
Tobacco	14.0	34.0	80.0	100.0	100.0	150.0

The above four cash crops still have an prices officially established by the government. The ratios of price increase for these crops from December 1980 to June of 1983 have all been about 10 to 1. This does not compare favorably with the same changes in the official exchange rates which have in the same period increased at ratios of 19.8 to 1 for Window 1 (USh 7.6 to 150 to the dollar) and a ratio of 37 to 1 for Window 2 (USh.7.6 to 280 per dollar). Nevertheless, the producers do appear to be adequately motivated to increase production at prevailing prices, especially for coffee and tea. The government attaches considerable importance to continued improvement in coffee production as it levys an export tax on coffee equal to about 33% of the export sale price (July 1983

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prices). The producer realizes about 47% of the value and the balance goes for processing and marketing. Calculation of estimated net returns on th above cash crops together with the major food crops would, except for coffee, favor food crops which do not have price controls and are more likely to respond to market conditions.

Table 4: Returns to Selected Crops (July, 1983)

	Yield per hectare (a) (kg)	Producer Price (USh/kg.)	Producer Cost (a) (USh/kg.)	Net Return to land (USh.'000/ha)
Robusta coffee	1,500	80	20	90
Cotton	259	60	39	5
Tea (leaf)	3,625	25	21	15
Tobacco	500	150	135	8
Bananas	10,000	8	1	70
Groundnuts	710	100	37	45
Maize	1,150	30	9	24

(a) Based on most commonly used technology. All labor costs, hired and family, are included and are valued at USh. 80 per manday for coffee and bananas and USh. 60 per manday for all other crops.

Source: World Bank, Uganda, Agriculture Sector Memorandum

Cotton, previously Uganda's second most important cash crop, has not experienced the same rapid recovery found with coffee. The pre-season estimate for 1982/83 was for 200,000 bales, but the outcome was about 65,000. Much higher projections are being made for the 1983/84 season (est. 200,000), but due to the shortage of financing for cotton purchase, farmers are reluctant to release their crop, fearing default in payment by the cooperative buyers. With current ginning capacity of 200,000 bales per annum and a further planned development of 224,000 bales of ginning capacity being financed by World Bank and African Development Bank, there should be ample processing capacity if the cooperatives can secure financing for purchase. Further developments in cotton production and processing will provide additional cotton seed for oil extraction and cotton seed cake for the animal feed industry.

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Uganda now has an excellent opportunity to rehabilitate and further develop its own agricultural production base and attempt to satisfy domestic consumer demand for such products as edible oils, poultry products, animal feeds, dairy products, and certain food crops such as sugar and rice. Recapturing markets and returning to former levels of production or increasing to even higher levels will require special attention not only to direct inputs, but also to processing facilities, markets, and the managerial/technical skills required for these activities. The RPE project addresses many of these issues by focusing on the rehabilitation and/or expansion of productive activities that were previously well established in Uganda and for which there was effective consumer demand. RPE will complement current government policies directed toward encouraging the restoration of agricultural production and agro-industrial activities.

B. Industry

Rehabilitation efforts in this sector have not been as spectacular to date as in agriculture. Reasons for this include: (1) physical plants were allowed to run down with inadequate repairs/replacement during 1970's, (2) management and technical expertise (often of Asian origin) was forced to leave, (3) deterioration of supporting infrastructure, and (4) shortage of raw materials and required foreign exchange.

Several international donor agencies, including the EEC, Islamic Development Bank, and IBRD have pledged funds to support rehabilitation efforts in the manufacturing sector, but progress has been slow due to administrative bottlenecks, disputes on property ownership, and security problems in major industrial areas. Reliable transportation continues to be scarce. Whereas manufacturing's share of GDP in the monetary economy was 7.1% in 1970 and 6% in 1975, it dropped to about 3.5% for the period 1980-1982. The breakup of the East African Community further reduced the potential for regional African markets for manufactured goods from Uganda, and most manufacturing must now be oriented toward the Uganda domestic market alone. The reduction of import restrictions for manufactured and consumer goods will require that locally manufactured products be competitive in price and quality with imported goods if they are to gain back a portion of the local market. Investments should first gravitate toward those activities where Uganda appears to have a comparative advantage, which now would be in the agricultural and agro-industrial areas such as sugar processing and oil extraction.

III. The Project

A. Overview

The PID originally identified coffee and cotton as the major areas requiring financial support for rehabilitation efforts. During subsequent field investigations, however, it became apparent that these two commodities were being adequately supported by ADB, IBRD, and UK funds. Nevertheless, other appropriate agricultural production and processing areas were identified during field preparations for the Project Paper, which included; poultry hacheries, processing and production facilities; edible oil processing, animal feeds production, dairy production and processing, commercial fishing, and mixed farming.

All these project areas rely primarily on locally produced agricultural materials, or are engaged in direct agricultural production. They also tend to be labor intensive and job creating. Current market demand for planned project production comes from both regaining the previous market and from the natural increase in demand resulting from high population growth. Foreign exchange requirements are significant and essential, especially for capital equipment. The necessary investment capital has not been forthcoming, however, due to the ongoing liquidity problem, lack of external funding aimed at these areas, and lack of technical absorptive capacity of both credit intermediaries and the enterprises themselves. It is to these constraints, of course, that this project is directed.

B. Specific Sub-Project Activities

Areas identified for RPE support are of an agricultural production and processing nature aimed at domestic consumptions and sometimes import substitution. All activities were well developed at the time of the Amin takeover, some being primarily in the hands of Africans (fishing, farming, dairy), whereas most of the oil processing was owned and controlled by the Asian community.

During preparation of the project paper, a representative sample of the various loan categories were reviewed and site visits were made to several parts of the country. Of the loan applications submitted to the Uganda Development Bank (UDB) and reviewed by the PP team, none were adequately prepared and ready for appraisal. UDB senior management concurred. Preliminary costing and appraisals were made on several potential projects, but it was apparent that a considerable amount of preparatory work and analysis still remained before an adequate assessment of the applications could be made. The banking institutions have been reluctant to become involved in loan and project preparation work, however, due to the risks inherent in such projects without adequate feasibility analyses, the lack of externally supplied foreign exchange available for this area, and (according to the UDB) the fact that combining project development and appraisal function would compromise objectivity. Cost and logistic constraints associated with feasibility work are also deterants.

For purposes of analysis, the PP team developed some representative models for the various types of loan likely to be included in the RPE project. These models provide illustrative examples of financial viability for selected enterprises. These do not substitute for what will ultimately be required by way of complete analysis of each loan application, but such analyses will only be possible when adequate technical assistance is available to assist clients in sound evaluation and planning of potential investments. Undoubtedly there will be some changes in the profile of the agricultural lending activity during implementation, taken into account in project design, but the general focus of the effort in terms of level and nature should remain essentially valid. Changing economic conditions of the country will result in certain projects being more financially attractive than others, and undoubtedly there will be new enterprises identified during implementation. Examples follow:

1. <u>Poultry Production and Processing</u>

A well developed and integrated poultry production and marketing industry had previously existed in Uganda, and there is considerable interest being expressed by producers to re-establish it.

Success in poultry production depends on well established feed sources, processing facilities, and adequate markets. An ample supply of day-old chicks is also required. A reasonable level of profitability can be attained if the producer has a regular market for his mature birds. With an 8,000 broiler throughput per annum, breakeven would be at about 25% production. Annual profits are projected to be USh. 1.5 million giving an internal rate of return of 28.7% over 20 years on an investment of USh. 3.5 million (Ref Appendix 2-A). No such market exists, however, as the main processing cooperative, the Wankoko plant, is unable to operate and is in severe need of rehabilitation.

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A delay in processing mature broilers by even as little as one week can seriously reduce the profitability of a broiler operation. For this reason it is recommended that the rehabilitation of the Wankoko plant be given high priority. Most of the demand for broilers comes from the urban areas, especially Kampala and Jinja. A processing plant(s) with storage facilities to hold oven-ready broilers is required to provide dependable markets for producers.

Previous problems with the Wankoko processing plant can generally be attributed to mis-management, and it is important that this issue be addressed and rectified if producer confidence in the cooperative processing plant is to be restored. The Wankoko poultry plant could be rehabilitated for USh. 100 million and would be profitable operating at half capacity. The internal rate of return would be 33%. This assumes that existing land and building would be contributed and the return is calculated on additional finance, both capital and operating, required to bring the plant back into production. (Ref: Appendix 2-A).

With respect to Hatcheries, production is far below current demand in part due to inadequate equipment at existing facilities, and the shortage of foreign exchange for the importation of parent stock. The EEC has funded some new equipment for both government and private hatcheries, but this has not brought up the level of production to meet market demand. The private hatcheries are planning expansion as demand is such that customers are placed on waiting list for day-old chicks. The Bulemezi Hatchery is an example of a closed operation that would be made operational by the installation of a generator and the purchase of parent stock and drugs. Previous production was 4,000 chicks per week. Inadequate supply of quality feeds, another important factor, is discussed in the section below on feed milling.

The actual rearing of broilers and layers relies primarily on inputs available from within Uganda. Adequate building can be constructed of local materials, and the moderate climate keeps construction costs low. Medium-sized production units for (1,000-4,000) birds tend to be simple in construction and labor intensive. These units fit well with the high population density and small farming units around Kampala, and they have the advantage of being close to urban markets. Poultry products in other parts of Uganda are being supplied from the informal agricultural sector, and current opportunities for establishing commercial poultry production in these areas appear limited.

2. Dairy Production

The milk collection and marketing centers established by the parastatal Dairy Corporation are currently grossly under utilized, and prospects of the Dairy Corporation re-establishing previous milk processing levels appear limited. The Dairy Corporation currently pays the Government set price of USh. 20 per liter of milk delivered to the collection center. This is below the cost of production. The controlled price of milk has been increased to USh. 40, but this still is inadequate to encourage new investment. Even though the Dairy Corporation has a monopoly on the purchase and processing of milk for the formal market, the majority of milk now produced is sold locally through informal marketing channels. The price of raw milk in the open market varies considerably through the country from a low of USh. 20 per liter in the traditional milk producing area of Mbarara to a high of USh. 100 in the Mbale area. Prices in Kampala and other larger urban areas are generally between USh. 60-80 per liter in the open market.

As with all livestock projects involving cattle, a dairy enterprise must be viewed as a long term proposition. This is especially important when the enterprise relies on the initial herd for internal growth. When analyzing a medium-sized dairy farm of this nature (initial 30 cows increasing to 60 cows when fully stocked), a dairy farm located in an area of the country where there is sufficient market demand so that milk can be sold at USh. 80 per liter would experience a negative cash flow during the first (and possibly the second) year. It would not be until the tenth year that the herd would reach a full stocking level of 60 cows. The enterprise would be profitable, however, from the third year on, with a 12.9% internal rate of return on USh. 19 million investment. If open market prices continue, and milk prices increase faster than variable costs, the IRR would obviously improve. (Ref: Appendix 2-B.)

Much of Kampala is supplied with reconstituted imported milk powder supplied by the World Food Program and packaged by the Dairy Corporation, a parastatal, which it then sells to cover its operating expenses. With this operation in place, there is little incentive for reactivate producer collection centers. Transport costs to move liquid milk from outlying areas would not be economical given current costs for operating a milk transport fleet. There is potential for investment in rural collection/cooling centers, however, if the Dairy Corporation were to adopt a price policy competitive with the local

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market. The Dairy Corporation has embarked on a merchandising scheme whereby it supplies certain inputs to farmers (e.g., milk cans, fencing material). Such a scheme might be appropriate for RPE funding, but proposed project criteria would prohibit lending to a parastal corporation.

Dairy production should be encouraged in those parts of the country were it is a profitable agricultural activity. Such areas include Kampala, Jinja, Mbale, and Ft. Portal. Prices in Lira, Soroti, and Gulu would also warrant production investment. Constraints to increasing dairy production have been the scarcity of drugs, shortage of feed concentrates, and a poorly operated artificial insemination (A.I.) service. The shortage of dairy stock has also been cited as a constraint, and several officials recommend that Uganda should embark on a program to import dairy heifers. A field survey carried out during PP preparation indicated that dairy heifers were generally available for between USh. 100,000 to USh. 150,000 ($330-$500), which is about half the cost of importing stock from neighboring Kenya. With the reintroduction of the A.I. service through support of the EEC, adequate foundation stock is now available to provide the 600 head of dairy stock for 20 dairy units proposed for the RPE project. The GOU has also announced that the supply of drugs in the future will be handed over to commercial drug producers who will establish their own distribution network. Pfizer, Welcomer, and Bayer are expected to re-establish distribution systems in Uganda. (Feed supply for dairy production is covered below.)

3. <u>Feed Mills</u>

The lack of an adequate animal feeds industry responsive to the local market is considered by most livestock producers to be a critical constraint to increasing production and improving profitability. Most of the feed production capacity in Uganda is concentrated in one milling unit operated by a parastatal organization in Jinja. Not only are their products reported to be inconsistent in quality, but supplies are irregular and not widely distributed throughout the country.

Demand for animal feeds is increasing due to expansion of poultry and dairy production. Ingredients for manufacturing animal feeds are increasingly available in Uganda, and the only required imported ingredients is the pre-mix concentrate. Existing feed milling facilities need to be decentralized, with scaled down capacity and using less complex milling machinery with lower capital and maintenance cost requirements. More labour intensive processing methods are warranted as the

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availability of labour is not a constraint. Uganda also produces cereal crops and agricultural by-products that are suitable for animal feeds. Human requirements for cereal crops are now being met, and surplus and inferior grades of these commodities should be used for animal feeds. The current revival of cotton ginning and oil extraction will also restore cotton seed cake, an important protein source for animal feeds, to the market.

Small scale feed mills (1-5 tons per hour) are low capital cost processing facilities, and given the good system of electricity distribution in Uganda, energy is also available. Transportation costs are, relative to other variable costs, high in Uganda, and the selection of location for feed mills should take this into consideration. Several substitutions can be made in the make-up of animal feed, and mill operators should take advantage of the least-cost formulation.

An illustrative model of a small feed mill derived from current market prices for inputs and capital equipment costs indicates that a mill can breakeven operating about 35% capacity on single shift. An investment of USh. 20 million would be required for this type of mill. If production increased to 67% of mill capacity by the third year and continued at that level, a 28.6% internal rate of return would be realized over 10 years. Because of the low capital cost to variable cost ratio, feedmills like this can breakeven on 800 tons per annum. (Ref: Appendix 2-B.) Road transportation costs about USh. 40 per ton/kilometer, meaning that feed costs increase by 6% for every 100 kilometers of transport on feed valued at USh. 65,000 per ton. Moving feed from Jinja to Ft. Portal would increase feed costs 18% (USh. 16,000 per ton).

4. <u>Oil Seed Processing</u>

A recent consultant report for the USAID (Oil Seed Processing - Uganda, May, 1983) reviewed the current status of oil milling in Uganda and recommended consideration of selective investment in potentially viable operations. Most of the existing plant is low technology and labor intensive, designed for processing only cotton seed.

All oil mills (18 units) and their auxiliary soap activities were taken over by the Lint Marketing Board (LMB) through a government decree in 1974 with no compensation paid to former owners. Because of a shift in the cotton production areas toward the north in recent years, several mills are no longer in a geographic location that would warrant rehabilitation.

There are no crushing facilities at Gulu, however, a major cotton producing/ginning area which also has potential for other oil seed crops. The consultant study recommended that a mill be established at Gulu, and the Madhavani Group has already prepared a study on a 60-ton-day unit for this area to be a joint venture with other Uganda citizen investors holding majority shares. There is a serious policy issue to be resolved, however, before any financing is provided for the rehabilitation of oil seed milling capability. Oil production in Uganda is taxed at 70% for the domestic market which makes the resulting price higher than that for imported oil.

Cotton seed cake is sold locally for USh. 6 per kilogram which is low in comparison to world market prices, but it provides a cheap source of protein for the animal feeds industry. Equipment installed in any new oil crushing plant should be of the type that can also be used for other oil seeds like sesame, sunflower, and soy beans.

Estimated market demand for oil is only 25,000 ton per year due to high retail prices (Kampala price USh. 900 per kilogram). If total production reaches the government projected level of 300,000 tons of cotton seed per year, reserving some 50,000 tons for planting material, the remaining 250,000 tons would produce about 30,000 tons of oil. Consumer demand would increase if the retail price were to come down. It is also important that any new facility be able to take advantage of lower cost for cottonseed resulting from low material transport costs. If the Lint Marketing Board were to adopt a uniform delivered price and force transport costs of cottonseed to be absorbed in this same price, obviously this would be a disincentive to new investment and provide for higher costs to the consumer. The current EMCO oil mill (51% Uganda Government and 49% Madhavani) in Jinja with a 300 ton/day capacity would be the prime beneficiary of this distorted pricing system. The price for cottonseed should be established ex-gin with the oil miller being responsible for transport costs.

Investment opportunities for RPE funds would potentially exist for the construction of a new facility at Gulu and rehabilitation of existing facilities at Soroti, Mbale, and Tororo. Most of rehabilitation work would be for replacement equipment and some building repairs. Refer to Appendix 3 for net margin calculations on cottonseed oil processing and the internal rate of return for a proposed plant. The IRR would increase with a reduction in the 70% tax.

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Appendix 1 TAble I - UGANDA: COUNTRY DATA D-4

Population	13.51 million (1982)	Area	236,000 sq. km.
Population Growth Rate	2.8% per annum (1980-82)	Population Density	57.25 per sq. km.
Adult Literacy Rate	52.3% (1980)	Population Density (less lake and swamp areas)	69.5 per sq. km.
Primary School Enrollment	50.0% (1980)		
GNP Per Capita	US$ 240 a/ (1982)		

Gross National Product in 1982 b/ / **Real Annual Growth Rates: Percent**

	US$ Million	%	1970-75	1975-81	1982
GNP at Market Prices	7,336	100.0	--	- 3.2	7.8
Gross Domestic Investment	609	8.3	-11.9	- 4.7	27.1
Gross National Savings	353	4.8	-16.9	-10.4	44.7
Current Account Balance	-256	-3.5	--	--	--
Export of Goods, NFS	339	4.6	-11.3	- 7.3	36.1
Import of Goods, NFS	558	7.6	- 9.2	- 5.9	19.0

Annual Rates of Inflation c/

1970-75	19.24%
1975-79	56.74%
1979-80	107.23%
1980-81	92.80%
1981-82	44.87%
1982-83	30.00% (Estimate)

Value Added (1966 Prices)

	1980		1982	
	US$ Million	%	US$ Million	%
Agriculture	424.0	51.7	536.0	56.8
Industry	46.0	5.6	44.0	4.6
Services	350.0	42.7	363.0	38.6
Total	820.0	100.0	943.0	100.0

Government Finance — Central Government

	USHs Million	(% of GDP)	
	1981/82	1971/72	1981/82
Current Receipts	27,878.0	13.5	4.9
Current Expenditures	30,071.0	13.5	5.3
Current Surplus	-2,193.0	--	-0.4
Capital Expenditures	13,225.0	8.6	2.3

a/ Adjusted to account for overvalued exchange rate
b/ Calculated at official Window One exchange rate
c/ GDP deflator

Source: Uganda Country Economic Memorandum, IBRD, December, 1983

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TABLE II

Gross Domestic Product by Industry

(Millions of Shillings at 1966 Prices)

	1965		1970		1975		1980		1981		1982		1980/1970	1982/1980
	GDP	% Share	GDP	% Share	GDP	% Share	GDP	% Share	GDP	% Share	GDP	% Share		
netary Economy	3,939.0	68.07	5,095.0	69.97	4,768.0	64.81	3,822.0	62.50	3,833.6	60.34	4,044.0	60.01	.75	1.06
Agriculture	1,324.0	22.88	1,781.0	24.46	1,605.0	21.82	1,234.0	20.18	1,232.0	19.40	1,382.0	20.51	.69	1.12
Agro-Processing	85.0	1.47	114.0	1.57	59.0	.80	43.0	.70	31.0	.49	43.0	.64	.38	1.00
Manufacturing	375.0	6.48	517.0	7.10	446.0	6.06	218.0	3.57	216.0	3.40	235.0	3.49	.42	1.08
Other	2,155.0	37.24	2,683.0	36.84	2,658.0	36.13	2,327.0	38.05	2,354.0	37.06	2,384.0	35.38	.87	1.02
ubsistence Produc.	1,848.0	31.93	2,187.0	30.03	2,589.0	35.19	2,293.0	37.50	2,519.0	39.66	2,695.0	39.99	1.05	1.18
Agriculture	1,494.0	25.82	1,763.0	24.21	2,085.0	28.34	1,734.0	28.36	1,952.0	30.73	2,124.0	31.52	.98	1.22
Other	354.0	6.12	424.0	5.82	504.0	6.85	559.0	9.14	567.0	8.93	571.0	8.47	1.32	1.02
oss Domestic Product at Factor Cost	5,787.0	100.00	7,282.0	100.00	7,357.0	100.0	6,115.0	100.00	6,352.0	100.00	6,739.0	100.00	.84	1.10

ource: Uganda Country Economic Memorandum, IBRD, December, 1983

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TABLE III

Production of Major Crops

(Thousands of Tons)

	1980	1982	Percentage Change
Coffee	135.2	166.6	+23.22
Cotton Lint	6.1	5.1	-16.39
Tobacco	.4	.6	+50.00
Tea	1.5	2.4	+60.00
Sugar (Raw)	4.3	2.5	-41.86
Maize	286.0	393.0	+37.41
Finger Millets	458.0	528.0	+15.28
Sorghum	299.0	400.0	+33.78
Sweet Potatoes	1,200.0	1,600.0	+33.33
Cassava	2,072.0	3,300.0	+59.27
Bananas	5,699.0	6,600.0	+15.81
Groundnuts	65.0	90.0	+38.46
Beans (Mixed)	186.0	300.0	+61.29

Source: Uganda Country Economic Memorandum, IBRD, December, 1983

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TABLE IV

Balance of Payments

(In US$ Million)

Item	1970	1975	1978	1979	1980	1981	1982	1983
Merchandise Exports FOB	261.6	237.2	322.9	397.2	319.1	245.5	335.0	333.0
Merchandise Imports CIF	-204.9	-262.5	-352.1	-322.1	-503.7	-414.7	-457.5	-497.0
Trade Balance	56.7	- 29.3	- 29.2	75.1	-184.6	-169.2	-122.5	-167.0
Invisibles (Net)	- 43.3	- 49.2	-112.3	- 82.0	- 63.4	- 84.5	-133.3	- 95.0
Current Account Balance	13.4	- 74.5	-141.5	- 6.9	-248.0	-253.7	-255.8	-262.0
Official Grant Receipts	7.0	21.1	8.8	31.6	93.2	103.3	88.4	102.0
Public M & LT Loans (Net)	21.3	16.0	33.8	109.4	81.8	- 1.1	151.1	103.0
-Disbursements	27.4	29.3	69.5	150.4	134.0	92.9	256.6	236.0
-Scheduled Repayments	- 6.1	- 13.3	- 35.7	- 41.0	- 52.2	- 91.8	-105.5	-133.0
Use of IMF Credit (Net)	--	9.9	- 1.8	- 3.5	26.5	125.1	82.4	104.0
Other Capital Items 1/	- 36.9	28.0	48.8	-195.7	-107.2	74.3	78.6	-27.0
Overall Balance of Payments	4.8	0.5	- 51.9	- 65.1	-153.7	50.1	144.7	20.0
Financed By:								
Accumulation of Arrears	--	17.2	70.3	9.6	141.1	- 39.5	- 86.4	- 20.0
Change in Reserves (—INCR)	- 4.8	- 17.7	- 18.4	55.5	12.6	- 10.6	- 58.3	N/A
Memo Items								
Arrears Level (End of Year)	--	36.5	105.9	115.5	256.6	217.1	130.7	N/A
Reserves Level (End of Year)	64.8	31.9	72.3	16.8	4.2	14.8	73.1	N/A

1/ Includes Errors and Omissions

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TABLE V

Central Government Budgetary Operations

(In USHs Billion)

	Actual FY72	Actual FY81	Actual FY82	Estimates Budget FY83	Estimates Latest FY83	Estimates Budget FY84
Revenue and grants	1.5	3.3	27.9	45.9	52.8	84.7
Revenue	1.5	2.7	24.4	44.1	52.2	76.5
Grants	-	0.6	3.5	1.8	2.4	8.2
Expenditure	2.4	13.1	43.3	61.0	69.4	102.9
Recurrent	1.5	11.0	30.1	41.3	45.6	63.9
Development	0.9	2.9	8.9	19.3	11.7	35.6
Other	-	-0.8	4.3	0.4	12.0	3.4
Deficit	-0.9	-9.8	-15.4	-15.1	-16.5	-18.2
Financed by:						
External borrowing (net)	0.1	0.8	1.0	12.6	3.6	14.2
Domestic borrowing	0.5	9.0	14.4	2.5	12.9	4.0
Ratios (%)						
Deficit/expenditure	36.6	74.7	35.6	24.8	23.8	17.7
Revenue/GDP	14.0	0.8	4.3	5.3	6.3	7.0
Expenditure/GDP	22.1	3.9	7.6	7.3	8.4	9.4
Deficit/GDP	8.1	2.9	2.7	1.8	2.0	1.7

Source: Uganda Country Economic Memorandum, IBRD, December, 1983.

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TABLE VI

Uganda
Sources of Secured Financing
for the
Revised Recovery Program - FY 84 - FY 85
($ Millions)

Donor	Agriculture	Industry & Tourism	Mining & Energy	Transport & Communications	Social Infrastructure	Total
EEC/EDF	34.43	.40	5.70	12.00	3.40	55.93
IDA/IBRD IFC	30.50	41.75	.40	25.90	27.35	125.90
IFAD	9.80	--	--	--	--	9.80
ADB	14.00	17.00	--	--	1.50	32.50
U.N. Family	7.20	.62	--	2.20	20.67	30.69
USAID	5.00	--	--	--	--	5.00
FRG	2.60	--	--	--	--	2.60
France	.30	--	--	1.10	--	1.40
UK/CDC	--	6.00	.40	--	--	6.40
CIDA	--	--	--	--	1.82	1.82
Arab Organizations	--	39.00	--	2.00	--	41.00
Other	.30	28.90	.60	16.30	4.14	50.24
Total Donors	104.13	133.67	7.10	59.50	58.88	363.28
GOU	1.40	3.76	6.00	7.00	24.69	42.85
Total Financing	105.53	137.43	13.10	66.50	83.57	406.13
Total Cost	159.38	165.95	25.80	106.50	128.96	586.59
% Secured	66.2	82.8	50.8	62.4	64.8	69.2

Source: Revised Recovery Program, 1982-1984

Appendix 1

Table 7

NATIONAL ECONOMIC TRENDS FOR
MONEY, CREDIT, AND PRICES

	1977	1978	1979	1980	1981	1982
	(USH million outstanding end of period)					
Money Supply	7,400	9,585	13,166	17,435	30,847	38,512
Bank Credit to GOU	5,522	7,288	9,485	14,848	29,332	34,175
Bank Credit to Other	2,885	3,221	3,371	5,951	11,459	23,428
	(Percentage or index number)					
Money % of GDP	13.9	13.7	11.9	8.0	6.9	5.5
General Price Index (1966 = 100)	706	917	1702	3527	6800	9851
Annual Percentage Change in:						
General Price Index	117	30	86	107	93	45
Bank Credit to Public Sector	15.3	32	30.1	56.5	97.5	16.3
Bank Credit to Private Sector	48.9	11.6	4.7	76.5	92.6	86.5

Source: IBRD

Appendix 2-A

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Break Even Analysis		Units Sold	Profit or Lo
Broiler Production Unit 2,000 Birds		500	-366215.00
Retail Price .	1000.00	1000	-232430.00
		1500	-98645.00
Fixed Costs	(Totals)	2000	35140.00
Interest Cap Dev	300000.00	2500	168925.00
Depreciation	150000.00	3000	302710.00
Other	50000.00	3500	436495.00
TOTAL Fixed Cost	500000.00	4000	570280.00
		4500	704065.00
Variable Costs	(Per Unit)	5000	837850.00
Labor	3.27	5500	971635.00
Materials/Feeds	570.00	6000	1105420.00
Transportation	45.45	6500	1239205.00
Other	113.71	7000	1372990.00
TOTAL Variable Cost	732.43	7500	1506775.00
		8000	1640560.00
Quantity Increment	500	8500	1774345.00
Discount Rate (%)	0	9000	1908130.00
		9500	2041915.00
ASSUMPTIONS:		10000	2175700.00
		10500	2309485.00
1. 2,000,000 loan 15% int		11000	2443270.00
2. 6% mortality		11500	2577055.00
3. 1,500,000 working capital		12000	2710840.00
4. 2,000 bird intake/90 day cycle		12500	2844625.00
5. market 1875 birds quarterly		13000	2978410.00
7500 per year		13500	3112195.00
		14000	3245980.00
		14500	3379765.00
		15000	3513550.00
		15500	3647335.00

==

Year	Investment	Annual Cash Inflows
	3500000	0
1		570280
2		1506775
3		1506775
4		1506775
5		1506775
6		1506775
7		1506775
8		1506775
9		1506775
10		1506775
11		1506775
12		1506775
13		1506775
14		1506775
15		1506775
16		1506775
17		1506775
18		1506775
19		1506775
20		1506775
21		0
22		0
23		0
24		0

Internal Rate of Return 28.7%

Appendix 2-A (cont.)

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Break Even Analysis		Units Sold	Profit or Lo
WANKOKO-Dressed Chicken		20000	-123755.00
Retail Price	4.00	40000	-113755.00
		60000	-103755.00
Fixed Costs	(Totals)	80000	-93755.00
Development	52880.00	100000	-83755.00
Marketing	5000.00	120000	-73755.00
Other	75875.00	140000	-63755.00
TOTAL Fixed Cost	133755.00	160000	-53755.00
		180000	-43755.00
Variable Costs	(Per Unit)	200000	-33755.00
Labor	.05	220000	-23755.00
Materials	.05	240000	-13755.00
Packaging	.07	260000	-3755.00
Live Birds	3.33	280000	6245.00
TOTAL Variable Cost	3.50	300000	16245.00
		320000	26245.00
Quantity Increment	20000	340000	36245.00
Discount Rate (%)	0	360000	46245.00
		380000	56245.00
		400000	66245.00
Calculated in US$1.00 = USh 300.		420000	76245.00
Development costs are debt service		440000	86245.00
Other fixed costs include indirect		460000	96245.00
labour, office expenses, R+M		480000	106245.00
		500000	116245.00
Full Production is 600,000 birds p.a		520000	126245.00
75% procuction 450,000 birds		540000	136245.00
50% production 300,000 birds		560000	146245.00
		580000	156245.00
		600000	166245.00
		620000	176245.00

Year	Investment	Annual Cash Inflows
	350000	0
1		16245
2		16245
3		16245
4		16245
5		16245
6		16245
7		16245
8		16245
9		16245
10		16245
11		16245
12		0
13		0

Internal Rate of Return 33.6%

Appendix 2-B

Break Even Analysis

Model Dairy Farm-30/60 Cow Unit

Retail Price per liter 80.00

Fixed Costs	(Totals)
Int Sh 19m Cap Dev	3800000.00
Depreciation 10% pa	1900000.00
Other	.00
TOTAL Fixed Cost	5700000.00

Variable Costs	(Per Unit)
Labor	1.81
Materials/Feeds	5.93
Transportation	4.01
Other	.37
TOTAL Variable Cost	12.12

Quantity Increment 10000

Discount Rate (%) 0

CAPITAL DEVELOPMENT
facilities are adequate for 60 cows and if each cow produced 9 lt/day the growth from initial 30 cows to 60 cows would be as follows:

- Year 1 - 80,000 lt
- Year 2 - 90,000 lt
- Year 3 - 100,000 lt
- Year 4 - 110,000 lt
- Year 5 - 120,000 lt
- Year 6 - 130,000 lt
- Year 7 - 140,000 lt
- Year 8 - 150,000 lt
- Year 9 - 160,000 lt
- Year 10- 170,000 lt

Units Sold	Profit or Lo
10000	-5021200.00
20000	-4342400.00
30000	-3663600.00
40000	-2984800.00
50000	-2306000.00
60000	-1627200.00
70000	-948400.00
80000	-269600.00
90000	409200.00
100000	1088000.00
110000	1766800.00
120000	2445600.00
130000	3124400.00
140000	3803200.00
150000	4482000.00
160000	5160800.00
170000	5839600.00
180000	6518400.00
190000	7197200.00
200000	7876000.00
210000	8554800.00
220000	9233600.00
230000	9912400.00
240000	10591200.00
250000	11270000.00
260000	11948800.00
270000	12627600.00
280000	13306400.00
290000	13985200.00
300000	14664000.00
310000	15342800.00

Year	Investment	Annual Cash Inflows
	19000000	0
1		-269600
2		409200
3		1088000
4		1766800
5		2445600
6		3124400
7		3803200
8		4482000
9		5160800
10		5839600
11		6000000
12		6000000
13		6000000
14		6000000
15		6000000
16		6000000
17		6000000
18		6000000
19		6000000
20		6000000
21		0

Internal Rate of Return 12.9%

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Break Even Analysis

FEEDMILL

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Appendix 2-C

		Units Sold	Profit or Loss	
Retail Price per Ton	65000.00	100	-6100000.00	
		200	-5200000.00	
		300	-4300000.00	
Fixed Costs	**(Totals)**	400	-3400000.00	
Development	3000000.00	500	-2500000.00	
Depreciation	3000000.00	600	-1600000.00	
Other	1000000.00	700	-700000.00	
TOTAL Fixed Cost	7000000.00	800	200000.00	
		900	1100000.00	
Variable Costs	(Per Unit)	1000	2000000.00	Year 1
Labor	400.00	1100	2900000.00	
Materials	45000.00	1200	3800000.00	
Packaging	4500.00	1300	4700000.00	
Other	6100.00	1400	5600000.00	
TOTAL Variable Cost	**56000.00**	1500	6500000.00	Year 2
		1600	7400000.00	
Quantity Increment	100	1700	8300000.00	
Discount Rate (%)	0	1800	9200000.00	
		1900	10100000.00	
		2000	11000000.00	Year 3
		2100	11900000.00	
		2200	12800000.00	
		2300	13700000.00	
		2400	14600000.00	
		2500	15500000.00	
		2600	16400000.00	
		2700	17300000.00	
		2800	18200000.00	
		2900	19100000.00	
		3000	20000000.00	
		3100	20900000.00	

Mill capacity is 1.5 tons per hour or 3000 tons p.a. on 260 workdays Development Cost represent interest on 15 million loan. Depreciation rate is 20% p.a. Throughput for first year is 50% of capacity up to 67% by year 3.

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Year	Investment	Annual Cash Inflows
	20000000	0
1		2000000
2		6500000
3		11000000
4		11000000
5		11000000
6		11000000
7		11000000
8		11000000
9		11000000
10		11000000
11		0
12		0
13		0

Internal Rate of Return 28.6%

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Appendix 3

COTTON SEED OIL PROCESSING

The cottonseed oil processor in Uganda realizes about USh 300 per kilogram of refined cottonseed oil after paying a 70% tax to the government and currently about USh 8 per kilogram of cotton seed cake when sold on domestic markets. If the cake is exported for foreign exchange and the currency converted at Window II rates, (USh 270 = $1.00) the export price ex-oilmill would be US$ 29.63/ton which is very low in comparison to world market prices. Comparison of values in the USA and Uganda are as follows on each of the domestic markets:

PRICE	USA MARKET		UGANDA MARKET	
	$US	USh	$US	USh
Cottonseed Oil (Kg.)	.506	136.6	1.11	300
Cottonseed Cake (Kg.)	.18	48.6	.03	8

(exchange rate: US$1.00= USh 270)

The value of 1 Kg. of oil in the USA is 2.78 times the value of 1 Kg. of cake, while oil in Uganda is 37 times the value of cake. The cake should eventually be utilized in the Uganda livestock industry and with broilers selling for USh 1100 per kg. ($1.85 lb. vs. $0.39 to $0.49 per lb. in the USA) cottonseed cake at $30/ton is cheap.

PRODUCT YIELD & ANNUAL PRODUCTION
COTTON SEED OIL EXTRACTION PLANT

Production: 60 ton/day capacity X 250 days = 15,000 tons cottonseed

Product	Yield from Cottonseed-%	Annual Productio Metric Tons
Oil	15.2%	2,290
Soap	.6%	96
Cake	59.2%	8.880
Hulls) Lint) FUEL Waste)	25.0%	3,734
Cottonseed	100.0%	15,000 Tons

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PROCESSING MARGIN PROJECTION/TON

PRODUCTS	% YIELD	USh PRICE KG	USh REVENUE
Oil	15.2	300	45,600
Soap	.6	200	1,200
Cake	59.2	8	4,736
(waste)	25.0		
Gross Value of Products	75.0		51,536
Cost of Cottonseed	100.0 %	15	(15,000)
Gross Margin			36,536
Supplies (Window II rates)			(5,673)
Manufacturing Expenses (Yr. 2) (Incl. interest)			(8,533)
NET MARGIN			USh 22,330 ton

Cash Inflows in the following calculation of the internal rate of return are based on 15,000 tons crushing per year. The net margin figure of USh. 22,330 per ton is converted to US$ at rate of 300:1, or about $74.50/ton. $74.50 X 15,000 = $1,117,500.

(Source: USAID/Kampala Consultant Report "Oil Seed Processing-Uganda, May, 1983).

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Year	Investment	Annual Cash Inflows	
	5000000	0	Internal Rate of Return
1		1117500	
2		1117500	
3		1117500	
4		1117500	18.3%
5		1117500	
6		1117500	
7		1117500	
8		1117500	
9		1117500	
10		1117500	
11		1117500	
12		1117500	
13		1117500	
14		1117500	
15		1117500	
16		1117500	
17		1117500	
18		1117500	
19		1117500	
20		1117500	
21		0	
22		0	

ANNEX C

FINANCIAL ANALYSIS

Introduction

Preparation of the financial analysis reviewed the potential project participants (the ICI(s) and their clients) on management capability to effectively use the RPE funds and an estimate of how the RPE project will affect the viability of the participants. There are two basic components in this project: (1) a line of credit to ICI's for on-lending to viable enterprises, and (2) technical assistance to strengthen both the ICI(s) and their clients under the project. The assessment of financial viability was made relative to the institutional capability of the ICI's identified as participants in the project. Individual assessments of illustrative examples of typical sub-loan (enterprises) can be found in the appendices in the Economic Analysis, but conclusions about the potential for profitability of actual loan applications are not included in this financial analysis. The ICI's using their established loan criteria and procedures and AID's general criteria will evaluate loan applications relative to their financial and technical viability. The success of RPE in financial terms will be determined by how well the ICI(s) manage the line of credit provided them under the project. The technical assistance component of the project will also contribute to the success for both the ICI(s) and the sub-loan beneficiaries.

Background

Uganda had a history of a well developed banking sector during both the pre- and post-independence period up too the 1970's. Several international commercial banks, including Standard Bank, Barclays Bank, Grindlays Bank and Bank of Baroda, maintained full banking services throughout much of the country. The Cooperative Bank of Uganda also provided commercial banking services for its clients. The commercial banks catered for agricultural clientele besides their usual industrial and trade accounts. When the Uganda Government formed the Uganda Commercial Bank (UCB), much of the branch network of the commercial banks was taken over, and UCB became the dominant bank together with the Cooperative Bank in the rural areas. The overseas commercial banks now limit most of their activity to Kampala, although they have retained many of their agricultural clients. The GOU has recently encouraged the commercial banks to consider re-establishing branch banks. Grindlays is considering the reopening of a Jinja branch.

Recent upheavals in the financial environment of Uganda* have had a profound effect on the financial sector and banking system in the country. Banks now generally face a severe liquidity crisis. Bankers attribute part of this problem to delays in

* Brought about in part by what is in effect a float of the Uganda shilling through weekly auctions of foreign exchange to the public.

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payments from the government to their various suppliers. Another factor is that outside major urban areas, the commercial banking system is not operating efficiently, therefore, most trading must be carried out on a cash basis thereby requiring large quantities of physical cash to be available for business transactions. Recent increases in interest rates have not produced a noticeable increase in deposits, and this situation will most likely continue if interest rates remain negative in real terms relative to the current rates of inflation. However, real progress is being made in bringing down the rate of inflation and if this trend continues, there will be more incentive to save.

<u>Table 1</u> Annual Inflation Rates

1970-75	19.24%
1975-79	56.74%
1979-80	107.23%
1980-81	92.80%
1981-82	44.87%
1982-83	30.00 (est)

(GDP deflator) Source: Uganda Country Economic Memorandum-IBRD, December, 1983.

As the inflation rates have been declining since 1980, interest rates have been increasing with the most favorable rates for the borrower in the agricultural sector. There continues to be a liquidity problem in the commercial banks as so much money must remain outside the banking system to support commercial trade activities. Interest rates for the period 1980 to present are presented in the table below:

<u>Table 2</u> Interest Rates (%)

	Dec/1980	Dec/1981	Dec/1982	June/1983
Rediscount rate	7.0	9.0	10	12
Treasury bills (90 day)	5.1	9.0	12	12
Savings Deposits (minimum)	3.0	8.0	9	11
Lending Rates (maximum)				
-Agriculture	8.0	13.0	14	16
-Export & Manufacturing	12.0	14.0	15	17
-Commerce	12.0	15.0	20	22
-Unsecured	12.0	17.0	20	22

According to recent World Bank reports, the GOU has kept within the limits of growth for domestic credit as established in consultation with the IMF. Furthermore, IBRD projected Uganda's foreign aid requirement for 1982 to be $400 million, and $450 million in 1983. Actual receipts were about $360 million for each of those years.

Financial Soundness

AID is funding this project on the basis of a grant to the GOU. Of the $19 million grant, $12.5 million will be used as a line of credit passed through the Bank of Uganda (BOU) for on-lending by the UDB and other participating ICI's on commercial terms to productive enterprises. The ICI's will receive payments on their outstanding loans according to their established lending criteria. The ICI's will borrow these funds from the BOU as long term loans, and repayment of interest will be annually with principle repayments starting after the tenth year. Repayment of borrowed funds by UDB and the commercial banks to the BOU would be placed in a separate account, and the disposition of these funds would be decided jointly by the BOU and USAID. Lending by UDB and the commercial banks would be within the normal lending criteria of each of the lending institutions in complying with general criteria and areas of lending as established under the RPE project.

Local contributions to the RPE are projected to be:

1.	UDB lending from own sources Est. requirement is 50% of the foreign exchange requirement	$5,000,000
2.	Commercial Banks participating as ICI. (50% minimum of loan in local currency from own resources)	$2,700,000
3.	Client equity investment (minimum 4:1 debt equity ratio on #1 & #2 above plus $12.5 AID grant).	$4,000,000
	Total	$11,500,000 (in L/C)

(local contribution will be about $11.5 million)

The RPE line of credit could leverage total funds for investment in enterprise development of more than $24 million when local currency ICI funds and equity contributions are considered. An additional amount of loan funds will be internally generated by the ICI's as their principal payments to BOU do not start until the tenth year, whereas client will be repaying principle much sooner. Over $3 million will be available for relending from client principal payments and interest earned in excess of administrative costs. (Ref. Appendix 1, Table 2)

Because the funds to be received by GOU are a grant, the financial soundness of the project can be insured by adjustments of the spread in interest rates of funds from the BOU to the ICI, and also on the rates, terms, and conditions of lending by the ICI to the target client groups. Smaller loans that have higher administrative and supervision costs can have a larger spread in interest. This can also be done for loans that are considered to be higher risk. The BOU has prepared a draft for the small loan guarantee scheme, and this draft is to be circulated to the proposed ICI's for their comments before final approval by the Board of the BOU. The BOU have proposed that the initial fund for the guarantee scheme to be USh. 500 million. BOU will seek external donor assistance to support this fund. GOU carries little risk from changes in foreign exchange rates as the repayments from the ICI will be in local currency. These repayments will be deposited in a special fund account which will circulate back to other approved development activities.

RPE Line of Credit

This component compliments the Government recovery program that is directed, in the short term, to the revival of the productive economic sector with a focus on rehabilitation and improved utilization of existing capacity. Preliminary reviews of loan applications pending in UDB indicate that there is demand for both foreign exchange and local currency. A review of a representative sample of UDB loans indicated that the local currency requirements of the loan were about 50% of the foreign exchange element. The client will be expected to put up a portion of this, but the UDB will require about $5 million in local currency. To support this local currency requirement, the BOU will make available the required local currency by purchasing discounted UDB commercial paper. This will provide the required liquidity to the UDB. Funds for the sub loan would pass through the Bank of Uganda to the UDB and participating commercial banks. The terms and conditions of lending by BOU to UDB and the commercial banks would provide for adequate margins to UDB and the commercial banks to enable them to cover expenses and earn reasonable profits on this lending. To encourage smaller loans and lending to higher risk clients, the BOU would provide larger spreads for these higher cost/risk loan categories.

Of the US$12.5 million designated for the loan program, approximately US$8.5 million will be allocated to the UDB, and the remaining US$ 4 million will be allocated to the commercial banks participating in the project. The terms of the loan from the Bank of Uganda to the UDB have been proposed initially at 6.5% interest with a 10 year grace period on repayment of principal, with interest to be paid annually. The long grace period allows the participating bank to build up internal reserves which can be relent. The UDB will draw down the loan over a five year period. UDB will pay interest annually to BOU, and equal principal payments after the grace period. The UDB (and commercial banks) will have access to the principal repayments from clients for relending during the grace period that they have on repayments to BOU. These repayments will be placed into a special fund (local currency). The loan amortization schedule for funds from BOU to UDB project a total payment into the local currency fund of the equivalent of about US$ 16 million by year twenty. If the payments to the local currency fund were re-deployed earlier in the project, there will be an increase in total funds generated.

By relending principal payments made to the UDB and approximately 50% of the net interest on loans, the UDB would increase the total amount of their loan fund to $11.3 million from $8.5 million originally received from BOU by year 10. The amount available for lending would start to decline as principal repayments are made to BOU. When the total loan has been repaid to BOU by UDB in year twenty, UDB will have generated additional $6.9 million in local currency as a result of this project.

Until year 10, all payments by UDB <and other ICI's> to BOU will represent interest payments only, which will amount to about $2 million in year 4, and $4 million in year 6. By the end of the project, payments to the fund by all ICI's will total to over $20 million. Part of this fund could be used for the loan guarantee scheme. (Refer to Appendix 1 for additional information).

Project Technical Assistance

The technical assistance component of the project can be sub-divided into three categories: (1) long-term staff, (2) short-term consultants, and (3) training activities. Technical assistance activities will affect the rate of loan disbursement and quality of loans approved. Pending loan applications with the UDB are inadequate and incomplete, thus making loan appraisal difficult for the Bank. Bank management officials and other members of the financial community were in agreement that while there were considerable good investment opportunities in Uganda, processing loan applications was difficult due to the poor quality of the loan application. Furthermore, it was also concluded that often an enterprise sponsor had adequate technical background and general management experience for the enterprise, however the client often lacked financial management, planning, and other related analytical skills.

The technical assistance component will address these shortcomings by providing business advisory and managerial services to RPE clients. During the start-up phase of RPE, the technical assistance team will assist the ICI(s) and the BOU in preparation of the requisite agreements, schedules of loan criteria, and managements systems required for RPE implementation. The technical assistance team will also undertake reviews, where warranted, of ICI(s) internal operations, loan review and approval procedures, and supervision capability. Short-term and in-service training will be provided to up-grade staff skills during both the start-up period and during the implementation of the credit component of the project. Assistance on off-shore and local procurement will also be provided by the TA team. The technical assistance team will be located outside the ICI(s) and provide assistance and training to both the ICI(s) and the clients. ICI(s) have expressed support for this arrangement in that they feel that their objectivity in appraising a loan application may be compromised if they were also responsible for preparation of the application.

While technical assistance is approximately one-third of the AID grant, when viewed in terms of a potential $25 million credit project when local contribution are included, and considering that project focus is directed toward medium-size enterprise, the importance of the technical assistance component providing training to banking staff and business/financial management assistance is appreciated. The clients of FRE loan funds will be paying the going market rate for debt equity. They require a comprehensive analysis of their proposed investment and the ramifications of any financial obligation resulting from a RPE loan. Had the institutional capabilities been stronger, the technical assistance portion of the project could have been smaller. The technical assistance component is necessairly large owing to the rehabilitation and training requirements of both the UDB and the RPE loan clients.

Intermediate Credit Institutions

The PID had identified the Cooperative Bank of Uganda (CBU) as a potential candidate for the intermediate credit institution (ICI). However, a subsequent study of the CBU indicated that it was financially weak and administratively inadequate for the RPE project. As an alternative, both the Uganda Development Bank (UDB) and the commercial banks were considered ICI's for the project. Discussions have been ongoing with UDB and Grindlays Bank since August, 1983, concerning their possible role as an ICI for the RPE project.

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APPENDIX 1, TABLE 1

PROJECTED AID
RTERLY DISBURSEMENTS

Quarter	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	Total
Total Disbursement	312500	312500	312500	312500	518750	518750	518750	518750	675000	675000	675000	675000	831250	831250	831250	831250	787500	787500	787500	787500	12500000
Total Cumulative	312500	625000	937500	1250000	1768750	2287500	2806250	3325000	4000000	4675000	5350000	6025000	6856250	7687500	8518750	9350000	10137500	10925000	11712500	12500000	
UDB Disbursement	212500	212500	212500	212500	318750	318750	318750	318750	425000	425000	425000	425000	531250	531250	531250	531250	637500	637500	637500	637500	8500000
CumulativeUDB	212500	425000	637500	850000	1168750	1487500	1806250	2125000	2550000	2975000	3400000	3825000	4356250	4887500	5418750	5950000	6587500	7225000	7862500	8500000	
Comm. Bank Disbur.	100000	100000	100000	100000	200000	200000	200000	200000	250000	250000	250000	250000	300000	300000	300000	300000	150000	150000	150000	150000	4000000
Comm. Bank Cum.	100000	200000	300000	400000	600000	800000	1000000	1200000	1450000	1700000	1950000	2200000	2500000	2800000	3100000	3400000	3550000	3700000	3850000	4000000	

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850 = first year disbursement
8 = average loan period
850 = repay to BOU x 10
.15 = UDB lending rate
.065 = BOU lending rate
.2833 = % int relent

APPENDIX 1
TABLE 2
($'000)

U.D.B. LOAN REPAYMENT SCHEDULE

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	
drawdown/onlent	850	1275	1700	2125	2550																
int relent		36	92	168	265	385	401	419	436	455	474	458	442	424	406	387	366	347	326	303	
	850	1311	1792	2293	2815	385	401	419	436	455	474	458	442	424	406	387	368	347	326	303	
		106	270	494	781	1133	1181	1231	1283	1232	1125	960	731	434	439	439	435	427	413	395	
			13	47	109	206	348	496	649	810	951	1057	1116	1109	1022	929	830	724	624	535	
				2	8	21	47	90	152	234	335	452	578	704	817	901	955	978	967	926	
					0	1	4	10	21	40	69	111	167	239	324	420	522	622	715	794	
						0	0	0	0	1	2	4	9	18	32	52	81	119	166	223	
							0	0	0	0	0	1	2	4	8	15	25	40	61	88	
								0	0	0	0	0	0	0	1	2	4	7	12	20	
									0	0	0	0	0	0	0	0	0	1	2	3	
disbursements	850	1417	2075	2836	3713	1747	1981	2245	2543	2771	2956	3044	3045	2933	3049	3147	3220	3265	3286	3287	
prin repay.		-106	-283	-543	-897	-1361	-1580	-1627	-2106	-2316	-2481	-2586	-2603	-2509	-2643	-2759	-2853	-2918	-2960	-2984	
prin repay to BOU											-850	-850	-850	-850	-850	-850	-850	-850	-850	-850	
end yr loan bal	850	2161	3953	6246	9061	9447	9848	10267	10703	11158	10782	10390	9982	9556	9112	8649	8167	7664	7140	6593	TOTAL
int earned at UDB	128	324	593	937	1359	1417	1477	1540	1605	1674	1617	1559	1497	1433	1367	1297	1225	1150	1071	989	24259
int onlent by UDB	36	92	168	265	385	401	419	436	455	474	458	442	424	406	387	368	347	326	303	280	6873
BOU loan bal	850	2125	3825	5950	8500	8500	8500	8500	8500	8500	7650	6800	5950	5100	4250	3400	2550	1700	850	0	
int paid to BOU	55	138	249	387	553	553	553	553	553	553	497	442	387	332	276	221	166	111	55	0	6630
PRIN + INT TO BOU	55	138	249	387	553	553	553	553	553	553	1347	1292	1237	1182	1126	1071	1016	961	905	850	
(cumulative)	55	193	442	829	1381	1934	2486	3039	3591	4144	5491	6783	8020	9201	10328	11399	12414	13375	14280	15130	

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400 = first year disbursement
8 = average loan period
400 = repay to BOU x 10
.15 = ICI lending rate
.065 = BOU lending rate
.2833 = % int relent

APPENDIX 1
TABLE 3
($'000)

COMM. BANK LOAN REPAYMENT SCHEDULE

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20		
drawdown/onlent	400	800	1000	1200	600																	
int relent		17	52	96	152	183	191	199	208	217	226	218	211	203	194	186	177	167	157	147		
	400	817	1052	1296	752	183	191	199	208	217	226	218	211	203	194	186	177	167	157	147		
		50	152	284	446	540	563	586	611	587	512	409	274	207	209	210	208	204	198	189		
			6	25	61	116	184	254	327	404	471	516	532	510	469	425	377	327	279	240		
				1	4	12	26	49	81	122	172	230	292	351	400	435	457	463	453	429		
					0	1	2	5	11	22	37	58	87	123	165	212	260	307	350	385		
						0	0	0	0	0	1	2	5	10	17	28	42	61	85	113		
							0	0	0	0	0	0	1	2	4	8	13	21	31	45		
								0	0	0	0	0	0	0	1	1	2	4	6	10		
									0	0	0	0	0	0	0	0	0	1	1	2		
disbursements	400	867	1210	1606	1262	852	966	1094	1239	1352	1419	1435	1402	1406	1459	1504	1537	1555	1561	1561		
prin repay.		-50	-158	-310	-510	-668	-775	-895	-1031	-1135	-1194	-1217	-1191	-1203	-1265	-1318	-1360	-1388	-1404	-1414		
prin repay to BOU											-400	-400	-400	-400	-400	-400	-400	-400	-400	-400		
end yr loan bal	400	1217	2269	3565	4317	4500	4691	4891	5099	5315	5141	4960	4770	4573	4368	4153	3930	3697	3454	3201	Total	
int earned at ICI	60	183	340	535	647	675	704	734	765	797	771	744	716	686	655	623	589	555	518	480	11776	
int onlent by ICI	17	52	96	152	183	191	199	208	217	226	218	211	203	194	186	177	167	157	147	136	3337	
BOU loan bal	400	1200	2200	3400	4000	4000	4000	4000	4000	4000	3600	3200	2800	2400	2000	1600	1200	800	400	0		
int paid to BOU	26	78	143	221	260	260	260	260	260	260	234	208	182	156	130	104	78	52	26	0	3198	5242
PRIN + INT TO BOU	26	78	143	221	260	260	260	260	260	260	634	608	582	556	530	504	478	452	426	400		
(cumulative)	26	104	247	468	728	988	1248	1508	1768	2028	2662	3270	3852	4408	4938	5442	5920	6372	6798	7198		

Table 4 Estimated Employment/Cost per Job

Activity	Units	Job/ Unit	Unit Cost	Total Costs	Total Jobs	Cost/ Job
Dairy Farms	20	20	60,000	1,200,000	400	3,000
Hatchery (New)	3	20	100,000	300,000	60	5,000
(Rehab)	3	20	40,000	120,000	60	2,000
Poultry Farms	40	6	10,000	400,000	240	1,666
Wankoko	1	40	300,000	300,000	40	7,500
Oil Mills (New)	1	47	2500,000	2,500,000	47	53,200
(Rehab)	3	47	1000,000	3,000,000	141	21,275
Feed Mills	10	10	50,000	500,000	100	5,000
Fishing	10	4	8,000	80,000	40	2,000
Mixed Farms	20	20	50,000	1,000,000	400	2,500
Totals	111			$9,400,000	1,528	$ 6,150

Notes:

Average Loan Size is $84,685 (excluding oil mills $36,111)

Dairy Corporation funding for supply of inputs not included.

Only direct employment counted. Significant secondary employment also created, especially in the oil mills. It is anticipated that several thousand farmers will grow oil seeds and cotton which will be processed in the oil mills.

Notes to Appendix 1, Tables 2 & 3

1. For the purpose of projecting the utilization of Project funds, the amounts were arbitrarily set at $8.5 million for UDB, and $4 million for the commercial banks. Drawdown of funds would be phased as over five years.

2. The ICI's (UDB and commercial banks) would receive funds from the BOU at 6.5% per annum. Repayment by the ICI's to the BOU would commence in Year 11 and continuing for 10 years. Repayments will be in equal installments.

3. Sub-borrower loans were projected to be eight years average, one year grace on principal repayment, and installments in equal portions.

4. The ICI's will make annual interest payments to BOU. Interest on sub-borrower loans calculated for purpose of this exercise is 15% per annum, however, it expected to be in range of 17-18% by time disbursements actually start. A 15% sub-borrower interest rate will provide a 8.5% spread for the ICI.

5. The assumption is made that the ICI's can cover loan administrative costs including a provision for bad and doubtful debt with 4.25% of interest. Therefore, the 15% sub-borrower interest rate will provide an additional 4.25% to the ICI which will be re-lent. This internally generated source of additional lending will grow to about $400,000 by year 6 for UDB and declining to $300,000 by the end of the 20 year projection period. The same applies for the commercial banks participating on a basis proportional to the amount of funds they receive under the project.

6. The average amount available to UDB from the 4.25% on total loans outstanding resulting from Project funding will be $528,000 per annum over 20 years. For the commercial banks, the combined average amount per year is $262,000.

7. At the end of 20 years, when all obligations to BOU have been repaid, the UDB will remain with an internally generated capital fund of $6.5 million in local currency. The commercial banks would have generated $3.2 million. These funds come from the internal growth as the result of relending interest (refer to note 5 above).

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Table 5 Sub-Loan Project Activity Starts

Activity Year	1	2	3	4	5	Total
Dairy Farms	2	4	5	5	4	20
Poultry Hatchery (Rehab.)	1	1	1			3
(New)			1	1	1	3
Poultry Farms	3	6	12	12	7	40
Wankoko Poultry Plant		xxxxxxxxx				
Dairy Corp Input Supply	xxxxxxxxxxxxxxxxxxxxxxxx					
Gulu Oil Mill			xxxxxxxxxxx			
Oil Mill Rehabilitation		1	1	1		3
Feedmills	1	2	3	2	2	10
Commercial Fishing	1	2	3	2	2	10
Mixed Farms	2	4	5	5	4	20
Other Industrial	xxxxxxxxxxxxxxxxxxxxxxxx					
Com. Bank Projects	xxxxxxxxxxxxxxxxxxxxxxxx					

Estimated Unit Investment Cost:

1. Dairy Production Unit $60,000
2. Poultry Hatcheries
   a. New Units $100,000
   b. Rehabilitation 40,000
3. Poultry Production Unit 10,000
4. Wankoko Processing 300,000
5. Dairy Corp. 700,000
6. Gulu Oilseed Plant 2,500,000
7. Rehab. Oilseed Plant 1,000,000
8. Feedmill 50,000
9. Fishing Unit 8,000
10. Mixed Farm 50,000

<u>Estimated Funds Required Per Year</u>

Year One	$1,250,000
Year Two	2,075,000
Year Three	2,700,000
Year Four	3,325,000
Year Five	3,150,000
Total	$12,500,000

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Annex F

<u>Institutional Analysis</u>

UGANDA DEVELOPMENT BANK

A. HISTORY

The Uganda Development Bank (UDB) was estalished in 1972 with an input of Sh 100 million from the Government of Uganda (GOU). It was to assist in the development of agriculture, industry, tourism, housing and commerce. It was to provide such assistance in the form of short, medium and long term loans, equity and other share investments, guarantees, and managerial and technical advice. It was also to administer a credit guarantee fund consisting of contributions from GOU and banks, for assisting marginal borrowers in raising funds from banks and credit institutions.

UDB's inception coincided with the mass exodus in 1972 of non-Ugandan citizens, and the allocation of their trading and small manufacturing businesses to new owners without the requisite business experience. These new owners were unable to obtain finance from the commercial banks because they were largely unknown, and UDB was therefore requested by Government to lend to them. UDB therefore started by playing a non-developmental role of providing short term commercial credit. Its role has however not been limited to this. As envisaged under the decree, it has played the role of a multisector development bank by providing long term project finance in the agricultural, industrial, transport and tourism sectors. In addition it has managed two funds (including one for beef ranching development financed under an IDA credit) on behalf of Government.

Government intends to build UDB into its major development bank with a substantial role in investment financing in key sectors. In future therefore, UDB will concentrate on medium and long term development lending for commercial agriculture, medium and large industries, transport and tourism. Its role in lending to commerce and small industries has discontinued.

The problems which existed under the Amin Administration and the looting and destruction which occured during the War of Liberation, seriously undermined the quality of the UDB loan portfolio. The new administration has decided to undertake a serious reorganization of UDB to make it into the kind of development bank it was intended to be. The Government also agreed to a comprehensive reorganization program funded by UNDP and executed by the World Bank, including the assignment of 6 expatriates to key line positions within the bank. The West German govenment is planning to provide two credit specialist (one livestock and one corps credit specialist).

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One of the most important obstacles impeding the UDB from carrying out its development role has to do with questions of ownership of client enterprises. UDB can not responsibly lend to enterprises whose ownership is in dispute. There are many enterprises marked for rehabilitation waiting for the GOU to resolve the issue of ownership. The longer the Government delays on this question the more difficulty UDB will have in meeting its targets for disbursing rehabilitation funds. This is seriously impeding the rehabilitation of productive enterprises in Uganda in the industrial sector. This is much less a problem in the agricultural sector as few of the agricultural loan applications pending with UDB involve ownership disputes.

The GOU has formed a committee to review all such applications. UDB is encouraging this committee to decide on the larger more important cases first, especially for potential UDB clients, and not to wait until a decision is reached on all cases prior to announcing their decisions.

B. STRUCTURE

STAFFING:

Appendix 6 shows the newly created organization structure of UDB. The Department of Supervision and Monitoring shown in table 1 was established in early 1984 and is now operational. In order to ensure that addequate attention is given to client supervision, the UDB want to keep the supervision function seperate from the appraisal function which will be done by the combined Livestock and Crops Departments.

The UDB's board is appointed by the Minister of Finance and consists of up to seven members, including the Governor of the Central Bank and the Secretary of the Treasury as permanent ex-officio members. The decree establishing UDB stipulates that Board members should have experience in banking and financial matters. This requirement is being broadly interpreted. The current board was appointed in September 1983, and consists of the following people:

Mrs. C. Ogwal	Chairman
Hon. M.B.Asubo., M.P.	Director
Hon. A. Kadumbe-Mukasa, M.P.	"
Hon. I.O. Malinga, M.P.	"
Mr. W.J. Magambo	"
Mr. E.E. Wako	"
Secretary to the Treasury	"
Governor, Bank of Uganda	"

Given that a number of directors including the chairman come from a political background and do not have the banking and financial background originally intended under the decree establishing the UDB, there will be concern about possible undue political considerations in UDB policy and management decisions. AID will reserve the right to review and approve all loans in excess of $100,000 being financed under the project.

As part of the reorganization plan sponsored by UNDP and the World Bank, 6 senior positions at the bank will be filled by expatriate personnel. These are as follows:

			Department
1.	Assistant General Manager		- Operations
2.	Assistant General Manager	(vacant)	- Finance
3.	Chief Accountant	(vacant)	- Accounts
4.	Industrial Engineer		- Industry
5.	Financial Analyst		- Industry
6.	Industrial Economist		- Industry

A candidate has been identified to fill the position of Assistant General Manager-Finance and is expected to take up this position in July, 1984. His comes from a commercial banking background in Canada, is a CPA, and has recent banking experience in Nigeria.

In April, 1984, UDB had 58 professional staff, assigned as follows:

	TOTAL
General Manager's Office	4
Internal Auditor	2
Operations	
a. Crops	6
b. Industry	11
c. Livestock	16
d. Research (not operational)	
Secretariat	5
Finance and Administration	
a. Accounts	4
b. Admin. & Personnel	6
Supervision	4
TOTAL	58

At 1 September 1981 there were approximately 40 professional staff. The 18 additional positions have been created as part of the program to prepare UDB for a much more expanded and active role in financing the country's rehabilitation. Breakdown of staff within individual departments and qualifications of senior staff are provided in Appendix 6.

In addition to the expatriate assistance, there is also be a program of external fellowships for training UDB staff. For the 1983/84 period UDB has developed a training and development programme to be financed with $258000 granted by UNDP. The programme includes conducting in Uganda of introductory Livestock/Agricultural/Industry projects courses lasting 4-6 weeks for about 20 newly recruited UDB professional staff. Provision has also been made for sending about 12 UDB employees to 8-9 week seminars organized by the following overseas institutions:

a. EDI-European Development Institute
b. ADB-African Development Bank
c. Bradford University
d. Irish Development Authority
e. Development Banking Centre, New Delhi

UDB have made adequate staff provisions in the Industry Department. Yet, by UDB's own admission, their Crops and Livestock Departments require strengthening. Both of these departments need up-grading in financial skills, especially project analysis. The newly formed Supervision and Recovery Department is critical to successful UBD operations and will also require strengthening. UDB is requesting that USAID provide under the project technical assistance in this area.

UDB has adequate lines of credit to cater for the present and medium-term needs of the Industrial Department, and do not anticipate the need for additional credit under RPE for Industrial loans. Additional credit could not be effectively utilized with existing staff limitations in this department. UNDP/IBRD have a team of technical experts assigned to the Industrial Department of UDB providing services and training to strengthen the capability of this part of the bank.

A review of current loan applications pending with UDB in the Livestock and Crops Departments indicate considerable demand for credit facilities. While the technical skills relative to crop and livestock production appear to be adequate at the UDB, the level of experience and expertise relative to financial appraisal of agricultural projects is inadequate. UDB would benefit from having an experienced agricultural financial analyst to provide technical assistance in loan appraisal and training to UDB staff. The RPE project would provide this technical assistance in the form of one specialist serving in a line position for a period of three years.

The West German Government have recently informed UDB that they will be filling a long outstanding request from UDB for two advisors in the agricultural section of the bank. The two position to be filled are:

1. Livestock credit specialist

2. Crop credit specialist

To further improve on the procedures for project appraisal, it is recommended that the Livestock and Crops Departments be combined into one Agricultral Department. Many of the pending applications are for mixed farms making it difficult to determine which department should have loan appraisal responsibility. Seperate appraisal is counterproductive.

The reorganization of the Livestock and Crops Departments together with the proposed technical assistance would enable this section of the UDB to effectively appraise and supervise the loan applications proposed for funding by the RPE project.

Policies:

UDB limits its exposure per project to the lowest of:

a. 80% of the project's cost
b. 20% of UDB's net worth

It will not normally finance projects with debt/equity ratios exceeding 5 to 1, and if necessary will make equity investments to keep the financing plan of projects within this limit.

UDB has the stated policy of not accepting any foreign exchange risk. Yet the EEC credit leaves UDB with this risk and they incurred a USh 193 million exchange loss on this credit in 1983. UDB is now renegotiating this credti. According to UDB officials the GOU bears the exchange risk on the IDA and OPEC credits. However, it appears that certain BOU officials look on the UDB as a GOU institution which is as capable as any other GOU financial institution to absorbe the exchange risk. The issue of where the foreign exchange risk is lodged is a critical matter and requires resolution. Commitments of foreign lines of credit may soon reach $ 130 million (see Appendix 4).

Depending on the economic sector in question and GOU pricing policies, devaluation of the shilling could substantially increase the final borrowers debt service required on these loans. The UDB is taking the position that changes in exchange rates will be fully reflected in prices, and that debt service, as a % of the borrower's revenue, is likely to remain constant. This seems to be a very optimistic assumption which if proven wrong could result in many defaults.

Obviously it is very difficult to predict what the final effect of all these factors will have on the borrowers ability to repay. But it is interesting to note that during August, 1983 the exchange rate was in the area of Sh 270 per $1.00, and in November, 1983 it was Sh 330 per $1.00. This would increase loan balances by 20% over a 4 month period. Debt service on foreign exchange denominated loans, as a per cent of the borrowers total revenues, is most likely to become more burdensome.

Under the RPE project, clients will repay loans in local currency based on the prevailing exchange rate at the time of their drawdown with no foreign exchange exposure being passed to the loanee.

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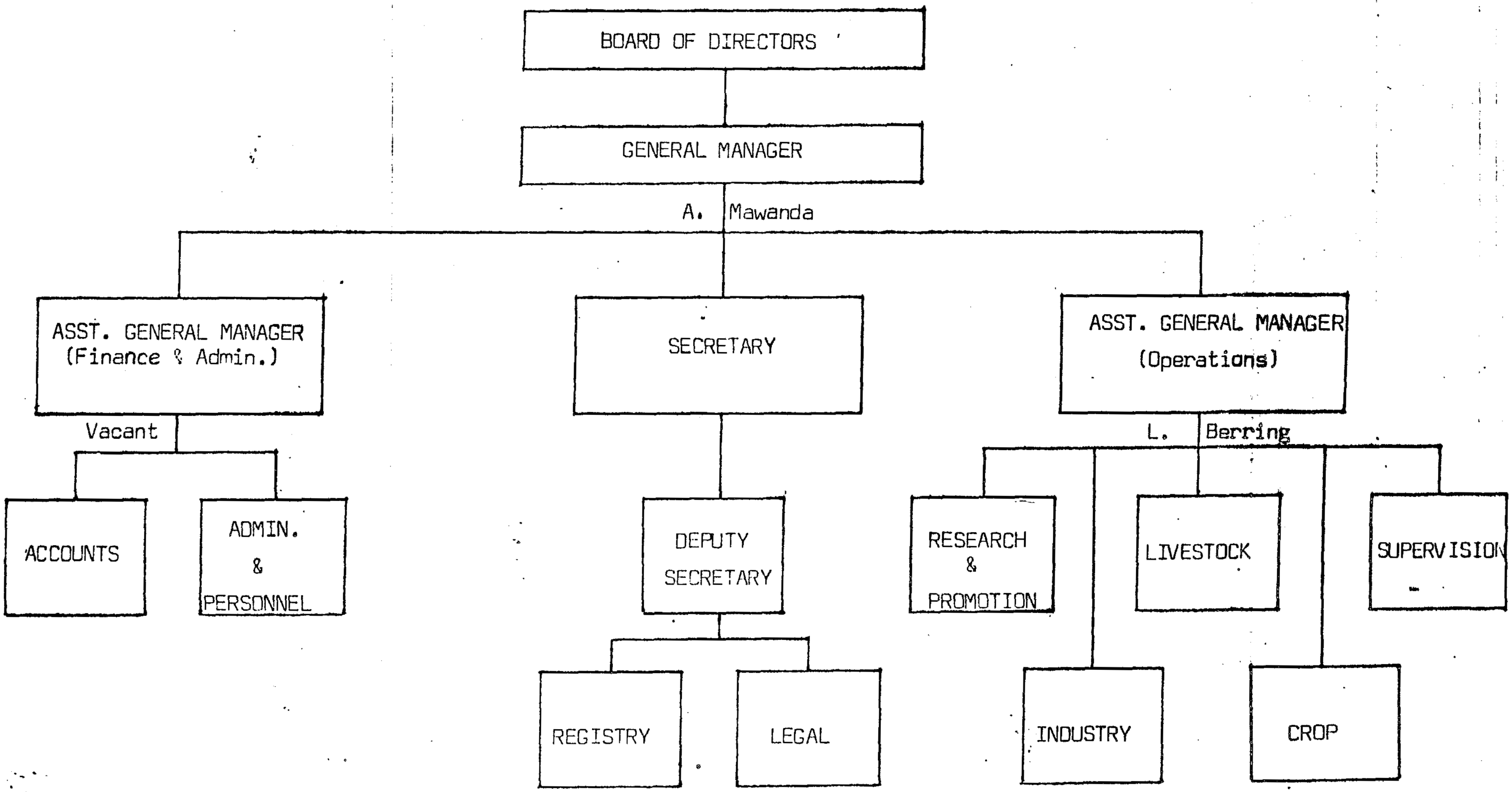
UGANDA DEVELOPMENT BANK

ORGANIZATION CHART



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Loan Processing Procedure

Some 14 steps have been identified in processing an loan application in the UDB. All processing is done now in the bank's head office. A description of the different steps is given below:

1. A standard application form is purchased from the UDB. This form, together with supporting documents stipulated in the UDB form, are completed and submitted to UDB. Supporting documents include:
   a. copy of Articles of Incorporation or Certificate of Registration,
   b. copy of Income Tax Clearance Certificate,
   c. copy of current operating license(s)
   d. copies of latest accounts--Profit and Loss, Balance Sheet,
   e. copies of bank statements for past six months
   f. list of title deeds, debentures, loan agreements, and contracts.

If a feasibility study has been prepared, a copy is to be sent to the UDB with initial application. Copy of application form attached.

2. The application is logged in at the General Registry, and forwarded to appropriate Division in UDB. The application is screened at this point, and one of three options exercised--
   a. cut if not a suitable project for UDB consideration,
   b. hold pending receipt of additional information,
   c. applicant called for personal interview.

3. Option "c" must be selected for application to continue. During the interview, the planned investment is discussed by the applicant with a loan officer.

4. If applicant is successful with personal the interview, then arrangements are made for a loan officer(s) to visit project site. This also serves a an opportunity to verify physical property and other aspects of the initial application.

5. Preparation of appraisal report--done by the loan officer assigned to the application with assistance from other specialized personal (financial analyst) in the Division.

6. Division Committee Review of application and appraisal report-committee composed of Head of Division, Senior Loan Officer in charge of section, and loan officers who made site visit. Meetings called when 3 or more applications ready for review. This committee has three options:

   a. reject the project,

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b. return to client or appraisal staff for additional work,
c. recommend application to Operations Committee.

7. Operations Committee--meets weekly, and chaired by the Ast. General Manager, Operations. Members include all the Heads of Divisions, and the Head of Supervision as secretary. A summary of the project is presented by the loan officer in charge of the appraisal. If the loan application is approved, it is forwarded with a recommendation to Policy and Investment Sub-Committee of the Board of Directors.

8. Policies and Investments Sub-Committee-made up of three directors of the Board of which one is chairman. A representative of the Governor of the BOU and the General Manager of the UDB also members. Projects are presented by the Ast. General Manager-Operations. This amounts to the final review of the project, but one additional approval step is required if the project is recommended by this sub-committee. Meets every one-two months.

9. Board of Directors--final approval based on recommendations of the Policy and Investment Sub-Committee. Intervals for meetings to confirm loans sometimes up to three months. No loan offers can be made until loans confirmed by this Board

10. Secretary of the Board approved loans, and sends written notification to the Department Head. The Board reserves the option to add conditions to the loan (security requirements, right to approve management).

11. Department Head prepares a Letter of Loan Offer (example enclosed) giving conditions and disbursement schedule. This letter is sent to applicant.

12. If terms and conditions acceptable to applicant, the Letter of Offer is signed and returned with security documents (title deed).

13. Legal Department of UDB then prepares instruments to register a charge on the title deed(s) and forwards documents to Ministry of Justice to be registered.

14. When documents returned from Ministry of Justice, UDB then informs applicant and requires a 1% commission on total loan to be paid by applicant to UDB. Disbursement according to schedule then commences.

The time required for completion of the entire process, assuming that the application continues to move forward with being returned for additional work or information, is estimated to be six months with current volume of work in UDB. With increasing applications in the agricultural division, it is anticipated that the processing time will be even longer once a number of applications start to enter the system. There will also be applications which must be returned for additional information and analysis.

It is being proposed that during the early part of the project, a development banker work with the agricultural division to improve procedures in loan processing. It is furthermore recommended that consideration be given to delegating authority for a specified level of lending to be approved and authorized by executive staff of the UDB. Routine agricultural loans which fall into the approved categories of UDB lending would be more efficiently handled by the executive staff of the bank. Members of the Board of Directors have limited professional experience in finance and banking, and hence their contribution to the loan approval process is more likely to be in ensuring that lending complies with overall bank policy.

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The following extract from the 20 april 1982 Staff Appraisal Report (P 14) carried out by the World Bank on UDB in consideration of a new $ 35 million line of credit, adequately describes loan processing procedures.

"UDB already has well established procedures for processing projects. Its bye-laws prescribe that all applicaitons for financing should be made on a standard form. In addition sponsors are required to submit detailed feasibility studies if available. All applications are preappraised to quickly eliminate those which do not fall within UDB's mandate, and those where the state of preparation by the sponsor indicates that immediate consideration is not merited. Projects which are not rejected after preappraisal are appraised according to guidelines which are adapted to the needs of the sector and the project size. For small industry, commerce and small agricultural loans (these have accounted for a substantial proportion of the number of loans UDB has considered), UDB's appraisal is limited to basic commercial and financial analysis, and has adequately addressed issues. UDB's appraisal of large scale industry projects is comprehensive, and includes calculation of financial and economic rates of return. Because of the very small number of such projects that have been undertaken in Uganda since UDB's inception, its experience in undertaking such comprehensive appraisals has not been very extensive, and it will need some guidance and assistance, expecially in technical and economic evaluation, to appraise the larger number of projects to be financed under the proposed credit. This assistance would be provided by consultants and by IDA in its review of subprojects. All appraised projects are reviewed by an investment committee chaired by the General Manager and consisting of all division heads. This committee is responsible for making final recommendations on loans for approval by the Board."

"UDB's supervision procedures call for quarterly visits to each borrower. In practice, this has not been possible because of the security situation and transport difficulties. Clients around Kampala have therefore tended to be adequately supervised while those in distant areas have generally been barely supervised. This is a problem which is faced by all financial institutions in Uganda, and will only be resolved with general improvements in the security and transport situations."

C. FINANCIAL

PAST

Appendix 1 is a summary of UDB's income and expenditure statement for 1978 through first quarter of 1984. Appendix 2 shows the balance sheets for this same period. UDB incurred losses each year from 1978 through 1983, with a cumulative loss at 31 Dec 1983 of Sh 729 million; the total share capital at the time was Sh 1143 million. Outstanding loans during this period has grown substantially from Sh 125 million to Sh 2358 million. Most of this growth occured during 1983 when UDB began heavily utilizing foreign lines of credit. The growth in borrowings increased from Sh 9 million in 1980 to Sh 188 million in 1981 to Sh 817 million at the end of 1982 to Sh 3241 million in 1983. Appendix 3 is a historical statement of sourses and application of funds.

It should be pointd out that a 70% provision for bad debts was made in 1980. This represented a potential write off of Sh 90 million, out of a total of Sh 134 million. Yet current experience indicates that this provision is probably excessive. Loans put on UDB's books prior to the float of the shillings can now be repaid with greatly devalued shillings. These borrowers are voluntarily clearing these old debts in order to be eligible for new loans.

As with other institutions in Uganda, the UDB suffered from the chaos of the 1971 to 1981 period. Accounting standards were poor during this period and this has resulted in qualified audits for 1980 and 1981. A primary reason for the qualification is that UDB could not produce a list of individual loan balances, showing specific allocation for bad debts. The accounts department is actively working on this problem.

PRESENT POSITION AND FUTURE PROJECTIONS

The draft audit for 1983 has been completed by Price Waterhouse and is being reviewed by UDB. Appendix 5 is a copy of the 1983 draft audit. The most noteworthy elements of the 1983 draft audit are as follows:

1. A 16 fold increase in foreign borrowings over two years, Shs 201 million (1981) compared to Sh 3241 million (1983). At the end of 1983 the total foreign lines of credit avalable stood at Sh 16,642 million (compared to Sh 1920 million for 1981).

2. A net loss for the year of Sh 473 million compared to a loss of Sh 110 million for 1982. Significant increases in administrative expenses account in part for this increased loss. UDB is maintaining a larger staff (especially in agricultural) anticipating increased lending in this area.

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3. There was a loss of Sh 74 million in the Ranch Rehabilitation Program. This was due to stolen goods (purchased by UDB), death of cattle, and an "apparent" foreign exchange loss. Because of movement in foreign exchange rates, an exchange loss is carried on the books until the goods are sold when their full value is recovered.

4. Under th EEC line of credit, the UDB is not permitted to pass exchange risks on to the borrower. This resulted in a Sh 193 million exchange loss in 1983. UDB is making efforts to renegotiate the terms of this credit.

5. UDB's operational efficiency has improved during the year and they are making progress in solving various problems and the implementation of improved systems.

6. With respect to income, it is worth noting how UDB accounts for interest income. UDB accrues interest only on loans guaranteed by GOU. On other loans it accounts for interest income only when the money is actually received. The 1983 interest income from loans was Sh 176 million, yet this contains at least Sh 144 million of accrued income on GOU guaranteed loans.

Appendix 4 shows the approximate position of UDB's Industrial Department at 31 December, 1984 with respect to foreign lines of credit.From this table one can see that the focus of UDB's current lending policy is on industrial rehabilitation. The focus of the UNDP assistance to UDB has been on strengthening the staff in the Industrial Department in preparation for this increased lending activity. Yet even with the external assistance (expatriate engineer and economist) it is not likely that the Industrial Department could responsibly administer any more credit beyond the $106 million which is now available. On the other hand the Crops and Livestock Departments do not have such large credits.

There is only one foreign line of credit (ADB II <Ranch Rehabilitation Project> for 10 million units of account (estimated to be $13 million) which is available to the Livestock Department. This credit has now been almost fully disbursed, and the workload in this department is drastically reduced. No lines of credit are available to Crops Department. These two Departments now have a significant excess of staff, some of whom will be transferred to the new Supervision and Recovery Department. The RPE credit can be staffed from existing personnel.

Another line of credit is the Kuwait Fund Loan ($25 million) which dates back to the time of the Amin administration. It was originally intended that these funds should go to financing large livestock projects. These funds should have been disbursed by the Ministry of Agriculture but for various reasons they were

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unable to do so and this line of credit has remained dormant. The UDB has been given the task to re-activate this fund and a meeting took place in December 1983 to discuss the issue. The general outcome of that meeting is that the Kuwait would like these funds to be used to rehabilitate the parastatal Uganda Livestock Industries, Ltd. <ULI>-(large scale government stock farms). A condition to the credit is for local banks to put up 25% of the amount in local currency for working capital for ULI, but it is doubtful is any local bank would be willing to put up working capital for ULI as their financial position is very poor.

An issue of considerable importance to the successful implementation of UDB's loan program is their ability to mobilize local currency. The best use of foreign lines of credit is for the importation of needed foreign goods, such as factory equipment. Yet the importation of such equipment is only part of a typical rehabilitation loan package. The installation and utilization of such equipment requires local construction, working capital, and other uses of local currency. The Development Finance Department of the Bank of Uganda said that the BOU will make available local currency to the UDB, however consideration should also be given to using part of the RPE funds for local currency requirements, especially when items previously thought to be available only through direct importation become available on the local market. Rather than to explicitly state that RPE funds be restricted to only off-shore pruchases, it is more important to ensure that the total financing package of a client's project contains the mutually agreeable portions of equity contribution, local ICI finance, and RPE funds.

In most cases the loan package from UDB will have to include the local currency portion as well as the foreign currency. Recent estimates by the industrial department of UDB indicate that for every $ 1 of foreign exchange $ .50 of local currency may also be required. The Industrial Dept. currently has foreign lines totaling $106 million (Appendix 4) this may require as much as Sh 17 billion in local currency to implement these loan packages. The combined savings of all the commercial banks in Uganda does not total Sh 17 billion, and all of these deposits are being fully utilized in their own loan portfolios. Currently there is no excess liquidity in the Uganda banking system.

A condition to the IDA loan was that UDB share capital be increased by the government. A condition to this credit was an increase of USh 100 million per year for three year. This condition has not been met. The IDA credit also provided that the first $10 million of the $30 million credit disbursed would be converted to equity in the UDB. UDB engaged the services of an international consulting firm, PE International, to appraise major loan application in the industrial sector, and now have appraised projects which will commit about half of the IDA credit ($15 million).

Eventually principal and interest repayments from UDB loans will be sufficient to provide the shillings needed to implement new projects. Yet, due to the grace periods provided for in most UDB loans these loan repayments will not be significant in the initial years.

It is likely to be very difficult for UDB to mobilize the local currency needed to execute their existing foreign lines of credit. Because of this situation USAID may wish to channel shillings generated under other USAID programs to the UDB for use as local cover needed to implement RPE loan packages.

The duration of these foreign lines of credit and the terms of UDB's lending policies creates another problem exposing UDB to foreign exchange risks. The average sub-loan under UDB's various foreign lines of credit is for 5 1/2 years, but the average repayment period for these lines is 13 years. The borrowers obligation ends with the repayment of his loan after 5 1/2 years. During the remaining 7 1/2 years UDB may be exposed to the foreign exchange risk on such loans. The management of UDB say they will come to an arrangement with GOU to be free of such exchange risk. Yet, to date, no such arrangement exists.

D. Loan Recoveries

UDB's success as an ICI will depend on its ability to properly appraise and supervise loans and keep defaults to reasonable minimums. Considerable effort is now underway in upgrading and streamlining UDB operations. The past gives no indication of what UDB's performance is likely to be in the future. The bank is undergoing a period of substantial transformation.

Nevertheless, current information at UDB indicates that all the changes and upgrading that has been taking place at UDB has not yet resulted in an improvement in loan recoveries. Because of grace periods very little of UDB's loans have any principle due, yet interest is to be paid. It was already mentioned that about 82% of 1983 interest income was accrued, not collected. If one takes into account the uncollected interest (Sh 133 million) on other loans (not guaranteed by GOU) this percentage increases to 90%.

UDB financial performance for the first quarter 1984 also indicates poor recoveries. During the quarter UDB expected loan recoveries (primarily from interest and delinquent loans) of Sh 339 million. Actual recoveries were less than Sh 5 million.

The Supervision and Recoveries Department needs to be substantially improved before UDB will be a viable self-sustaining institution. The strengthening process is still underway. If UDB can not improve its recovery rate, funds currently planned for onlending through UDB should be channeled through other ICI's. The Project Agreement with GOU should spell out certain performance criteria for UDB. Failure to maintain these performance standards should be grounds for suspending the flow of AID funds to the UDB until performance is

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back up to the specified level.

IV GRINDLAYS BANK

Grindlays Bank (U) Ltd. is a locally incorporated bank (October, 1969). Grindlays was the first bank to open in Uganda in 1906. Grindlays was the government banker from 1913 until the formation of the Bank of Uganda in 1966. In 1970 Grindlays operated 18 branches and 32 sub-branches with representation in all major towns. With the military government transferring all government and parastatal accounts to Uganda Commercial Bank, insufficiant banking business remained to justify branch operation up-country. Grindlays Bank operations have since been reduced to one banking facility located at 45 Kampala Road, Kampala (P.O. Box 7131, Cable MINERVA).

Grindlays is capitalized at USh 20 million and ownership is 51% Grindlays Bank Limited London and 49% Republic of Uganda. A summary of Grindlays financial performance for recent years is as follows:

Table 1. Grindlays Performance 1979-83
(USh '000,000)

DATE	TOTAL DEPOSITS	TOTAL LOANS	PROFIT BEFORE TAX	CAPITAL & RESERVES
10/79	983	337	5.6	78
10/80	1,086	487	17.5	92
10/81	1,873	396	23.5	99
10/82	2,317	921	135.6	359
10/83	4,441	2,301	167.3	378

Source: Grindlays returns to BOU

Grindlays Board of Directors (31/10/83)

Mr. G.G. Howard
Mr. J.E. Milligan
Hon. C.H. Obonyo-Jabwor, M.P.
Hon. G.M. Ssenduala M.P.
Mr. C. Kasibayo
Mr. T. Nkayarwa
Mr. J.B. Simpson (Secretary)

As of June, 1983, 52% of their lending was to the agricultural sector with the following being a futher sub-division of total bank lending related to the agricultural sector: 41% marketing, 9% processing, and 2% production. Most of the lending to

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marketing, was to coffee cooperatives to finance seasonal coffee purchasing.

Grindlays lending policy is based on their many years of experience in commercial banking in Uganda. A Risk Asset Management guide has evolved providing Grindlays staff with guidence for loan appraisal. The criteria for loans is based on (1) target market, (2) security offered, (3) amount of loan.

Levels of authority are:
(currently being revised upward)

1.	Manager (Kampala Branch)		USh. 5 million
2.	Country Credit Manager		USh. 5 million
3.	General Manager		USh. 50 million
4.	London Office	over	Ush. 50 million

Loan applications are made by the client in written form following an initial discussion with bank manager. This application is then screened using the Risk Asset Management guide including the assignment of a risk grade. Processing is fairly rapid with a decision generally within three months. Acceptable securities are: (1) fixed deposits, (2) mortgage, (3) personal guarantee by person acceptable to Grindlays, (4) treasury bills and government stock, (5) debentures, (6) surrender value of insurance, (6) other acceptable guarantees.

Repayment periods depends on type of loan for the market groups. Maximum period is currently 3 years with grace period up to 12 months. Loan recovery is by bank order for monthly fixed or variable repayments depending upon what type of activity is being financed.

Bank of Uganda consideres Grindlays performance on loan recovery to be very good.

The manager Mr. David Edger has expressed strong support for the program. He feels that many of his small to medium sized customers are the kinds of people USAID has targeted in RPE and that they could productively benefit from this scheme.

The following is an outline of the program discussed with Grindlays (ref: Dempsey memo to I.Coker dated 21 November 1983):

a. <u>Source of Funds:</u> USAID grant to GOU which would on-lend to Grindlays at a rate sufficient to allow Grindlays to cover costs and make a fair profit. Grindlay's repayment would be in shillings based on Window II exchange rate prevailing on the day of dollar disbursement. The foreign exchange component of the loan would come from USAID sources, but the local currency requirements would come from Grindlays own sources.

b. <u>Terms of Subloans:</u> loan repayment periods will be 2-5 years depending the repayment capacity of the project. Repayment terms to GOU would be 8-10 years. The prevailing commercial rates will apply on all sub-loans. The borrower provides collateral in the form of a cash deposit (interest bearing) at Grindlays equal to 60% of the foreign exchange loan. Grindlays would require GOU to guarantee the remaining 40%. Grindlays would bear the full credit risk on the local currency portion of the loan.

c. Appraisal and Technical Asst. Since Grindlays will be lending to established customers with proven track records of repayment, they feel it not necessary to have an exhaustive technical appraisal of each loan. In addition there will be the 60% collateral held on deposit. Grindlays feel that a simple standardized appraisal would suffice.

d. Procurement USAID would make the services of a procurement service available to help Grindlays with the purchase and monitoring of foreign goods. All dollar disbursements will be made directly to the suppliers.

Grindlays staff report that many of thier clients are now providing collateral in form of interest bearing deposits equal to 100% of the amounts borrowed. This does not make economic sense but is done (according to Grindlays staff) to discourage demands on client funds from the extended extended family. In effect these borrowers are paying 4%or 5% (the spread between deposits and lending rates) to borrow their own money. With this experience they feel that they would have no difficulty obtaining 60% collateral deposits.

An issue that requires better definition is the amount of RPE funds that could be productively channeled through Grindlays. Their staff conducted a survey to better quantify the likely demand (and likely sectors) for RPE funds. The response was favorable and initial client interest was much higher than originally anticipated. The management of Grindlays fell that this will depend in part on how effective the procurement mechanism proves as Grindlays intends to use RPE funds to finance clients off-shore procurement needs.

Another concern is the willingness of GOU to approve a program with Grindlays. Several months ago GOU strongly opposed the idea of using the private commercial banks. Yet, since that time CBU has been dropped from consideration. It is recognized that UCB could, at this moment, responsibly absorb limited funds, and UDB is not expected to be able to absorb more that the amount provisionally set at $8.5 million. Commercial banks are a suitable option available to channel RPE funds, and if the UDB proves unable to absorb the amount of funds provisionaly set aside for the UDB, then consideration can be given to shifting additional funds to the commercial banks.

It is recommended that USAID should take a very strong position with GOU that would allow the inclusion of private commercial banks into the RPE Program. Generally speaking their internal financial controls are much better than their quasi-governmental counterparts, their default rates are much lower, their client base is more reliable and less in need of technical assitance, and their lending decisions are less subject to political considerations.

Subject to resolving some of the issues mentioned earlier we recommend at least a pilot project be tried with Grindlays, with further expansion being dependent on a successful pilot. The GOU may find it more easy to approve a "pilot" project with a commercial bank.

Because the commercial banks do not have significant technical support staffs, USAID may wish to make such support available to them on a selective basis. In this way USAID may be able to channel more of the RPE funds into areas of higher priority to USAID.

V. Uganda Commercial Bank

Background

The Uganda Commercial Bank (UCB) was established in 1965 by Act of Parliament. UCB was the successor to the Uganda Credit and Savings Bank inheriting 9 branches. From its inception the UCB has experienced rapid growth owing in part to government policies that directed all government and parastatal institutions to use the UCB as their banking facility. It is now the dominant banking institution in Uganda accounting for a majority of the banking business. UCB is owned entirely by the Government of Uganda.

UCB head office is located in Kampala in the UCB Building. Mailing address is P.O. Box 973, cable address UGACOMBANK.

Objectives

UCB offers a wide range of banking services to the general public. Providing credit and other banking services to the agricultural sector is a specific objective of UCB. It has also engaged small-scale industrial lending and term lending to agriculture. Several government development funds are administered by the bank on a managed funds basis. UCB small-scale industry lending program was recently expanded through a $5 million line of credit from IDA.

Structure

UCB management responsibility is vested in a 10 person Board of Directors. The Chairman of the Board is also the chief operating officer of the bank. There are two General Managers, Administration and Operations, and these positions are currently being covered by Department Heads in the capacity of acting General Managers.

Table 2. UCB Board of Directors

Name	Position	Occupation
Mr. R.H.Kaijuka	Chairman	Managing Dir./UCB
Prof. F. Banugire	Member	Economics Lecturer
Mr. C.P. Atidoro	"	Business Lecturer
Prof. J. Ilukor	"	Physics Lecturer
Dr. W.B. Nganwa	"	Dental Surgeon
Mrs. I. Wanendeya	"	Businesswoman
Mr. J. Mulwana	"	Businessman
Mr. A.D. Lubowa	"	Gen.Manager EMCO
Hon. S.K. Byakika	"	Politician
Mr. J. Bagabirwa	Secretary	Chief Legal Dept/UCB

The management and decision making process of UCB is centralized. There are eight departments in the bank; credit, accounts, international, audit, administration, legal, personnel, and research/planning. There are over 50 branches, but except of routine account management decisions, branch managers have limited discretionary authority in approving credit applications. They do have responsibility for supervision and collection.

Policies and Procedures

Adequacy of security is the most important criteria for lending at UCB. The bank uses all normal forms of security, but prefer mortgages in agricultural and industrial loans. Other forms of acceptable security are fixed deposits, debentures, and acceptable guarantees by companies or government. Once the BOU guarantee scheme becomes operational and if it has an adequate level of coverage, UCB would be able to expand their lending to viable projects previously excluded due to inadequate tangible security.

Loan applications are made on standard forms through the nearest branch office. Loan applications include the following: (1) income tax certificate, (2) statement of liabilities and assets, (3) cash flow projection, (4) valuation report when tangible property is offered for security. The branch manager will pre-screen the applications, add comments and recommendations, and pass the application to the head office credit department for a decision on the loan application. The BOU has established guidelines to encourage lending to certain priority sections of the economy. These guidelines currently favor agriculture and industry, and UCB takes this into consideration when approving loans. The Credit department conducts its own analysis of the application usually following a visit to the project site.

UCB uses several disbursement methods including overdraft facilities, credit to current account, direct payment to suppliers and contractors, and supply of actual inputs. UCB prefers to make in-kind disbursements, but this is often not practical in many situations.

Repayments are generally made by bankers orders with frequency of payment (monthly, quarterly, or semi-annual) based on projected cash flows. All borrowers are required to maintain their business banking account with UCB thus enabling the bank the opportunity to monitor account activity. Loans tend to be short to medium-term, not generally over 5 years. Moratorium on repayment can be up to 12 months.

Staffing

Total staff of UCB exceeds 2,600, with about 5% being professional banking staff. UCB has its own training school to provide specialized training, opportunities for staff up-grading, and orientation for new staff. UCB is generally considered to be a good employer, and therefore staff turnover is small. Promotion generally come from within, and a review of current officers in Department Head positions indicates a average age in the early forties with 20 years service in the bank. UCB also has several specialists on their staff such as lawyers and engineers. (An organizational chart and biographical information of department heads is attached as Appendix 9).

Financial Position

UCB has made a profit every year from 1976 to present with the except 1979 when there were considerable war related write-offs. The most recent balance sheet (September 1982) reported a operating profit before tax of USh. 251 million for the year. There was also recorded a significant increase of USh 2.48 billion in the capital reserve as the result of restating the value of bank property, however, the auditors qualified this entry as this could not be supported by independent professional valuation.

Lending has increased significantly in recent years. Lending up to 1982 generally ran 50-60% of total deposits, and be September of 1982 this increased to 86%. The amount that UCB lends to agriculture has generally been around 40% which is close to the guideline of 30% as established by the BOU. Only a small portion of this agricultural lending has been for production with the majority going to agricultural marketing and procession (finance the purchase and processing coffee and tea). This trend has continued to the present, and slow payments for coffee exports have contributed to current the liquidity problems facing UCB and other banks.

The 1982 audited account shows nearly USh 700 million as being items in transit (funds from branches). The previous year this amount was even larger. The auditors noted that this amount has not been reconciled nor investigated. Other commercial banks in Uganda, except for the Cooperative Bank, have much lower percentage levels for transit items.

It is difficult to evaluate the loan portfolio of UCB using normal criteria in assessing arrears because much of the portfolio is made up of short-term loans (overdrafts) that are rolled over with regularity. A portion of the short-term loan account would be more appropriately considered as medium-term credit as many overdraft accounts remain at relatively constant levels throughout the year. Seasonal credit advanced to finance crop purchases also remains outstanding longer than originally planned due to delays in remittence by commodity export authorities.

Current authorized share capital for UCB is USh 1.5 billion. Paid up share capital stands at USh 280 million, and this is expected to increase to USh 500 million by end of 1983. Further increases in share capital will be required for UCB as capital base is inadequate for present and projected operating levels if the leverage ratio (total assets/equity) are to be maintained at acceptable levels. Income in 1982 was nearly 8 times share capital and profit after taxation was slightly more than total share capital.

Growth of UCB's operations, like all other credit institutions in Uganda, depend mainly on development in the economy and on external influences especially those related to security. As is difficult to accurately forecast those developments, meaningful financial projections are difficult to prepare. Projections necessarily have to be highly qualified resulting in documents of limited value when assessing the capability of a credit institution to effectively manage funds. If the economy continues to improve as current indications suggest, there will be increased lending opportunities to viable projects by all banks. Given UCB current share of the market, they are well placed to take advantage of RPE funds, especially provisions related to off-shore procurement.

Recommendation

Consideration of the UCB as an ICI for the RPE project followed a request by the BOU that UCB be included. This request came during the final stages of preparation of the project paper. Insufficient time remained to complete a full ICI assessment for UCB. It is recommended that before a final decision is made on UCB, a review of the 1982-83 audit report should be completed. This document is expected to be available during the third quarter of this year.

A indication of UCB capability for small-scale loan management can be determined from closer examination of their current management of the IDA industrial rehabilitation credit. Many of the features of this credit program for industrial rehabilitation are similar to those enterprises being proposed for rehabilitation under RPE. A demonstrated effective system for loan appraisal and supervision for the IDA credit would support UCB as an ICI for RPE.

APPENDIX 1

UGANDA DEVELOPMENT BANK

Historical Profit And Loss Statements For Year

Ended December 31

(U.Shs. million)

INCOME	1978	1979	1980	1981	1982	1983	1st.Quart. 1984	Budget 1984
Interest on Loans	11.518	11.600	6.400	16.567	80	176	112	1076
Profit Sale Bicycles	-	-	-	-	-	83	-	-
Commission and Committment Fees		0.131	0.347	2.018	-	-	-	-
Exchange Gain	-	-	-	-	-	-	13	-
Other Income	0.256	0.300	2.150	1.551	6	12	2	11
Total Income	11.783	12.031	8.897	20.136	86	271	127	1087
EXPENDITURES								
Interest on Borrowings	0.280	0.280	0.280	18.619	63	157	22	478
Staff Salaries and Wages	3.339	3.127	5.286	12.382	-	-	-	80
Other Administrative Expenses	5.829	6.551	12.109	25.667	-	-	-	225
Total Administrative Expenses	9.168	9.678	17.395	38.049	130	215	93	335
Loss on Ranch Rehabilitation	-	-	-	-	-	74	10	56
Exchange Loss	-	-	-	-	-	193	-	-
Total Expenses	9.446	9.958	17.675	56.668	196	639	125	869
Profit Before Provisions	2.336	2.073	(8.778)	(36.532)	(110)	(368)	2	218
Loans and Provisions for losses	2.817	1.817	89.610	-	-	(105)	(28)	(112)
Profit After Provisions	(0.482)	0.256	(93.388)	(36.532)	(110)	(473)	(26)	106
Loss Brought Forward	-	-	10.596	109.082	146	256	729	729
Loss Carried Forward	-	10.596	109.082	145.614	256	729	755	623

ref: ADB Report Annex 3.5

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APPENDIX 2

Historical Balance Sheets as of December 31

(U.Shs. million)

ASSETS	A 1978	A 1979	A 1980	A 1981	B 1982	B 1983	C Mar 84	PROJECTED D 1984
Current Assets								
Cash and Bank Balances	0.899	3.141	56.446	27.237	106	513	1305	351
Treasury Bills	2.992	8,992	6.510	29.741	-	-	-	-
Bicycles Project Acct.						221		
Other Current Assets	18.111	16.330	3.631	11.711	20	171	186	68
Total Current Assets	22.002	28,463	66.587	66.689	126	905	1491	419
Fixed Assets								
Portfolio Loans	125.552	104.714	44.084	239.665	696	2358	3321	12518
Stock	-	-	-	-	154	764	717	-
Other Fixed Assets	6,287	8.561	11.217	22.676	30	55	57	305
Total Assets	153,841	141.738	121.888	331.030	1006	4082	5586	13242
Liabilities and Equity								
Current Liabilities								
Bank Overdrafts	4.425	1.664	1.920	0.904	14	54	-	-
Accounts Payable	.594	1.088	5.036	24.257	43	283	249	322
Other Current Liabilities	.429	2.835	2.515	0.439	-	-	-	-
Total Current Liabilities	5.448	5.587	9.471	25.600	57	337	249	322

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	A 1978	A 1979	A 1980	A 1981	B 1982	B 1983	C March 84	PROJECTED D 1984
Long-Term Debt	42.555	42.835	9.147	187.692	853	3331	4921	9627
Share Capital	100.000	100.000	100.000	100,000	352	532	532	3032
Accumulated losses	(6.514)	(37.036)	(106.082)	(146.614)	(256)	(729)	(725)	(366)
Capital Contribution	12.352	32.552	112.352	163.352	-	611	611	627
Total Shareholders Worth	105.838	93.516	103.270	117.738	96	414	418	3293
Total Liabilities and Equity	163.841	141.738	121.888	331.030	1006	4082	5586	13242
Debt/Equity Ratio	0.40	0.45	0.01	1.58	8.9	8.0	11.8	2.9
Current Ratio	3.4	3.5	7.0	2.25	2.2	2.0	6.0	1.3
Average Gross Assets	151	177	178	271	669	2544	4834	8662

Ref: A - ADB Report Annex 3.6
B - Draft 1983 Audit
C - 1st Quarter Financial Report
D - 1984 Budget

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APPENDIX 3

UGANDA DEVELOPMENT BANK

Historical Statements of Sources and Application of Funds

For Years Ended December 31

(U.Shs. million)

SOURCES	A 1980	A 1981	B 1982	B 1983	C March 84	PROJECTED D 1984
Net Profit	(98.388)	(36.532)	(110)	(368)		107
Provisions	89.610	-	12	408		201
Cash Generated From Operations	(8.778)	(36.532)	(98)	(40)		308
Increase in Share Capital	80.00	51.00	89	791		2500
Loan Repayments	31.621	44.079	39	33		66
Increase in LT Loans	-	184.306	626	1208		7224
Ranch Stocks Distribution	-	-	-	-		1357
Other Sources	3.135	0.839	30	-		279
Total Sources	105.978	243.746	686	1992		11734
APPLICATIONS						
Loans Disbursed	52.771	239.660	437	802		10743
Purchase of Fixed Assets	3.309	13.302	17	33		214
Repayment of Loans	-	6.997	-	-	-	125
Increased Stock	-	-	154	610	-	951
Increase in Treasury Bills	-	23.231	-	-	-	-
Other Applications	-	8.030	7	(40)	-	-
Movement in Liquid Funds			71	587	-	-
Increase (Decrease) in Working Capital	49.898	(46.474)	-	-		(299)
Total Applications	105.978	243.746	686	1992		11734

Ref: A - ADB Report Annex 3.7
B - Draft 1983 Audit
C - 1st Quarter Financial Report
D - 1984 Budget

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APPENDIX 4

TABLE 1

STATUS REPORT ON LINES OF CREDIT WITH INDUSTRY DEPARTMENT

A. LINES OF CREDIT WHERE BOROWER TAKES FOREIGN EXCHANGE RISKS

Line of Credit	Amount of Line of Credit U.S. $ M	Amount Committed at 31/3/84	Amount Disbursed at 31/3/84	Amount Committed but Undisbursed	Amount Uncommitted
1. E.E.C	1.5	1.4	1.4	0.05	0.05
2. A.D.B.I.	13.0	12.1	6.0125	6.0875	0.9
3. EEC Uganda Hoes	3.5	-	-	-	3.5
4. E.I.B.	7.5	6.65	6.65	-	0.85
5. IDB Trade Financing (Hima)	3.7	3.7	2.2	1.5	-
6. I.D.B.	6.5	-	-	-	6.5
7. ADB III	26.0	-	-	-	26.0
Sub-total	61.7	23.85	16.2625	7.6375	37.80

B. LINES OF CREDIT WHERE GOVT. TAKES FOREIGN ECH[illegible] RISK

Line of Credit	Amount of Line of Credit U.S. $ M	Amount Committed at 31/3/84	Amount Disbursed at 31/3/84	Amount Committed but Undisbursed	Amount Uncommitted
8. WORLD BANK (IDA)	30.0	4.8	-	4.8	25.2
9. OPEC	15.0	0.2	0.2	-	14.8
Sub-total	45.0	5.0	0.2	4.8	40.0
GRAND TOTAL	106.7	28.85	16.4625	12.4375	77.8

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APPENDIX 5

DRAFT

UGANDA DEVELOPMENT BANK

YEAR ENDED 31 DECEMBER 1983

AUDITORS' REPORT TO THE MINISTER OF FINANCE ON THE
FINANCIAL STATEMENTS OF UGANDA DEVELOPMENT BANK
FOR THE YEAR ENDED 31 DECEMBER 1983

DRAFT

1. We have audited the financial statements on pages 2 to ~~18~~ 11. Our audit was conducted in accordance with generally accepted auditing standards except that the scope of our work was limited by the matters referred to below.

2. As explained in note 5 to the accounts, the directors have been unable to assess accurately the amount of loans which will ultimately prove irrecoverable. We are, therefore, unable to form an opinion on the reasonableness of the provision for loan losses included in the financial statements.

3. Ranch rehabilitation loans receivable have been included in the balance sheet at an amount of Shs 420 million, as shown in note 8 to the accounts. There was no system of control over the accounting for such loans upon which we could rely for the purpose of our audit and we were unable to obtain confirmation of the loan balances from the borrowers. We are, therefore, unable to form an opinion whether ranch rehabilitation loans receivable are fairly stated.

4. In our opinion:

(i) the financial statements have been prepared on a basis consistent with that of the preceding year and are in agreement with the books of account;

(ii) subject to the adjustments, if any, which may ultimately prove to be necessary to the loan loss provision and to the amount at which ranch rehabilitation loans receivable are stated, proper books of account have been kept and the financial statements give a true and fair view of the state of financial affairs of the bank at 31 December 1983 and of the loss and source and application of funds for the year then ended.

UGANDA DEVELOPMENT BANK

PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 DECEMBER 1983

	Note	1983 Shs millions	1982 Shs millions
INCOME			
Income from loans		176	80
Income from short term investments		11	3
Profit on sale of bicycles	3	83	2
Miscellaneous income		1	1
Total income		271	86
EXPENSES			
Charges on borrowings		157	63
Administration expenses		215	130
Loss on ranch rehabilitation project	4	74	-
Exchange loss (net)		193	3
Total expenses		639	196
LOSS BEFORE PROVISION FOR LOAN LOSSES		(368)	(110)
LOANS WRITTEN OFF		(50)	-
PROVISION FOR LOAN LOSSES	5	(55)	-
LOSS FOR THE YEAR BEFORE TAXATION		(473)	(110)
TAXATION	6	-	-
LOSS FOR THE YEAR AFTER TAXATION		(473)	(110)
LOSS BROUGHT FORWARD		(256)	(146)
LOSS CARRIED FORWARD		(729)	(256)

UGANDA DEVELOPMENT BANK

BALANCE SHEET
AT 31 DECEMBER 1983

	Note	1983 Shs millions	1982 Shs millions
ASSETS			
Fixed assets	7	55	30
Loans receivable	8	2,358	696
Stock and goods-in-transit	9	764	154
Debtors and prepayments	10	171	20
Bicycles project account	11	221	-
Cash and bank balances	12	513	106
Total assets		4,082	1,006
LIABILITIES, CAPITAL AND RESERVES			
Liabilities			
Bank overdrafts	13	54	14
Loans payable	14	3,331	853
Creditors and accruals	15	283	43
Total liabilities		3,668	910
Capital and reserves			
Share capital	16	532	352
Accumulated losses		(729)	(256)
		(197)	96
Capital contribution	17	611	-
Total capital and reserves		414	96
Total liabilities, capital and reserves		4,082	1,006

_______________ CHAIRMAN _______________ DIRECTOR

UGANDA DEVELOPMENT BANK

STATEMENT OF SOURCE AND APPLICATION OF FUNDS
FOR THE YEAR ENDED 31 DECEMBER 1983

	1983 Shs millions	1982 Shs millions
SOURCE OF FUNDS		
Loss for the year before provision for loan losses	(368)	-
Adjustment for items not involving the movement of funds:		
Depreciation	8	-
Net unrealised loss on exchange on loans receivable and loans payable	400	-
TOTAL GENERATED FROM OPERATIONS	40	-
FUNDS FROM OTHER SOURCES		
Capital contribution	791	89
Loans received	1,208	626
Loan repayments received	33	39
Net decrease in treasury bills	-	30
	2,072	784
APPLICATION OF FUNDS		
Loss for the year before provision for loan losses	-	110
Adjustment for items not involving the movement of funds:		
Depreciation	-	(3)
Fixed assets written off	-	(6)
Net unrealised loss on exchange on loans receivable and loans payable	-	(3)
Total absorbed by operations	-	98
OTHER APPLICATIONS		
Loans disbursed	802	437
Purchase of fixed assets	33	17
Increase in stock and goods-in-transit	610	154
Bicycles project account	221	-
Others (net)	40	7
	1,706	713
Increase in net liquid funds	366	71

UGANDA DEVELOPMENT BANK

NOTES TO THE ACCOUNTS
FOR THE YEAR ENDED 31 DECEMBER 1983

1. INCORPORATION

The bank is incorporated in Uganda by decree. The Uganda Government has a controlling interest in the ~~issued shares~~ bank.

2. SIGNIFICANT ACCOUNTING POLICIES

(a) Accounting convention

The accounts are prepared under the historical cost convention.

(b) Income recognition

Income from loans is accrued and credited to income in the year to which it relates except where loans are in default and where payment of the interest is not guaranteed by the Uganda Government, in which case no accrual is made, the income from such loans being taken into income when collected.

(c) Fixed assets and depreciation

Fixed assets are stated at cost less depreciation. Depreciation is charged on a straight line basis from the month following the date of purchase of such assets at rates calculated to write off their costs over their estimated useful lives. The annual rates used are as follows:-

Leasehold buildings	4%
Motor vehicles	25%
Furniture, fixtures and fittings	12.5%

(d) Stock and goods-in-transit

Stock and goods-in-transit are valued at the lower of cost and net realisable value. Cost, which is calculated using the first-in first-out basis, comprises invoice price converted, if denominated in currencies other than Uganda shillings, at rates ruling at the balance sheet date, and all carriage, duties, taxes, and other incidental expenses incurred in delivering the stock into store. For livestock and supplies for the ranch rehabilitation project, net realisable value is based on the amount estimated as chargeable to borrowers on disbursement of the stock to them.

(e) Provision for loan losses

Loans are stated net of a provision for that proportion of the balances considered by the directors to be irrecoverabl .

UGANDA DEVELOPMENT BANK

NOTES TO THE ACCOUNTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 1983

(f) Currency

The accounts are expressed in Uganda shillings. Assets and liabilities denominated in currencies other than Uganda shillings are translated at the rates ruling at the balance sheet date.

Foreign currency transactions which take place during the year are recorded at the rate ruling on the transaction date. All exchange differences are dealt with in the profit and loss account.

As disclosed in note 2(d), the invoice price of stock and goods-in-transit, if denominated in currencies other than Uganda shillings, is converted at rates ruling at the balance sheet date. Any exchange differences are therefore included in the cost of stock and goods-in-transit since in the opinion of the directors these differences are recoverable.

3. PROFIT ON SALE OF BICYCLES

This arises from the sale of bicycles acquired under a trade financing agreement with the Islamic Development Bank. It is stated before charging the exchange loss on the liability to Islamic Development Bank, which loss is included under "exchange loss (net) in the profit and loss account.

4. LOSS ON RANCH REHABILITATION PROJECT

This arises from the under-recovery of certain costs on disbursement of livestock and supplies purchased by the Bank under the ranch rehabilitation project, financed by a line of credit extended by the African Development Bank.

5. PROVISION FOR LOAN LOSSES

As a result of the uncertainties arising from the current economic environment prevailing within Uganda, the directors have been unable to assess accurately the amount of loans which will ultimately prove irrecoverable. A general provision of 10% of loans receivable, other than those guaranteed by the Uganda Government, has therefore been made.

6. TAXATION

In view of the losses for the year, no liability to taxation will arise, and amounts paid on provisional assessments for 1980 and 1981 are considered recoverable.

No final assessments have been issued by the Income Tax authorities since the inception of the bank in 1972.

UGANDA DEVELOPMENT BANK

NOTES TO THE ACCOUNTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 1983

7. FIXED ASSETS

	Leasehold land and buildings Shs millions	Motor vehicles Shs millions	Furniture fixtures & fittings Shs millions	Total Shs millions
Cost				
At 1 January 1983	5	19	12	36
Additions	-	11	22	33
At 31 December 1983	5	30	34	69
Depreciation				
At 1 January 1983	-	3	3	6
Charge for the year	-	5	3	8
At 31 December 1983	-	8	6	14
Net book amount				
At 31 December 1983	5	22	28	55

8. LOANS RECEIVABLE
Foreign Currency

	1983 Shs millions	1982 Shs millions
Industrial rehabilitation		
- guaranteed by Uganda Government	806	362
- Other	909	210
Ranch rehabilitation	420	-
Local currency	111	140
	2,246	712
Less: provision for losses	145	90
	2,101	622
Accrued charges receivable		
- guaranteed by Uganda Government	195	51
- Other	42	10
Staff	20	13
	2,358	696

UGANDA DEVELOPMENT BANK

NOTES TO THE ACCOUNTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 1983

	1983 Shs millions	1982 Shs millions
9. STOCK AND GOODS-IN-TRANSIT		
Livestock and supplies for ranch rehabilitation project	722	116
Bicycles held for resale	42	38
	764	154

	1983 Shs millions	1982 Shs millions
10. DEBTORS AND PREPAYMENTS		
Credit sales of bicycles	68	-
Expenditure to be reimbursed by Uganda Government		
Namanve Project	20	11
Water and Sewerage Project	16	4
Kuwait Fund	4	-
Taxation recoverable	2	2
Sundry debtors and prepayments	61	3
	171	20

11. BICYCLES PROJECT ACCOUNT

This represents funds held by the Bank of Uganda which can be utilised solely for the repayment of the liability due to Islamic Development Bank under the trade financing agreement for bicycles.

12. CASH AND BANK BALANCES	1983 Shs millions	1982 Shs millions
Local currency - interest bearing	112	8
- non-interest bearing	271	11
Foreign currency - interest bearing	136	92
Less: Bank suspense accounts	(6)	(5)
	513	106

13. BANK OVERDRAFTS	1983	1982
Local currency	3	14
Foreign currency	51	-
	54	14

The foreign currency overdraft arises from the payment of a letter of credit which was reimbursed, after the year end, by the African Development Bank.

UGANDA DEVELOPMENT BANK

NOTES TO THE ACCOUNTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 1983

14. LOANS PAYABLE

	1983 Shs millions	1982 Shs millions
African Development Bank		
Industrial rehabilitation	1,187	526
Ranch rehabilitation	1,020	121
European Economic Community	280	131
Islamic Development Bank	754	32
Uganda Government (local currency)	3	3
Accrued charges payable	87	40
	3,331	853

The terms of the loans are as follows:-

	Interest (% p.a.)	Repayment Period
African Development Bank - Industrial	7.5	1984-1995
- Ranch	7.0	1985-1995
European Economic Community	1.0	1992-2021
Islamic Development Bank	-	1984
Uganda Government	4.0	1984

15. CREDITORS AND ACCRUALS

	1983 Shs millions	1982 Shs millions
Amounts due for purchase of livestock and supplies for ranch rehabilitation project	208	-
EEC project account (training fund)	4	-
Other creditors and accruals	71	43
	283	43

UGANDA DEVELOPMENT BANK

NOTES TO THE ACCOUNTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 1983

16. SHARE CAPITAL

	1983 Shs millions	1982 Shs millions
Authorised		
400,000 (1982-400,000) ordinary shares of Shs 5,000 each	2,000	2,000
Issued and fully paid		
106,470 (1982-70,470) ordinary shares of Shs 5,000 each	532	352

The issued share capital was increased by the retroactive allotment of 36,000 ordinary shares of Shs 5,000 each at a Board Meeting held in March 1984.

17. CAPITAL CONTRIBUTION

	1983 Shs millions	1982 Shs millions
At 1 January	-	163
Contributions received during the year	791	89
Allotted as share capital	(180)	(252)
At 31 December	611	-

18. COMMITMENTS

At 31 December 1983 there were undisbursed loan commitments to borrowers equivalent to Shs 5,582 million (1982 - Shs 662 million).

Undrawn credit facilities available to the bank at 31 December 1983 were as follows:

	1983 Shs millions	1982 Shs millions
African Development Bank	2,892	1,665
European Economic Community	21	24
Islamic Development Bank (trade financing)	599	548
European Investment Bank	1,489	762
International Development Association	4,800	3,149
The OPEC Fund	3,600	1,574
	13,401	7,722

UGANDA DEVELOPMENT BANK

NOTES TO THE ACCOUNTS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 1983

19. CONTINGENT LIABILITIES

At 31 December 1983 the bank had no contingent liabilities under guarantees given to other banks (1982 - Nil).

20. FOREIGN CURRENCY EXCHANGE RATES.

The relevant rates of exchange ruling at the balance sheet date were approximately:

		1983 shs	1982 shs
1	African unit of account	257	118
1	European currency unit	201	104
1	United States dollar	243	107
1	Islamic dinar	254	118

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Appendix 6

UGANDA DEVELOPMENT BANK
LIST OF PROFESSIONAL STAFF BY DEPARTMENT AS AT 2ND APRIL, 1984

GENERAL MANAGER'S OFFICE

NAME	POSITION
Mr. A. K. Mawanda	General Manager
Mr. L. Berring	Asst. General Manager - Operations
Mr. A. W. Kabugo	General Manager's Office
Mr. L. Ssebunya	" " "

SECRETARIAT

Mr. M. M. Kiwanuka	Bank Secretary
Mr. N. J. Dolomoy	Deputy Secretary
Mr. B. Ssebuliba	Legal Officer
Miss Joy Binayisa	Legal Officer
Mr. O. O. Olok	Principal Legal Officer

ADMINISTRATION & PERSONNEL

Dr. C. K. Tibarokoka	Ag. Head/Administration & Personnel
Mr. L. K. Rwakaijengye	Senior Administrative Officer
Mrs C. Lubwama	Administrative Officer
Mr. R. K. Ssali	Administrative Officer
Mr. T. Ebong-Ongom	Administrative Officer
Mr. G. J. M. Ssemwogerere	Principal Administrative Officer

ACCOUNTS

Mrs S. Bbumba	Ag. Chief Accountant
Mr. J. Odong	Deputy Accountant
Mr. R. Rukundo	Principal Accountant
Mrs C. Kwoba-Abungu	Principal Accountant

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INTERNAL AUDIT

NAME	POSITION
Mr. F. Kasule	Chief Internal Auditor
Mr. S. B. Okeme	Principal Internal Auditor

INDUSTRY

Mr. F. J. Kasujja	Head of Dept.
Mr. M. Mugonyi	Principal Loans Officer
Mr. O. Lubulwa	Senior Loans Officer
Mr. H. Muteefu	Senior Loans Officer
Mr. S. Kato-Magambo	Loans Officer
Mr. B. Tumwesigye	Loans Officer
Mr. O. Ongaria Okonera	Loans Officer
Mr. J. Barahukwa	Loans Officer
Mr. S. Mpagi	Senior Loans Officer
Mr. G. W. Kijjambu	Senior Loans Officer
Mr. I. Kasiira	Loans Officer

LIVESTOCK

Mr. L. K. Lubowa	Head of Dept.
Mr. E. I. Laboke	Principal Loans Officer
Dr. Okidi-Odaka moi	Principal Loans Officer
Mr. P. M. Kyaka	Principal Loans Officer
Mr. J. Potore	Principal Loans Officer
Mr. F. Rwakijanju	Senior Loans Officer
Mr. F. Kumbategire	Senior Loans Officer
Mr. J. Bukenya	Senior Loans Officer
Mr. M. Kibirige	Loans Officer
Mr. D. Kasirya	Loans Officer
Mrs. A. Masifa	Loans Officer
Mrs. H. Nsubuga	Loans Officer
Mr. Bosco Ogwang	Loans Officer
Miss C. Mbabazi	Loans Officer
Mr. J. Oloya	Loans Officer
Mr. M. Or itum	Loan Officer

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CROP

NAME	POSITION
Mr. A. E. R. Byaruhanga	Ag. Head of Dept.
Dr. D. W. Maloba	Principal Loans Officer
Mr. Kasimagwa	Loans Officer
Mrs. V. Sseçkitoleko	Loans Officer
Mr. S. Okello-Dinga	Loans Officer
Mr. A. Sematimba	Loans Officer

SUPERVISION AND RECOVERY

Mr. B. Buhamizo	Head of Dept.
Mr. D. Musanje	Senior Loans Officer
Mr. S. Twase	Principal Loans Officer
Mr. G. Musana	Loans Officer

Note. Nearly all staff listed above have a university degree or professional accounting qualification.

APPENDIX 7 UDB Loan Application Form

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CONFIDENTIAL

FORM UDB/1

Register No..............................

File No..............................

No. 2735

Shs. 120.00

No 10769

UGANDA DEVELOPMENT BANK

I.P.S. BUILDING—P.O. BOX 7210, KAMPALA.

LOAN APPLICATION FORM

SECTION I.—PERSONAL PARTICULARS OF APPLICANT(S)

1. Full Names of Applicant(s)..

....

2. Full Address ....

....

3. Present full-time Employment..

SECTION II.—PARTICULARS OF BUSINESS

4. Name of Business..

5. Address..

....

6. Date when Business Established..............................Registration No..............................

7. Nature of Business..

8. Main Activity ....

9. Location:—

District	Town or County	Street or Sub-County	Block and Plot No.

10. Is your Business on Leased Land? If Yes, State:—

Length of Lease.. Expiry Date..............................

(*a*) If Factory, Shop, etc., State whether Premises in which the Business is Housed belongs to you. Yes ☐ No ☐

If Yes, State:—

Cost of Construction/ Purchase Price	Date of Construction/ Purchase	REMARKS

(*b*) If Rented: Monthly Rent Shs..

(i) Name of Owner(s) ....
(*Block letters*)

(ii) Address..

(iii) Length of Tenancy Agreement..............................Expiry Date ....

11. Form of Ownership (Please tick):—

(*a*) Sole Proprietor ☐ (*b*) Partnership ☐ (*c*) Limited Liability Company ☐

(*d*) Statutory Corporation ☐ (*e*) Co-operative Society/or Union ☐

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12. Names of Owners of the above Business:—

Names of Owners	Age	Nationality	Number of Shares	Face Value *Shs.*
....	......	......	......	......
....	......	......	......	......
....	......	......	......	......
....	......	......	......	......

13. The person who should be contacted in the event of any query on this application:

Names..P. O. Box..........................,Telephone..................,

14. (*a*) Bankers..Branch ....

(*b*) If no bankers, state which Bank you intend to use..Branch..................

15. (*a*) Total Investment (Complete the following table to indicate your total Investment to date):—

Item	Total Investment *Shs.*	Amount Already Paid *Shs.*	Your Contribution *Shs.*	Present Book Value *Shs.*
(i) Machinery ...	......	......	......	......
(ii) Land	......	......	......	......
(iii) Buildings ...	......	......	......	......
(iv) Livestock ...	......	......	......	......
(v) Crops... ...	......	......	......	......
(vi) Others ...	......	......	......	......
TOTAL ...	......	......	......	......

(*b*) If you have any Outstanding Liabilities under (*a*) State:—

(i) How much..

(ii) To Whom..

(iii) Address..

(iv) Method of Repayment..

SECTION III.—PARTICULARS OF LOAN APPLIED FOR

16. (*a*) Amount of Loan applied for—Shs..................................Repayment period...................months

(*b*) Purpose of Loan:—

(i) Purchase of Business ... ... ☐

(ii) Expansion of existing Business ... ... ☐

(iii) Establishing new Business ... ... ☐

(iv) Other (State) ... ... ☐

Make a brief statement specifying the nature and indicating the viability of your project or proposal (if space is not enough attach a separate statement).

(c) Total Scheme Value: Shs..

Amount available for the Scheme from the Applicant:—

		Shs.
(i)	Cash in Hand...	....
(ii)	Cash in Bank...	....
(iii)	Overdraft Facilities	....
(iv)	Bank Loan	....
(v)	Others	....

17. Security offered to cover the above Loan:—

Type of Security (e.g. Buildings, Land, Insurance policy, Share Certificates)	Estimated Value *Shs.*	Location			
		District	Town/County	Street/ Sub-County	Plot No.

Is/Are the above Security(ies) free of Encumbrances (Mortgages)? Yes ☐ No ☐

If no, give details below:—

(i) Name of Mortgagee(s)..

(ii) Address..

(iii) Original Amount of Loan (Shs.) ....

....

(iv) Present Balance (Shs.) ....

(v) Arrears, if any (Shs.) ....

SECTION IV.—OTHER INFORMATION

18. In the case of a business already established, the following information in respect of this business should also be supplied:—
    (i) a copy of the Memorandum and Articles of Association, Certificate of Registration or Incorporation;
    (ii) a copy of current Income Tax Clearance Certificate;
    (iii) a copy of current operating licence(s);
    (iv) copies of the latest accounts—Trading, Profit and Loss Accounts and Balance Sheet;
    (v) copies of bank statements of the latest past six months;
    (vi) a list of title deeds, debentures, loan agreements and contracts.

19. Have you in your own name (or that of your wife/husband or any of your children) or in the name of a business in which you have an interest received a loan from this Bank? If so, give full details below:—

....

....

20. Have you or any of your family members ever before applied for a loan from this bank which was not accepted? If so, give particulars and date of application, etc.:

....

....

21. Have you any Substantial Interest and/or Shareholding in any other Company or Firm? If so, give particulars below:—

Name of Business	Nature of Business	Your Investment in *Shs.*	Your Position in Business

Please Note (1) This form must be duly completed before submission.

(2) An application fee of Shs. 1,000 is payable when submitting this application.

SECTION V.—DECLARATION

I/WE HEREBY DECLARE that to the best of my/our knowledge and belief the particulars given in this form are true and complete in all respects.

Signature of Applicant:.. *Designation:*............................*Date:*..........

Official Stamp:..

SECTION VI.—FOR BANK USE ONLY

Management's Recommendation:

Minute No.............................(1) Approval—Amount Shs.............................Interest Rate...........% p.a.

Loan period:..Months:....................

Period of grace:..Months:....................

Repayment Period:...Months:....................

....

....

(2) Further analysis to include:—

☐ Special purpose application (specify)..

....

☐ Financial statement as of..

....

☐ Current appraisals (specify)..

....

☐ Profit and Loss Statement for...

....

☐ Cash flow schedules...

....

☐ Complete Capital Budget..

....

(3) No further processing. Reasons:..

....

....

(4) Application to be rejected. Reasons:..

....

Board's Decision:

Minute No.............................(1) Loan approved—Amount Shs..........................Interest Rate.........% p.a

Repayment period...

....

(2) Further analysis required (specify)..

....

....

....

(3) Loan Application rejected. Reasons:..

....

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APPENDIX 8 UDB Loan Offer Form F-46

UGANDA DEVELOPMENT BANK

TEL: 30740/6,
TELEX 61143,
CABLE DEVBANK.

IPS BUILDING,
14, OBOTE AVENUE,
P.O. Box 7210,
KAMPALA.

REF:........... DATE:.................

..........................,

....

....

....

Dear Sirs,

Loan Offer of................. and a local component of...................

With reference to your application for a loan to develop/rehabilitate your ranch, you are informed that a loan of Units of Account (UA)..................and a local component of U.Shs................and other amounts still to be determined as explained below has been extended to you in kind, subject to the fulfilment of and on the following terms and conditions:-

1. Loan Amounts : i)

   ii)

   iii)

2. Interest Rates : i) Will be 13% p.a. variable at the instance of the Bank on loan in Units of Accounts.

   ii) Will be 16% p.a. variable at the instance of the Bank on loan in Uganda Shillings.

3. Repayment Period : The loan is for a period of 9 years including 3 years of grace. Interest shall be payable during the grace period.

4. Commission : 1% p.a. on the principal amount of the loan disbursed and outstanding from time to time. First commission is payable on acceptance of the loan offer.

5. Commitment Fee : 1% p.a. shall be payable on the undisbursed portion of the loan which shall begin to accrue 45 days after the date of the loan offer.

..../2

6.	Exchange Rate	:	The exchange rate to be applied on payments made to the Bank by the borrower shall be the rate ruling on the date of such payments.
7.	Beneficiary	:	....
8.	Purpose of the loan and mode of disbursement	:	The loan shall be disbursed in kind and utilised for ranching project. The following listed cattle and materials shall constitute part of the total loan approved.

....../3

MATERIAL	QUANTITIES	UNITS OF ACCOUNT (U.A)		LOCAL COST (U.SHS)		REMARKS
		UNIT	TOTAL	UNIT	TOTAL	

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9. Security : That you mortgage your land with all developments on it and provide any other security may deem necessary to cover the loan.

10. Other Conditions to be observed :

i) You will be required to complete and sign all documents relating to the item on security before any part of the loan is disbursed.

ii) All correspondence in connection with the loan must be made on headed or plain paper antheticated by stamping with a rubber stamp of the company or affixing the seal of the company.

iii) The offer shall be valid for a period of 45 days from the date of this letter of loan offer.

iv) All animals should be branded with rancher's own brand.

v) Transport of cattle and other materials to your ranch from point of delivery shall be your responsibility.

vi) That you should keep proper records and submit to the Bank quarterly reports and audited annual balance sheets and profit and loss account.

vii) A resolution passed by the Board of Directors of the company authorising borrowing of the loan be produced to the Bank.

This letter is sent to you in duplicate and you should indicate your acceptance of the above terms and conditions by signing and returning to us one copy.

Yours faithfully,
UGANDA DEVELOPMENT BANK

for: SECRETARY   for: GENERAL MANAGER

..../5

c.c. Chief Accountant;
" Chief Internal Auditor;
" Supervision and Recovery
" Secretary/Board of Directors

/hb.

We on behalf of M/s......................................

accept the loan on the terms and conditions outlined above.

Signed:(i) ....

(ii) ....

(iii) ....

Appendix 9

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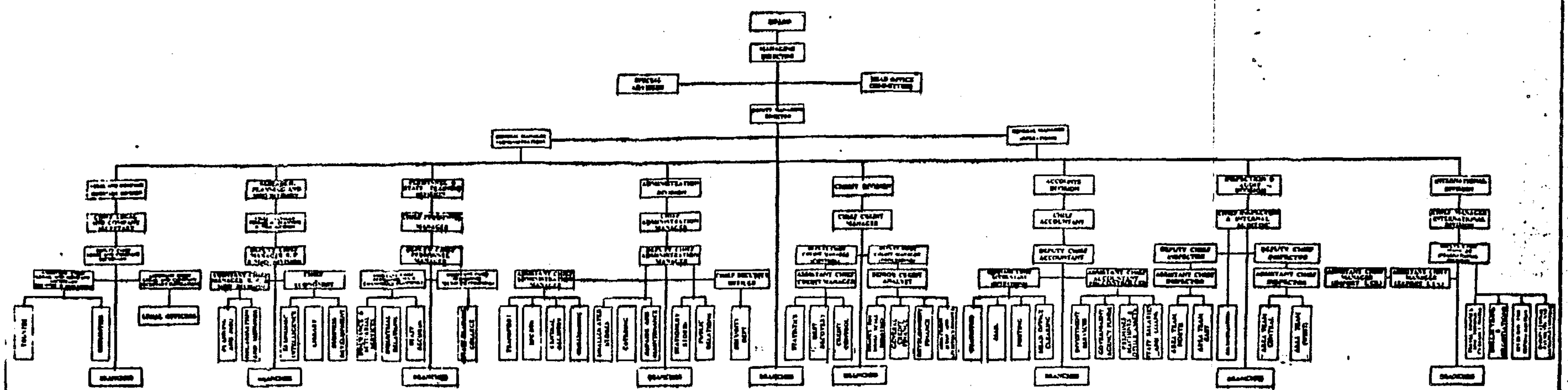
UGANDA COMMERCIAL BANK

ORGANISATION CHART



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ANNEX G

SOCIAL SOUNDNESS ANALYSIS

I. Introduction

The purpose of the project is to develop viable, self-sustaining systems for the effective absorption of investment credit by agricultural enterprise. This is an institution and system building project - focussed on both borrowing enterprises and lenders - with an emphasis on the former. The focus of this analysis will be on the two principal areas of project activity, a) the institution building effort primarily through the Uganda Development Bank, and b) the enterprises to be financed. The cooperative system will also be discussed briefly as this will be one of the principal sub-borrowing enterprise vehicles.

II The ICIs: Uganda Development Bank and Commercial Banks

A. The Uganda Development Bank.

With a broad mandate to serve a large community of development activities, and a primary interest in agricultural and industrial enterprise activities, the UDB is well placed to serve as the lead ICI in the project. The recent establishment of three field offices (Mbarara, Masidi, and Gulu) has further enhanced its utility and exposure in other geographic and rural sectors. Previously, UDB had been lending in these areas, but this required the farmers and owners of enterprises to present loan applications to the UDB head office in Kampala which undoubtedly discouraged a number of potential clients.

A review of staff qualifications of senior and middle level personnel in the UDB indicates that there is a fairly high level of formal education and technical qualifications in the specialized areas of engineering and agriculture. What is lacking to some degree is experience in banking, specifically development banking. (See Institutional Analysis Annex) There are plans to address this issue, however, through support from both the IBRD/UNDP project and this one for training activities, both in-country and overseas.

The UDB, however, together with other parastatal organizations in Uganda, must accept the fact that staff morale is suffering from the very low wage scales. This has forced many staffers to engage in other income generating activities in order to maintain a basic standard of living in an urban area like

Kampala, and has resulted less than full time dedication to responsibilities within the UDB. The problem is recognized by the Government, and there are plans to adjust salaries within the public sector, including parastatals. Inflation rates have also fallen drastically in the past three years (from over 100% p.a. to abut 30% present rate), and with a freeze on new hiring in the public sector, the government hopes to reduce the total civil service through normal attrition.

As conditions within the economy continue to improve, wages and salaries are expected to be gradually increased, hopefully affording the UDB staff the ability to diminish other income generating activities and devote increased attention to bank positions. Making available technical assistance under the RPE Project to the UDB will have a further positive effect on staff morale through on-the-job training, the introduction of new banking and loan appraisal techniques, and other related procedures.

Formal training is another means by which morale and performance standards can be raised. It is a nonmonetized benefit that can be extended to a large number of bank employees. Training can play a significant role in motivating participation in this component of the project. Care should be taken to distribute training opportunities among as many UDB staff members as possible and to set criteria for training that will reward performance.

In combination, the above factors should contribute to further productive participation and diminished self-interest. While this must be a rather guarded projection, it is felt to be realistic in terms of the economic and political upheaval that has beset Uganda in the past decade. Social mores, particularly among the urban wage and salary earning classes, have changed to accept behavior that in normal times would be considered dishonest and reprehensible. The re-establishment of a value system more compatible with norms of western morality, which Uganda once had, will be gradual and will require more security about the future, with accompanying economic and political stability, that have yet to be fully realized.

B. <u>The Commercial banks</u>.

Commercial banks individually will play a lower order but important role in RPE Project. While the exact number of banks to participate has yet to be established, no single commercial bank is expected to utilize more than 15% of RPE Project funds.

Being independent, commercial organizations, these banks have not had problems to the same degree that have plagued the cooperative development bank and UDB in terms of staff morale and inadequate training. Most of these banks are part of larger international banking concerns and have been able to draw support from parent organizations over the past decade. It is anticipated that these banks will be able to take on the additional activity generated by participation in RPE without having to add additional staff resources that they are not able to provide from within their own organizations.

C. Spread Effects, Social Consequences and Benefit Incidence.

Improving the banking capability of the UDB and increasing lending will enable the bank to expand services to a wider clientele. UDB is one of the few banking institutions capable of lending for medium and long term investment which is essential for rural development to take place. The additional resource mobilization and capitalization of the agricultural lending program resulting from project will channel larger sums (including local currency mobilized from the Bank of Uganda through the proposed rediscount facility) toward additional productive activities which if properly appraised and managed should result in ongoing expansion of economic activity and employment generation. UDB should be encouraged to increase the number of field offices as they build up a client base in various regional centers such as Mbale, Soroti, Masaka, and Lira. This would be particularly relevant to the project's contemplated lending for edible oil processing facilities, dairy, and animal feed mills.

Additional training of bank staff provided by the project should result in the diffusion of new knowledge and techniques to make the procedures of the bank more efficient. Short term training courses conducted in country should not be limited to UDB staff only, but participation in such courses be made open to staff of other banks participating in the RPE Project. This training, coupled with the proposed reorganization of the livestock and crops departments into a single agricultural unit, should contribute significantly to positive changes in organizational behavior. Expectations for performance should gradually be adjusted to higher levels, and new working relationships should be established that will ultimately have a positive effect on reestablishing conventional social values. Bank employees must be given adequate advanced notice and apple time to adjust to changes in organization and procedures for best results. Experience has shown that such organizations tend to resist change that is inadequately explained and precipitously implemented.

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III. The Loan Program

A. Sociocultural Feasibility

About 90 percent of the Ugandan population lives in the rural areas and engages in farming to meet subsistence and cash income needs. The protectorate government encouraged smallholder rather than estate agriculture, and today the production of export crops as well as food crops remains a small to medium farm enterprise. There are regional differences in the production of crops for export, with coffee predominating in the fertile crescent, cotton in the northern and western belt, tea in the highlands of both east (Mt. Elgon) and west (Ft. Portal), and sugar in the east along Lake Victoria.

Industry is also geographically clustered. By 1970, a significant amount of industrialization had occured in Uganda, primarily aimed at agroprocessing for export or import substitution. Most of this industry was located in Kampala or Jinja, in the Buganda-Busoga area around Lake Victoria. A pattern of internal migration had developed with (mostly) men from Buganda-Busoga moving to this industrial area to enter the producers on the farms. Immigrant labour from other parts of Uganda or neighboring Rwanda and Zaire was then hired to work on the farms producing export crops (mainly cotton and coffee) as well as subsistence crops. This trend was most pronounced in the fertile crescent around Lake Victoria, but was beginning to be generalized throughout Uganda by the early 1970's.

The Amin period brought a reversal of this trend. After the expulsion of the non-Uganda (primarily Asian) citizens engaged in industry and subsequent takeover by government or local, politically influential individuals, a total decline of industry ensued. For both economic and political reasons, employees of industry returned to their farms where they could grow subsistence crops, trade and surplus and keep a low political profile. According to the 1980 population census, Jinja had a net loss of population over the past ten years. Kampala has remained roughly the same in size, while some of the rural areas have grown as a result of the dwindling of off-farm employment. The impact has been felt throughout the Ugandan economy and into the neighboring countries as former farm laborers have been repatriated. It is anticipated then, that the rehabilitation of productive enterprises will benefit small and medium sized farm producers via improved prices and more competitive markets, provide additional employment for the emerging wage-earning class and improve the supply at

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reasonable prices of certain commodities such as edible oils, meat, and livestock products.

Direct project participants will be the owners and operators of the productive enterprises to be rehabilitated under the project. The exact number cannot be specified, because each loan application must be separately considered and approved, but an illustrative list and order of magnitude are as follows:

Table 1--Project Participants

Activity	No. of Units	Ownership
Dairy Farms	20	Private
Hatchery-Poultry	6	Private
Poultry Farms	40	Private
Poultry Processing Plant	1	Cooperative
Edible Oil Mills	4	Cooperative
Feedmills-Animal	10	Private
Mixed Farms	20	Commercial
Fishing Units	10	Private
Undetermined but substantial number of smaller enterprises (mainly financed by the commercial banks. Private	xx	Private

All of these enterprises are intended to be profit making concerns, operating within generally accepted business practices. Although most enterprises greatly decapitalized during the Amin years, the loans offered under the RPE Project, should allow the assisted enterprises to return to fully competitive and profitable status.

Employees of the enterprises will also participate in the project. It is anticipated that the rehabilitation will allow a number of the firms to operate at or near full capacity instead of at the present low levels (ranging from completely non-operational to about 60% capacity). Most of the employees, including top management are Ugandan citizens. Since so many of the present enterprises are either non-operational or operating at a very low level of capacity, the information and data required to assess hiring practices is inadequate, but information from other sectors such as coffee indicate that men and women generally receive equal pay for equal work.

Low labor productivity appears to be a major constraint to a return to full industrial capacity in Uganda. Two reasons are generally noted for this: (1) wages are so low that workers cannot affort to devote full time to wage employment and survive; and (2) food consumption, in terms of both timing and quantity, is inadequate to provide sufficient energy for a full day's work.

Many employees of AID's targeted enterprises consider their wage earnings as supplemental income to their farming or other income-earning operations. Some of the employment is, in fact, seasonal (e.g., cotton ginning), but other year-round operations have difficulty in recruiting labor because the work interferes with individual productive activities that are equally important for economic survival. This may become an increasing constraint upon the borrowing enterprises under the project until such time as more realistic wages are able to be paid in Uganda. Alternatively, the enterprises might consider a multiple shift work permanently on a part-time basis. This latter approach might have a slightly higher management costs, but it would mean a positive impact on employment with perhaps a reduced level of frustration for the managing staff of a given firm.

The question of low energy levels may also need to be addressed by enterprise management before higher labor productivity can be assured. In most of Uganda, the pattern of food consumption is to eat very little during the day and then to consume a large evening meal. The meal generally has a large quantity of starch such as plantain, millet, rice, white potatoes or cassava as the base, with a limited amount of meat or groundnut sauce. By the middle of the day workers' energy level is low and very little is accomplished in the afternoon hours. Although this pattern is not detrimental to on-farm production, it has serious implications for labor productivity in industry. One alternative would be the provision of a midday meal for workers, as is now done by some manufacturing concerns in Uganda.

Although the loan component is predominantly designed to improve Uganda's economic position, there are a number of considerations that should be taken into account in project development in order to enhance socio-cultural aspects of the project. These are as follows:

1. <u>Industrial Concentration</u>:

Competitive industrial development has been shown to have beneficial impacts on such things as prices paid to primary producers, prices to consumers, and management efficiency. The dairy and poultry industries are fairly diversified, and the controlled price is generally ignored in the case of milk. Local demand and market conditions determine the farmer selling price. Poultry and animal feeds are also expected to be fairly competitive with market conditions establishing the wholesale and retail prices. It is only in the edible oil sector that some concern is being raised. The present high government tax on locally produced oil makes it unattractive to local consumers and this will be a factor in increasing consumer demand for locally produced edible oil. There will be additional demand for oil seeds other than cottonseed created from the installation of new and expanded oilseed extraction facilities. A reduction in the tax on oil would allow for higher prices being paid to farmers and/or lower retail prices for oil while at the same time allow for a reasonable return on the investment in the crushing plant.

2. Employment Impact:

Clearly, getting industry moving again will have beneficial employment effects. One of the criteria by which loans are to be assessed will be the enterprise's ability to generate employment. In cases where factories are operating considerably under capacity, the employment effect should be substantial, even given the labor productivity concern. This may not always be, however, in new job creation, but rather in fuller employment of existing staff.

Rehabilitation implies restoration of prior capacity. In those cases in which a complete reconstruction of the physical plant is necessary, project criteria will require a preference for capital-saving, labor-intensive technologies for maximum employment impact. Even in existing plants, upgrading need not imply capital intensification. For example, the small feedmills, dairy farms, and mixed farms will have a relatively higher input of labor than larger centralized farms or plants. Decentralized and smaller plants will take advantage of location and access to locally produced raw materials, thereby reducing the cost of material transport. Thus, the labor intensity of industry can be shown to coincide with a competitive firm operating on free market principles and need not be selected in order to increase artificially the employment effect.

3. Firm Management:

It is almost universally agreed that local management capacity in Uganda is low. This circumstance has its origin in the Protectorate era, and was continued in the post-independence era with the domination of trade by mostly Asians, both expatriates and citizens. The present economic situation is also a contributing factor, as many experienced Ugandans prefer to remain overseas where their earning potential can be fully realized. The private banks list management capability as a major criterion for lending. In the past, management has been a significant problem for cooperative enterprises such as Wankoko Poultry Cooperative. The project proposes technical assistance for both cooperative and privately owned enterprises to assist management. In each case, it is proposed that the enterprise share part of the cost.

It is intended that some loans will include funds for training and technical assistance to increase and upgrade the cadre of indigenous managers. The most likely means for accomplishing this goal would be to build into the loans specific funding for on-the-job training of qualified Ugandans. In those situations where expatriate management is used, the individual project should establish a plan for training and localizing the management within a specific time frame. This is not an unrealistic goal, given the generally high level of academic training found in Uganda, and practical on-the-job training should be able to provide the necessary "hands-on" skills required by senior management. Many individuals simply lack the experience of management, or have lacked the opportunity to work as part of a competent management team and learn from more experienced managers. The project will provide management training to enterprises on a selected basis as well as consulting assistance to sob-borrowers where required.

4. <u>Geographic Distribution</u>:

Uganda has some 40 ethnic groups, with very distinct and cohesive tribal affiliations centered in specific regions. Politically, economically and socially, these tribal distinctions have caused serious divisiveness among the Ugandan population. Until the Amin period, the Buganda-Busoga region was heavily favored in just about every respect - its favorable climate and soils led to early development of export crop production, and industrial development was centered in the region. Today, the political opposition to the present government is located in this region. Coffee, the major cash crop, has been badly neglected, industry is at a virtual standstill and there remains a fear of punitive military action or common theft not found in other parts of the country.

In addition to reopening old political and economic wounds, the prospects of increasing rural-urban migration emerges with the rehabilitation of industry. The Jinja area experienced a net loss of population over the past 10 years as the economy declined and wage earners moved back to the rural areas and to subsistence farming. City services in both Kampala and Jinja have declined, with housing a particular constraint. So a rapid build-up of population in the two major urban areas would tax already debilitated urban services.

There is also a problem of the movement of raw materials and finished goods within the country. Roads are in poor condition and vehicles in short supply and/or constant need of repair. The cost of petrol is high, and fuel (particularly diesel) is not consistently available. The railway is short of cars. All of these factors contribute to extremely high transport costs.

In view of the tribal, migration and transport concerns, a decentralization of industry would be most desirable and would effect a more broad based distribution of the project benefits. This will definitely be facilitated by the project. Such projects as storage facilities, maize and feed mills, milk cooling centers, oil mills (particularly small, capital saving types to meet local needs), dairy and poultry activities (hatchery and production especially) would all be suitable candidates for geographical dispersion. This should be further discussed with the UDB and participating commercial banks and added to the list of loan criteria.

5. Black Market Activities.

A constant concern in Uganda is the diversion of inputs for other-than-intended uses for personal gain. Magendo, or black market activity, has become a way of life for most wage or salary earners, due to economic conditions of the past 10 years (See the FY 1984 CDSS for details). To the extent possible, safeguards, such as those discussed below, should be built into the project to assure that the project inputs are utilized for the purposes intended.

For the private sector, the necessity to repay the loan in order to stay in business and maintain creditworthiness should in itself be a significant incentive for inputs to reach their proper destination. Moreover, the foreign exchange will not actually be available to businesses to put to alternative uses, rather equipment and raw material orders will be placed against foreign exchange credits, thus limiting opportunities for diversion. Finally, the criterion to invest counterpart resources in the enterprise should be factored in whenever possible to raise the incentive to make the enterprise profitable.

Cooperative enterprises have similar incentives to private enterprise. Here, though, social pressure is even stronger, especially when the proposed activities are at the primary society level, for example, district unions, primary society board members can influence management decisions via social and economic pressure. A high level of participation can be engendered by a requirement that each individual or primary society through the district union engage in a productive enterprise to be required to contribute resources to that enterprise. These resources can take many skills, transport or capital. An incentive to protect the individual's resource investment is thus built into project activity.

This can also operate at a higher level of organization in the cooperative movement. For example, the proposed restructuring of management for Wankoko Poultry Cooperative would make these strictly processing and marketing, rather than production entities. The proposal calls for competent professional management to be hired. This management would be overseen by a diversified Board of Directors that all have an institutional interest in the success of the enterprise, including, perhaps, a representative of the UDB, the Ministry of Animal industries, the UCCU (if they have an equity contribution), the Ministry of Cooperatives, and, most notable, the poultry producer society representatives. This restructuring has other economic advantages, but it should provide better control and accountability. Another example at the district union level of increased participation might be to condition the loan on the holding of elections and general meetings and the production of an annual report together with audited accounts to ensure that primary societies are allowed to participate as they are supposed to.

B. Spread Effect, Social Consequences and Benefit Incidence:

The rehabilitation of agro-industry in Uganda should result in substantial macroeconomic benefit to the country. Increased foreign exchange savings and earnings will benefit virtually all producers and consumers. It is likely that those directly involved in the enterprises to be rehabilitated - owners and employees - will benefit directly. A secondary benefit flow will be directed to small farmer producers, consumers, and to cooperatives. Credit will be available at the beginning of a recovery program and provide an opportunity to move towards longer term investment and development activity.

1. Benefits Resulting from Loan Criteria.

Loan criteria specified in the body of the project paper includes several that will improve the diffusion of immediate benefits from agricultural and industrial rehabilitation. The criteria with most relevance to spread effect and benefit incidence are discussed below.

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a) Direct linkage to increased agricultural production.

Producers of primary agricultural products should benefit via improved access to agricultural inputs and outlets for their produce. As virtually every small farmer in Uganda producers at least once commodity for cash sale, this criterion should cause considerable diffusion of project benefits.

b) Private ownership or market responsiveness.

These enterprises tend to be smaller scale (as for example in the case of feed mills and poultry farms) which generally implies a more labor intensive/appropriate technology orientation. They also operate on a sounder financial footing because they must show a profit to survive, whereas parastatals, for example, may receive government subsidies. Thus, market-oriented firms are willing to pay wages and salaries that will attract the best management and labor, and will pay prices for raw materials that may exceed the GOU control price, if the materials are needed to maintain a certain level of operation. In general, it has been found that there are greater incentives for efficiency in operations in market responsive firms and that some costs can be reduced and higher producer prices can be paid while maintaining the same profit margin. In other instances the mere ability of the private firms to pay cash rather than operating on credit as the cooperatives are often forced to do, allows the private firms to pay a lower price to the producer, but the producer at least gets paid on delivery. AID should also work with the GOU to try to make the cooperatives more competitive on this issue of cash payment. The RPE project provides yet another form for discussion of this cash constraint.

c) Use of local raw materials with few imported inputs.

Any purchase of local raw materials should, of course, benefit the material producers through the availability of both a more reliable market outlet and via increased profits.

d) Enterprise participation in financing of rehabilitation

This in itself is a participatory element of the project. Beyond that, investments of resources should lead to a heightened interest in enterprise success and an incentive to realize a return on the investment. This contrasts with little or no investment that often characterizes public sector enterprises where there is very little sense of "ownership" and responsibility for the firm's operations.

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e) Employment generation

Increases in employment, or fuller employment of the existing workforce will have immediate benefits in terms of the financial status of the workers and their households. In turn, this should generate effective demand for farm products and finished goods, thus having wider economic impact.

f) Use of appropriate technology.

This tends to have a beneficial impact on employment generation, as human capital is substituted for financial capital. Secondly, particularly in a rehabilitation effort, use of the appropriate scale of technology should enhance the financial viability of the firm by discouraging overambitious capital investment aimed at markets that have not yet materialized. For the beneficiaries, sustained employment or market outlets may be more important than higher wages or prices that fluctuate.

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Beneficiaries fall in four major groups for the loan component: owners and employees of industry, cooperatives, individual farmers (producers) and consumers. Although the categories are not mutually exclusive, they are useful for distinguishing the types of benefits likely to accrue to each.

Owners and employees of industry have been discussed above at some length. The only additional point to be made here is that loans should be made on the basis of reasonable rather than exorbitant projected profit margins; and recycling profits into business should be encouraged whenever possible. The AID program should have adequate safeguards attached to ensure that funds are not being used for unreasonable personal enrichment via extensive profit making. A preference should be indicated for reinvestment of capital in the enterprise.

The cooperative as organizations are likely to benefit on a separate level from their individual membership. Many of these oil and poultry processing facilities are owned and operated by cooperatives. Both physical plant and management capacity should be enhanced through he loan component. Cash flow should improve, with cooperatives consistently able to pay producers immediately rather than delaying payment for several months. This will result in enhanced financial stability with funds available to return to members as dividends or invest in other activities.

There are some problems with the politicization of cooperatives management, especially at the district union levels, that will interfere with the efficiency of operation of the enterprise. Special provisions should be built into the loan terms for cooperatives that condition lending on the holding of annual meetings, preparation of annual audited accounts, the election of representative Management Committees and, perhaps, on the appointment of one or more members of the UDB's choice to the Management Committee for the duration of the loan. This individual or individuals could come from the bank, the GOU, or other source, but should be a disinterested party with no local political connections.

Small farm operators will also derive a variety of benefits. Locally-made agricultural inputs, such as livestock feeds, should compete well with higher-cost imports, and farmers should realize a savings there. Secondly, better and more reliable markets should be available for their production, particularly surplus food crops. It should be noted here that although farmers are price-responsive, price alone will not dictate their production decisions. For example, in recent years cooperatives have faced a serious problem in their ability to pay cash on purchase of farm commodities. Farmers who have immediate cash needs may turn to middlemen who are willing to pay cash, even though the price per unit may be lower than the official price. Alternatively, in cotton-growing areas, production has simply been held off the market in some years because of a lack of trust on the part of the farmers. There are also reports that in the cotton-growing zones, particularly in Eastern Uganda, farmers are allocating resources to other cash crops, such as rainfed rice instead of investing in cotton production. Pesticides for cotton are said to be moving poorly, with few farmers willing to invest anything beyond household labor in cotton production. The implications seem to be that even with substantial rises in producer prices over the past two years, farmers may not be meeting their costs, and other commodities appear to be more profitable.

One other factor affecting the diffusion of benefits over the large segment of the rural producer economy is the role of women. Generally, women supply a substantial amount of the on-farm labor and participate in decisions about the farming enterprise. They market food crop surpluses, and occasional cash crops, but marketing and purchase and the use of inputs requiring cash fall generally two the male household members.

A project such as RPE may have a highly differentiated impact on household members. Two means of addressing this concern are: (1) allow women to become individual cooperative members rather than having only one membership per household, and (2) build into the individual loan feasibility studies a requirement to assess the impact of the loan on local household economics. A study has been built into the project as part of the Data Management Component to identify women participants and beneficiaries of the enterprise rehabilitation effort. It should identify how the groups are expected to participate and/or benefit and identify any obstacles or constraints to participation and to receipt of benefits (e.g., the problems of delayed payments of cash to farmers).

Finally, although the other categories of beneficiaries include consumers, it is important to view the loans from the consumption side. Reduced cost to consumers should be a goal of the overall program and applied to individual loan approval processes when applicable. Not only will farm inputs increase in availability and decrease in cost through import substitution, but consumers of certain food products, such as edible oils, dairy products, and poultry should realize a benefit in greater availability. With more employment, there may also be greater ability to pay for such commodities. Ultimately, a beneficial impact on nutrition is anticipated.

Due to the fact that individual loans proposals cannot be reviewed at this stage of project design, the above discussion of spread effect and benefit incidence has been necessarily general.

IV. Cooperative Economic Activity

Because of the importance of the cooperative movement in Uganda in the past, and the likely participation of a number of the cooperatives in the RPE Project, a description of the general cooperative structure could prove useful to understanding how the cooperatives will not only benefit from the RPE Project, but also the importance of this movement in providing the vehicle for small farmer participation in marketing of food and cash crops and benefits from value added through crop processing. It is anticipated that up to 65% of the RPE funds will be used for both rehabilitation and expansion of cooperative agricultural activities during the life of the project.

The Uganda Cooperative Movement is a pyramidal structure based on over 3,000 primary societies with an estimated membership of one million households. The primary societies are predominantly organizations for marketing farm produce. They are very localized entities, managed by committees elected by the membership. The district cooperative unions are at the next level of the structure. There are 33 district unions, each of which is composed of the primary societies in the district. The primary societies have representation on the Policy Committees of the District Unions. There are six national cooperative organizations at the next level of the structure, which serve specialized functions of banking, procurement, transportation and insurance. In all these areas the cooperative unions/societies are free to use services provided by other commercial organizations, and historically the commercial banks have played an important role in providing banking services.

The Cooperative Bank of Uganda was originally identified during the project identification stage as the main ICI. Subsequent reviews of the bank revealed a number of serious shortcomings and constraints that would have been impossible for the project to deal with, however.

Note: This Social Soundness Analysis was based on the original draft written by J. Atherton for the RPE Project at a time when the principal ICI for the project was to be the Cooperative Development Bank (CDB). Subsequently, the target enterprise mix of the project likewise evolved to a degree from the original, heavily export oriented, somewhat higher economic level group. The greater beneficiary population, however, remains fairly similar to the original. although, there is now a greater emphasis on direct agricultural production rather than primarily agro-industrial cash export crop processing as was initially proposed. If anything, the social soundness of the project would appear to have improved under the new design.

* ANNEX H

TELEGRAMS: "FINSEC."
TELEPHONE MINISTER, KAMPALA 43054 & 32370.
OFFICE, KAMPALA 34700/9 (10 LINES).

IN ANY CORRESPONDENCE ON THIS SUBJECT PLEASE QUOTE NO. EC.76/180

THE REPUBLIC OF UGANDA

OFFICE OF THE MINISTER OF FINANCE.
P.O. BOX 8147.
KAMPALA. UGANDA.

15th February, 1984.

H.E. Irvin Coker,
Director,
United States Agency for
International Development
Kampala.

Your Excellency,

Re: **Application for Financial Assistance for Agricultural Sector**

I wish to refer to various discussions you and your officials have been holding with Uganda Development Bank and the Ministry of Agriculture regarding financial assistance for the Agricultural Sector.

The Agricultural Sector has been given top priority in the Revised Recovery Programme and any financial assistance for projects in this area is vital and helpful towards successful implementation of the programme.

In this regard, I wish to formerly request the Government of the United States of America to extend a grant or a concessionary loan to Uganda Government to be channelled through Uganda Development Bank to finance development projects in the following agricultural sub-sectors:

- Agro-Based Industries
- Crop Production
- Dairy Farming
- Poultry
- Piggery
- Fishery

There is also need to strengthen Uganda Development Bank professional staff position relating to the management of the loan and the areas in which the loan proceeds are to be utilized. In this connection, I wish to further request your Government to extend technical assistance to Uganda Development Bank.

Finally, I wish to express Uganda Government appreciation for the United States Government contribution and support during the recent Consultative Group Meeting on Uganda held in Paris and for the continued encouragement and assistance in our Recovery Programme.

Accept, Your Excellency, the assurances of my highest consideration.

(Ambassador E R Kamuntu)

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BANK OF UGANDA

THE GOVERNOR

37/43 KAMPALA ROAD,
P.O. BOX 7120,
KAMPALA

G.68/B/79/B

16th February, 1984.

Mr. Irvin D. Coker,
Mission Director,
United States of America Agency for International Develpment (USAID),
P.O. Box 7007,
Kampala.

Dear Mr. Coker,

Thank you for your letter of 6th February, 1984 following the discussions held at Grindlays Bank (U) Ltd., Kampala, on 23rd January between your representative and the Grindlays Bank.

The suggestion to include private commercial banks as intermediate credit institutions in your proposed Rehabilitation of Productive Enterprises (RPE) project is acceptable to us. As regards the proposal to institute a Credit Guarantee Scheme for small borrowers, I have to advise that the Bank of Uganda has accepted it in principle. As you will appreciate, the Bank will have to establish a special Fund before it could go ahead with the implementation of the scheme. I understand that at the meeting held on 23rd January at the Grindlays Bank, the question of USAID extending assistance to the Bank of Uganda for building the Fund was raised. I hope that the matter is engaging your attention. We would appreciate any assistance from USAID to supplement our efforts in this direction.

Meanwhile, I have advised the Director of the Banks Development Finance Department to attend the meeting when it is convened by you.

Yours sincerely,

(J. R. O. Elangot)
DEPUTY GOVERNOR

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Mr. Winston M. McPhie
Project Design Officer
United States Agency for
International Development

22.6.84.

With the Compliments of
G.V. Ramamurthy, Director,
Development Finance Department
Bank of Uganda

P.O. Box 7120 Kampala Telephone 58441

BANK OF UGANDA - EXPERIENCE IN HANDLING EXTERNAL AID

The Bank of Uganda has been involved closely with both World Bank and I.D.A. Reconstruction Credits to Uganda. Most of the technical work in processing the credits is handled by the External Debt Management Office (E.D.M.O.) of the Bank.

The Aid Co-ordination Unit in E.D.M.O. works closely with Aid Co-ordination both in the Ministry of Finance and the Ministry Planning and Economic Development. The Department keeps full records of all the Letters of Credit opened by importers. It also liaises closely with the World Bank office in Nairobi and Washington to keep accurate records of disbursements of funds by the World Bank. The officers in the Aid Co-ordination Unit physically visit the various importers to resolve problems and to ensure speedy utilisation of the World Bank funds. Where local cover is due to be paid to the Project Account, then this is followed up on an ongoing basis and regular reports are made to the senior Management of the Bank of Uganda and to the Ministry of Finance.

In a recent development, the work of the Aid Co-ordination section was expanded by the establishment of an External Grants Desk. Records of external grant aid will be kept in E.D.M.O.and close contact will be maintained with the various donors. Regular reports will be prepared in the Department on the utilisation of External Grant Aid as to amounts received, amounts still due, associated problems e.t.c. Every type of external grant aid will be handled here whether commodity aid, project related expenditure, technical assistance and relief aid.

STAFFING:

The section on Aid Co-ordination is presently headed by the Deputy Director of the Department. There are two other officers working in this section, one at Senior Banking Officer level and the other at Banking Officer Grade One level.
It is hoped that two more officers will be recruited to this work.

Michael J. Bourke.
MICHAEL J. BOURKE
DIRECTOR, E.D.M.O.

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a) Direct linkage to increased agricultural production.

Producers of primary agricultural products should benefit via improved access to agricultural inputs and outlets for their produce. As virtually every small farmer in Uganda producers at least once commodity for cash sale, this criterion should cause considerable diffusion of project benefits.

b) Private ownership or market responsiveness.

These enterprises tend to be smaller scale (as for example in the case of feed mills and poultry farms) which generally implies a more labor intensive/appropriate technology orientation. They also operate on a sounder financial footing because they must show a profit to survive, whereas parastatals, for example, may receive government subsidies. Thus, market-oriented firms are willing to pay wages and salaries that will attract the best management and labor, and will pay prices for raw materials that may exceed the GOU control price, if the materials are needed to maintain a certain level of operation. In general, it has been found that there are greater incentives for efficiency in operations in market responsive firms and that some costs can be reduced and higher producer prices can be paid while maintaining the same profit margin. In other instances the mere ability of the private firms to pay cash rather than operating on credit as the cooperatives are often forced to do, allows the private firms to pay a lower price to the producer, but the producer at least gets paid on delivery. AID should also work with the GOU to try to make the cooperatives more competitive on this issue of cash payment. The RPE project provides yet another form for discussion of this cash constraint.

c) Use of local raw materials with few imported inputs.

Any purchase of local raw materials should, of course, benefit the material producers through the availability of both a more reliable market outlet and via increased profits.

d) Enterprise participation in financing of rehabilitation

This in itself is a participatory element of the project. Beyond that, investments of resources should lead to a heightened interest in enterprise success and an incentive to realize a return on the investment. This contrasts with little or no investment that often characterizes public sector enterprises where there is very little sense of "ownership" and responsibility for the firm's operations.

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e) Employment generation

Increases in employment, or fuller employment of the existing workforce will have immediate benefits in terms of the financial status of the workers and their households. In turn, this should generate effective demand for farm products and finished goods, thus having wider economic impact.

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H-2

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G.68/B/79/B

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Yours sincerely,

(J. R. B. Elangot)
DEPUTY GOVERNOR

H-3

Mr. Winston M. McPhie
Project Design Officer
United States Agency for
International Development

With the Compliments of
G.V. Ramamurthy, Director,
Development Finance Department
Bank of Uganda

22.6.84.

P.O. Box 7120 Kampala Telephone 58441

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Michael J. Bourke.
MICHAEL J. BOURKE
DIRECTOR, E.D.M.O.

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