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EL PROGRAMA DE CREDITO PARA LA REACTIVACION AGROPECUARIA



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Date: July 12, 2001
To: John Caracciolo, Banking and Financial Advisor/ANRO
From: Warren Gerber, COP/ARC Program
Subject: June 30, 2001 Quarterly Report: USAID Contract No. PCE-I-00-99-00006-00, Task Order No. 806 Agricultural Reactivation Credit Project

According to the Agricultural Reactivation Credit (ARC or CRA) work plan and budget, the contractor is obligated to submit quarterly progress reports to USAID, through FONAPROVI, beginning June 30, 2000. This quarterly report includes a summary of the accomplishments between March 31, 2001 and June 30, 2001, plans for the upcoming quarter, a description of any changes that might affect the performance of the project in achieving the desired results, and any other information that pertains to the management and oversight of the project.

Recent Accomplishments

In the most recent quarter the CRA program accomplished the following:

1. **Managed the CRA and Barents audits.** During the last quarter our own internal audit program, PriceWaterhouseCoopers, the GAO, the Office of the Regional Inspector General from El Salvador, and the Defense Contract Audit Agency all looked at aspects of the CRA program or the management of the Barents contract. PriceWaterhouseCoopers has questions or comments on several of the CRA loans they reviewed, and we will be meeting with them to discuss their concerns. We have not received any notice of findings from the other audits. Over the life of the CRA program we have collected on one loan where the borrower did not use the loan funds for the purpose specified in the investment plan. Three other borrowers have paid of their loan in full, one because he sold the land that was involved in the project being financed, and the other two repaid for unknown reasons.



2. **Submitted the Post-Completion Date monitoring plan for the CRA program to USAID.** The plan includes the following recommendations:

- ◆ Maintain the Management and Oversight Unit (MOU) of the ARC program for an additional 24 months beginning January 2002 to manage and supervise the CRA loan portfolio
- ◆ Aggregate the trust funds from prior USAID financed lending programs into a single new trust fund, to be managed by MOU
- ◆ Expand the delivery of MOU products and services to a wider target group within FONAPROVI
- ◆ Implement a credit supervision program for CRA borrowers and participating banks
- ◆ Enhance the training component of the program using MOU personnel
- ◆ Use the MOU to continue to measure and report on the impact of ARC funds on increased employment, enhanced revenues, and other indicators
- ◆ Procure from USAID an increase of an additional \$4,000,000 in loan funds for CRA on lending through December 31, 2001
- ◆ Execute a short-term technical assistance program that provides the MOU an equivalent of two months of evaluation, support and training by a US credit advisor over the two year extension period

The requests for additional loan funds, as well as the short-term technical assistance component, were deleted from the proposal that was submitted to the senior management of USAID.

3. **Continued the training and technical assistance program for borrowers.** Three training programs on cash flow management were completed during the quarter. One session was held in Nacaome for approximately 45 livestock producers. Another training session was held in El Espino for the 50 members of an association of irrigators who have recently received land as part of a Ministry of Agriculture land settlement program. The land was property that had been foreclosed on by Banco Occidente, and then purchased by the Ministry of Agriculture for redistribution to the newly formed irrigators association. A third session was held as part of a field trip organized by CRA that included 8 bankers from Choluteca and 15 agricultural producers from Agua Fria and Costa del Amate. The field trip's technical session included a review and discussion of cash flows prepared by Fausto Yu-shan for plantain and livestock production. The cash flow analyses were presented as models for the producers and bankers to use when they prepared their own forecasts of what they might expect from investments in those enterprises if the production levels and commodity prices were the same as those projected by Fausto.
4. **Measured the CRA program impact.** In addition to the volume and number of loans that have been disbursed, the CRA program also reports on the employment generated and the value of farm production that result from the loans to the

producers. Through the second quarter 2001, CRA financing has resulted in the creation of 1,908 full time jobs, and has produced over \$17.4 million annually in increased sales of agricultural products, as shown in Table 1.

Table 1. Direct Employment and Value of Farm Production by Enterprise Through June 2001.

Enterprise	Hectares or Unit Financed	Employees per Unit	Total Employees per Enterprise	Per Unit Value Of Production	Total Value of Farm Production
Banana	592	1.00	592	\$7,060	\$4,179,520
Plantain	269	0.55	148	5,067	1,363,175
Shrimp	682	0.22	150	7,353	5,014,746
Watermelon	114	0.66	76	2,576	294,926
Coffee	515	0.55	284	2,669	1,375,763
Milk Cows	4,532	0.0481	218	444	2,012,208
Chickens	241,243	0.00092	222	8	1,929,944
Fish (Ha)	2	1.31	2	37,926	59,165
Horticulture	118	2.30	272	10,000	1,181,200
			Total 1,908		\$17,410,647

In addition to the direct labor added to the workforce as a result of the CRA loans, the project financed the restoration of 1,487 kilometers of livestock fences, provided funds for the production or purchase of 241,243 chickens, and 4,532 head of livestock. CRA funds were also used to rehabilitate, replace or improve \$341,792 in water systems, \$6,890,852 in buildings and installations, and \$1,497,522 in machinery and equipment.

5. **Processed loan applications and disbursed loan funds.** As of June 30, the CRA program disbursed 185,790,151 Lempira in loan funds (\$12,223,036). Eleven banks have participated in the CRA program and have disbursed loans to 410 agricultural producers. Banhcafe is the most active bank with 40 percent of the number of loans, followed by BGA with 20 percent. Both BGA and Banhcafe have about 43,000,000 Lempira in loan volume, together representing over 45 percent of the total volume of loans. Unfortunately, Banhcafe is no longer qualified to participate in the CRA program because they have been removed from the list of approved banks by FONAPROVI.

Plans for the Upcoming Quarter

1. **Monitor and respond to the debt forgiveness legislation.** The legislation that has recently been passed by the Honduran congress involves a financial restructuring plan for agricultural producers. The features of the new legislation include total, or partial, debt forgiveness as well as interest rate subsidies. At this stage we believe that 16 of the 410 CRA loans will qualify for some type of relief under the new

legislation. These 16 loans will qualify for new debt relief because they were included in the program of debt relief legislation that was passed last year (Decreto 28-2000). As part of the new legislation these 16 loans will most likely qualify for a subsidy on the interest rate paid by the producer. This subsidy should have no impact on the interest rate CRA will receive on the loan funds advanced to participating banks, nor on the interest and principal repayment schedules. The remaining CRA loans do not qualify for either debt forgiveness or subsidized interest rates under the new legislation. The CRA staff will be heavily involved over the next quarter responding to banks and borrowers who have questions about the new legislation and how it might affect their loan.

2. **Implement training program on managing problem loans.** During the last quarter the CRA staff developed a training program on managing problem loans that is designed for loan officers who are lending to the agricultural sector. The very high number of foreclosure notices on agricultural properties that are published in the local press indicate non-performing loans are becoming a very serious problem for the commercial banks. Banhcafe has around 14% of their loan portfolio in non-performing status, and without an increase in coffee prices, the non-performing loan volume will continue to increase. It is particularly important that the loan officers use the best available techniques to resolve problem loans if some of the CRA portfolio begins to deteriorate in the future.

Changes that might affect the performance of the project

The legislation that is designed to provide assistance to agricultural producers who have severe debt repayment problems has passed Congress and is in the early stages of implementation. The assistance to the farmers is in the form of debt forgiveness and preferential lending rates depending on the size of the debt, the crop being financed, and other factors.

The legislation is already having an impact on the CRA program. The volume of new loans that is being submitted for CRA approval has fallen slowly but steadily since the legislation was under consideration. Some potential borrowers are probably delaying decisions about taking out new loans until the implications of the new legislation are better understood. The banks are also beginning to exercise more caution with new borrower requests, and they are very busy dealing with current customers who are seeking relief under the new legislation.

A more serious impact of the legislation is the affect it is having on the expectations of the agricultural producers. Many producers are expecting they will qualify for debt forgiveness, or subsidized interest rates, and may not be making loan payments in anticipation of receiving their benefits. If they do not receive their expected benefits they blame the banks for not complying with the legislation. We believe only 16 of the 410 CRA borrowers will qualify for a benefit as a result to the new legislation. However, CRA borrowers who were very satisfied with a loan at 21% last year, now consider the rate "too

high" if their neighbors receive a loan under the new legislation at 8%, or debt forgiveness of 50,000 lempira. The propaganda about the new "Banco Popular" that will receive funding from alcohol and cigarette taxes, and dedicate its portfolio to cheap loans for small producers further adds to their flawed expectations about the products and services they can expect from the financial sector. Using banks, especially the commercial banks, as tools to implement social programs that transfer income from one sector to another runs the risk of damaging the commercial and legal framework required to maintain a healthy financial sector.

Banhcafe has been disqualified as a participating bank by FONAPROVI because of their high volume of non-performing loans. Their non-performing loan volume may increase over the next several months if the price of coffee, one of the important indicators of the health of the bank's loan portfolio, remains depressed. We assume that other banks are also experiencing high levels of non-performing loans and have little optimism for a turnaround in the near future.

Other management and oversight information

CRA program is projected to run out of funds in September 2001. As of July 1 there were approximately \$2.5 million in funds available for disbursement. The rate of disbursement of loan funds has slowed over the past quarter, but the reduction in volume may be in part due to the reduction in marketing effort on the part of the CRA staff and the loan originators.