CLASSIFICATION

PROJECT EVALUATION SUMMARY (PES) — PART I

Report Symbol U 447

1. PROJECT TITLE	2. PROJECT NUMBER	3. MISSION/AID/W OFFICE
Housing Guarantee Program ("Marginal Community Improvement Project")	519-HG-006	El Salvador
	4. EVALUATION NUMBER (Enter the number maintained by the reporting unit e.g., Country or AID/W Administrative Code, Fiscal Year, Serial No. beginning with No. 1 each FY) 83-1	
	☐ REGULAR EVALUATION ☐ SPECIAL EVALUATION	

5. KEY PROJECT IMPLEMENTATION DATES			6. ESTIMATED PROJECT FUNDING	7. PERIOD COVERED BY EVALUATION
A. First PRO AG or Equivalent FY 80	B. Final Obligation Expected FY____	C. Final Input Delivery FY____	A. Total $ 23,750 B. U.S. $ 20,000	From (month/yr.) Nov., 1980 To (month/yr.) March, 1983 Date of Evaluation Review

8. ACTION DECISIONS APPROVED BY MISSION OR AID/W OFFICE DIRECTOR

A. List decisions and/or unresolved issues; cite those items needing further study. (NOTE: Mission decisions which anticipate AID/W or regional office action should specify type of document, e.g., airgram, SPAR, PIO, which will present detailed request.)	B. NAME OF OFFICER RESPONSIBLE FOR ACTION	C. DATE ACTION TO BE COMPLETED
1. Determine amount of ESF available to support shelter program and mechanism for channeling funds. Prepare and negotiate ESF agreement.	Caceres, Sogge, Rifenburg	May 30, 1983
2. Technical Assistance Program and Funds approved.	Brady/Caceres	April 30, 1983
3. Contracting of technical assistance.	Caceres	on-going
4. Projects approved for new FNV projects and INU's $5.0 million.	Caceres/RHUDO/LA	May 15, 1983
5. Approval of documentation for next disbursement.	Caceres/RHUDO/LA	June 15, 1983
6. Preparation of supporting documentation for supplemental authorization FY 83.	Caceres/RHUDO/LA	Aug. 15, 1983.

BEST AVAILABLE DOCUMENT

9. INVENTORY OF DOCUMENTS TO BE REVISED PER ABOVE DECISIONS

- ☐ Project Paper
- ☐ Financial Plan
- ☐ Logical Framework
- ☒ Project Agreement
- ☐ Implementation Plan e.g., CPI Network
- ☐ PIO/T
- ☐ PIO/C
- ☐ PIO/P
- ☐ Other (Specify)
- ☐ Other (Specify)

10. ALTERNATIVE DECISIONS ON FUTURE OF PROJECT

- A. ☐ Continue Project Without Change
- B. ☐ Change Project Design and/or ☐ Change Implementation Plan
- C. ☐ Discontinue Project

11. PROJECT OFFICER AND HOST COUNTRY OR OTHER RANKING PARTICIPANTS AS APPROPRIATE (Names and Titles)

Charles Brady, Chief, GDO.
Mario Caceres, PRoject Officer
Manuel Robles, Minister of Planning

12. Mission/AID/W Office Director Approval

Signature

Typed Name Martin Dagata

Date

AID 1330-15 (3-78)

NOTE: The evaluation team was asked to use the PES format in preparing its report. The format has been modified where necessary to incorporate additional information requested in the scope of work.

13. Summary

A. Program Targets: The targets of the Housing Guarantee Program in El Salvador (519-HG-006) have been revised downward during the course of implementation. The time frame has lengthened and the total output has been reduced substantially from the original estimates. The March, 1980 Project Paper contemplated two phases: a fast disbursing (18 months) $9.5 million which would produce about 7,400 solutions; and a second phase of $5.5 million benefitting about 4,500 families, primarily in secondary cities. Originally, more than half of the total number of solutions were to be home improvement loans. However, a decision was made in 1981 to reprogram funds from home improvement loans to new units, based on the assumption that new shelter could be produced more rapidly. As a result, the estimated output for the first $15 million is now about 3,200 new shelter units, only 27% of the original target of 11,800 beneficiaries.. At the same time, the expectations for rapid disbursements have not been met.

In September, 1982, a request was made for a supplemental authorization of $5 million to produce additional units. It was estimated that all of the units planned for the total authorization of $20.0 million would be completed by July 1984. The estimate was optimistic. Currently, 2,118 units are either completed or in execution, with completion dates in 1983.

No. Units	Expected Completion/Sales
734 (IVU I - 2 projects)	Completed
434 (1 IVU project and part of Prados de Venecia)	May (699 applicants with downpayments)
399 (IVU II - 2 projects)	September (800 "interested" families)
551 (Rest S&L projects)	November
2,118 Total completed or under construction.	

These projects account for approximately $11.7 million of the $15.0 million already contracted. While other projects have been identified which will complete the total Program of $20.0 million, they are still in the approval process.1/ Since projects take about 18 months from the time they are initiated,2/ and since initiation dates are still unknown, it is unlikely that the final projects will be completed before the end of 1984.

1/ Private developers have two projects pending with the Financiera Nacional de Vivienda (FNV) for about 900 units with a value that exceeds $4.0 million. Projects will have to be adjusted to available funds. The Instituto de Vivienda Urbana (IVU) has made a request to the Ministerio de Planificación (MIPLAN) for sole access to the new $5.0 million, presenting eligible projects with a value that surpasses that amount.

2/ The two IVU I projects took 25 months to complete because of problems with water and electrical connections. The five projects which are currently underway will be completed 16-20 months after initiation.

There have been notable achievements in this Program, such as the savings and loan system building its first low-cost projects. However, the achievements are dwarfed by the problem of slow disbursements. The Mission's urgency in delivering housing, disbursing dollars to the Government of El Salvador (GOES), and speeding national economic recovery, is shared by the Office of Housing and AID/Washington. Whereas HG programs in some other countries have been equally lengthy operations, the crisis atmosphere in El Salvador has made the slow pace intolerable.

B. Obstacles to Implementation: There has been concern that high interest rates and the lack of demand might be the principal impediments to the Program in El Salvador. Demand is not a problem, although sales and selection procedures could be improved. Other areas have been identified which have affected both disbursements and the achievement of program goals to a much greater extent.

1. Administrative Procedures

The operational structure in El Salvador is more complex than in many other countries and is part of the reason for the lack of momentum in project implementation. The National Assembly needs to pass two decrees for every loan which is contracted and specifically designates which institution will receive funds, and the amount. Passing a decree can take up to three months. In turn, the recipient institution signs agreements with project developers, specifying the terms and specific amounts of money they will receive. Making changes at a later time is difficult, at best. Even if a different institution can produce units more quickly than the one designated for funds, the money cannot be rechanneled.

Since each tranche of money is handled as a discrete operation, construction does not get underway until a developer is assured that funds are assigned. The HG loans are contracted in stages and each stage usually depends on the production under the previous stage. Because of production problems, the GOES has difficulty timing the contracting of loans to secure terms which are most advantageous. Developers need construction financing for projects, but institutions have waited until loans are contracted to give advances for construction from HG funds. Without production, HG dollars go into an escrow account, inaccessible to the GOES as foreign exchange.

Also, if the unit prices change during construction, which has been the case under the Program, a lengthy review process is needed in order to modify the agreements with developers. Developers work under severe constraints because of new arrangements with ANDA (Water Authority) and electrical companies. They are now required to supply off-site infrastructure as well as the traditional on-site water, sewerage and electrical lines, if the infrastructure agencies determine that off-site work is necessary. Since the reviews by ANDA and electrical companies have no set sequence, a developer may learn of new and costly requirements after a project is well underway.

2. Liquidity

IVU lacks liquidity to initiate new projects. The savings and loan system has a large inventory of unsold, expensive houses and apartments and lacks incentives to initiate new projects. The GOES has not been able to help with liquidity since counterpart funds have not been available; only recently $1.8 million were generated as counterpart from escrow earnings.

Because of capital constraints, large HG advances have been needed, but these were not available early in the Program. With a second disbursement in 1981, the total advance was increased to $6.0 million which has been maintained to date. (See Annex B for dates of financial transactions.) Currently, IVU's outstanding advance represents 78% of the value of disbursements expected for the three projects under construction. But IVU lacks funds to initiate new projects which are projected for the FY '82 authorization of $5.0 million.

When the transactions for the February 1983 disbursement are completed, the total advance for the current projects financed through the savings and loan system (CASA) will represent 70% of the value of those projects. When pending private sector projects are approved by the FNV, the ratio of advance to construction will be reduced to about 39%. The central institution (FNV) does not have resources available to complement the advance. (It should be noted that the FNV's participation in the HG Program has actually had a negative impact on its financial picture to date. Remedial action is being taken by the GOES.)

High advance levels can be maintained for projects which are under construction, and perhaps increased proportionate to the value of those projects. But advances cannot be made against projects which will be financed under future loans. Unless working capital becomes available to institutions from other sources, it will be impossible to build momentum into the HG Program.

3. Policy Issues

In concentrating so much on rapid disbursements, a general vision of low-cost housing strategies has been lost. There is need to focus more on the housing programs of the FNV and IVU, determine where they best fit into the overall sector, and utilize HG resources to strengthen those institutions. Also, there is concern for expanding both the number and the kinds of housing services provided, to expand geographical coverage and to reach more families who are lower on the income scale. Fast disbursement has been used to justify higher cost solutions since institutions have indicated that such projects can be built more quickly. Since some of these projects require 20 months to complete, the time assumptions warrant review and should be weighed against lost benefits, i.e. greater number of units.

IVU's legislative mandate is to serve middle and low-income families. At the same time other institutions, in particular the Fondo Social de Vivienda, have entered the middle-income market on a large scale, and with highly subsidized interest rates, making IVU's projects somewhat redundant and less necessary in that part of the market. To secure a firm place in the housing sector, IVU should be concentrating on low-cost housing. Yet up until now it has sought ways to continue its traditional programming, and is using HG resources as a vehicle to do so. It is adjusting projects currently in-hand in order to fit into the HG structure, rather than designing and promoting new low-cost typologies which meet the paying capacities of low-income groups. There has been pressure on AID (especially from the FNV) to reassess the median income figure and raise the loan ceiling so that higher cost units can be made elegible under the Program. The emphasis should be the opposite, building less in order to reach poorer families. Also, the available data does not justify changing the income criteria of the Program at this time.

At the same time, IVU has a small program for slum upgrading and sites and services, funded with internal resources in order to provide much lower interest rates. Currently, only six project worth about $1.5 million are being funded. In 1980, IVU proposed to the World Bank a total program with an estimated cost of close to $30 million. World Bank funding was not forthcoming. HG resources should be expanding these kinds of projects as well as funding the higher cost units which are currently in the pipeline. (IVU officials have indicated that the interest rates of some of the current projects, as well as future ones, might be adjusted to conform to the HG Program.)

The savings and loan system is producing low-cost units for the first time in its history. The fact that these units are being sold at market rates is of particular importance, since the programs may have an important demonstrative effect in the sector, proving that subsidized rates need not be used for low-income families. HG resources should be used to encourage expansion of these programs, but with more attention to the internal financial structure of the FNV and the associations. (See next section.) If benefits to the system can be more clearly defined, internal resources may be brought into play for low-cost housing when the savings and loan system becomes solvent again.

Along with continuation of low-cost projects like those underway, the potential of the savings and loan system as a vehicle for a home improvement loans program should be analyzed. If a structure can be established, the program should be reactivated. This kind of program could reach families who are very low on the income scale and could provide various financial benefits to the system.

4. Financial Constraints

At the government level, it has been difficult to separate the HG dollar transactions from the colon operation. While theoretically the HG dollar loan is made to the government and the government in turn lends colones to participating institutions at the interest rate it sees fit to use, up until now the terms of the dollar loan have been passed on directly to the institutions receiving colones. The Central Bank has required this structure. An effort should be made to change this policy.

With regard to internal distribution of funds, because of the way the HG Program has been structured so far, the FNV actually has been losing money by having to transfer some of the HG funds to IVU at a lower interest rate than the cost of funds, i.e. 14% money passed at 10% for IVU I and at 12% for IVU II. While this problem may be rectified by an amendment to the GOES-FNV agreement which defines the terms at which funds are transferred, the fact that the structure was imposed on FNV in the first place has created confusion in the institution about the goals of the HG Program and the benefits of participating. The FNV's future HG lending operations should clearly support the system; the first step is separating FNV completely from IVU's operation. Any additional funds for FNV should be for exclusive use of the associations. Low-cost ESF funds could be of considerable benefit to participating associations.

By law, IVU's maximum lending rate is 12%. The project which are currently being financed through the HG Program are at 12% but IVU uses various interest rates for its other programs. A draft decree to remove the interest rate ceiling is being considered. If this legislation passes, IVU's internal interest rate structure should be revised to be more in line with market realities and its internal financial needs. IVU's liquidity problem is directly related to its financial and administrative policies. Unless these are revised, IVU's will not achieve a sound financial position.

C. <u>Next Steps</u>:

1. <u>Definition of Strategies</u>

Mission personnel in El Salvador have suggested an alternative which may be the only way to accelerate the HG Program in El Salvador. If ESF funds can be made available as working capital, new projects could be initiated independent of the status of pending HG loans. Combined advances and ESF could create sufficient capital to provide momentum. With disbursement of HG funds, the original ESF funds would be freed up for new projects. Given the fact that ESF funds have almost no cost, care would need to be taken that the projects are developed with terms and interest rates consistent with HG financed projects.

ESF would also provide leverage to achieve programmatic goals, i.e. financing lower cost typologies through IVU, and providing incentives to the savings and loan system to continue low-cost projects and initiate home improvement loans. For example, if ESF funds are provided to the Savings and Loan system for the continuation of projects like "Prados de Venecia" and eventually for a home improvement loans program, these funds would generate income for the system until such time as higher-cost HG funds come into play. This would improve the financial position of participating associations, and provide additional capital for new projects.

It is recommended that ESF funds be made available to establish a rotating

-TA program initiated with FNV and IVU. Of particular importance are (1) a policy level seminar for FNV officials and presidents of associations on the objectives of HG Program and the financial benefits of participation; and (2) assistance to IVU on medium-term program, to combine and coordinate its upgrading activities with the department which handles new shelter construction. The medium-term program will provide the basis for the funding levels requested for the FY '83-84 HG authorizations. (See Annex C for more detailed technical assistance program.)

-Contracting procedures initiated for $5.0 million of FY '82 authorization.

-ESF funds are disbursed to IVU and work is initiated against the new $5.0 million. (ESF is combined with May disbursement for working capital.)

-ESF funds are disbursed to FNV for new eligible projects.

-FY '83 authorization requested.

3. Expansion of the Institutional Structure of the HG Program

It has been suggested that other institutions, especially the Fondo Social de Vivienda (FSV), should be included in the HG Program in order to produce more units more quickly. Of the various housing institutions operating in El Salvador, the FSV is one of the largest producers. However, for inclusion in the HG Program the key is "eligible" mortgages. The average unit price of FSV is close to C.18,000.00, but more importantly its interest rates are between 5-7%. FSV officials have indicated that they are not interested in changing the institution's interest rate structure nor in participating in the HG Program. The institutions currently participating either use market rates (Savings and Loan System) or have modified their interest rates (IVU). These institutions are capable of producing more shelter projects and should remain the main thrust of the HG Program for the foreseeable future.

14. Evaluation Methodology (Reason for evaluaton, Methods, Sources)

There has been concern at all levels within AID about El Salvador's HG Program. The Program has taken almost twice as long as originally estimated; figures on units constructed and sales have been confusing; each updated target subsequently has needed to be revised. The evaluation was proposed as a means to analyze the obstacles to disbursements and to make recommendations which could accelerate the program. Since new funds were authorized in FY 1982 ($5.0 million) and additional funds are being considered for FYs '83 and '84, questions have arisen about the absorptive capacity of the institutions with which we are working, and whether alternative institutions could be used. The final scope of work was described as a "truncated shelter sector assessment" because it included ideas and questions that go far beyond an analysis of the program's current structure.

Given time and personnel constraints, the evaluation will not be able to address all of the concerns laid out in the scope of work. Over the next five months, various techncial assistance activities should be programmed. These complement and expand upon the evaluation effort. The evaluation report describes how the program has functioned up until now, the reasons for some of the delays which have occurred, and provides a strategy for the next five to fund for participating institutions which capitalizes itself over time. The distribution of ESF would depend upon the amount of funds available. The colon equivalent of $10.0 million would provide the greatest flexibility. If between $5.0 and $10.0 million can be made available, they should be divided equally between the FNV and IVU for new projects. If less than $5.0 million are available, IVU should be given priority to initiate some of the projects projected for the $5.0 million which will be contracted this year. With the establishment of a mechanism for disbursing ESF funds, two separate lines of action should be begun simultaneously:

(1) Funding new IVU projects, with the condition that IVU includes upgrading or sites and services projects in addition to the higher cost units it is currently proposing. The projects would move forward independent of the three IVU projects which are currently under construction.

(2) Transferring ESF funds to FNV to use within a given period of time, for new projects like those which are underway, providing the system with margins which will increase liquidity. Sufficient ESF funds would be needed to be able to continue production at a reasonable level. $5.0 million would produce about 900 units using similar unit design and cost figures to those currently under construction. At this level of funding, it would be possible to require that the FNV open a new line of credit for home improvement loans when ESF funds turn over, e.g. designating about $1.0 million to initiate this operation for low-income families. The leverage for inititating a home improvement loans program depends on the availability of a sizeable fund.

A reasonably large working capital fund would provide momentum in project construction. The HG contracting process could occurr simultaneously with project initiation, or after the fact. If fewer ESF funds are available, the impact will be less, but still positive.

2. Specific Steps

-The pending private sector project(s) are approved by the FNV for the remaining funds already contracted (approximately $3.3 million).

-Disbursements are made against the "Jose Simeon Cañas project" (IVU) and part of "Los Prados de Venecia" (S & L) and for advances for new projects. If possible, all $5.5 million are disbursed from escrow.

-New IVU projects are approved for the $5.0 million authorization, including upgrading and sites and services projects. AID agrees that the HG funds, when contracted, will be exclusively for IVU.

-AID/El Salvador determines amount of ESF funds available and establishes mechanism to disburse them to the GOES.

-The GOES arranges mechanism to disburse funds directly to institutions. (The FNV may be a recipient but cannot be the proxy of the GOES in distributing to other institutions.)

-A memorandum of understanding or agreement is signed between AID, MIPLAN, FNV, and IVU which outlines use of funds and the distribution of margins. (See ANNEX D) to bankruptcy by the end of 1981,[1/] the normal relationship with developers changed completely. Now developers must build both the on-site and complementary off-site infrastructure, if required. The work is supervised, inspected, and approved by ANDA. Construction costs accrue to the project. Once operating, the final system must be turned over to ANDA. A similar situation exists with CAESS although the causes are slightly different. The concession, owned by a foreign firm, may not be renewed in 1984 when the current contract expires. Therefore, the company is not willing to make major investments. Previously, the off-site and on-site connections were made by CAESS free of charge since cost recuperation was distributed over the entire system. (CAESS works in the Metropolitan Area of San Salvador and some secondary cities.)

Some developers do not have the expertise needed to carry out the work. IVU, for instance, has resorted to contracting ANDA for the work it previously carried out automatically. Whether the work is contracted or done in-house, the developers have had to gear up for work which previously was not their domain. IVU was caught off-guard in 1981, and the long delays in making water and electrical connections in the IVU I projects were directly attributable to the confusion caused by the new requirements. Now the institutions are fully aware of the additional requirements and include them in their programming although the total costs are not always known at the outset of construction.

Because of the new rules and because of uncertainties which are built into the design/approval process for projects, project developers are faced with much higher risks than before. Once projects are approved in principle by ANDA and CAESS, developers prepare plans, secure interim financing, and actually begin construction before the "details" of ANDA and CAESS requirements are known. There is no set sequence for ANDA and CAESS reviews. If recommendations require additional expenditures, a developer may already be well along in the urbanization and construction of the project. Often assumptions prove incorrect. In the case of "Prados de Venecia", CAESS required that the developer install a main electrical line over one kilometer long instead of accessing to an area next to the project site. An additional C.335 per unit is attributable to this electrical work. The total increment, if approved by the FNV[2/], represents an increase of 5.2% from the original estimated cost per unit.

The developer of "La Toma" in the secondary city of Aguilares has a much more serious problem since the infrastructure which was required by ANDA is extremely costly. The developer planned to hook up to the sewerage lines contiguous with his project site. Because ANDA determined that those lines did not have the proper carrying capacity, the developer is currently

1/Most of El Salvador's infrastructure agencies are in serious financial trouble. The priority has been rebuilding damaged systems in war zones.
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six months. It addresses the potential for expansion of the institutions which are currently participating, and whether the Fondo Social de Vivienda (FSV) should be included in the HG Program.

Information was derived from project files and from interviews with Mission personnel and policy-level, technical and social staff of the key housing and urban development institutions in El Salvador, and from site visits to projects and informal interviews with beneficiaries. The persons contacted are listed in Annex A.

15. External Factors (Major changes in project setting, Continuing validity of assumptions)

With the continuation of the civil war, El Salvador's economic crisis has deepened since 1980 when the Project Paper was prepared. It is instructive to review the assumptions in the Logical Framework (Annex B of Project Paper) which are related to the achievement of the goal, purpose, and outputs.

Assumptions
"Political Stability achieved."
"Programs supported by other donors implemented as planned."
"Qualified directors remain as heads of key institutions involved in project implementation. Housing sector institutional and financial structue rationalized."
"Inflation rate doesn't exceed rate projected in PP." (18% 1979, projected up to 20-30% PP p.3.)
"No shortage of building materials."

Except for inflation, it might be said that none of the assumptions have been valid for the Program up to this time: The political situation remains volatile. Institutions such as the World Bank and the IDB have a moratorium on lending to El Salvador. The Government and the heads of participating institutions were changed in 1982, causing difficulties in program continuity and in the contracting of the $5.5 million tranche. The rationalization of the institutional and financial structure is far from accomplished. Finally, the lack of foreign exchange has caused shortages of imported building materials, some of which are critical to project completion, e.g. pumps for wells to provide potable water to new units. While no official statistics are available, it appears that inflation is lower than projected (estimates range from 7% to 11%) but this can be attributed to deepening recession rather than to positive economic indicators.

The new arrangements between project developers and the Water Authority (ANDA), and the largest company for the distribution of electricity (CAESS) should be included under "external factors". Previously ANDA supplied all off-site infrastructure for urbanizations. Once a project was approved, the developer was able to lay out the internal distribution network for water and sewerage connections with the assurance that hook-ups could be made when the project was completed. ANDA either extended the main lines of a system or dug on-site wells to supply the new housing developments. Because ANDA was close

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Because of the new rules and because of uncertainties which are built into the design/approval process for projects, project developers are faced with much higher risks than before. Once projects are approved in principle by ANDA and CAESS, developers prepare plans, secure interim financing, and actually begin construction before the "details" of ANDA and CAESS requirements are known. There is no set sequence for ANDA and CAESS reviews. If recommendations require additional expenditures, a developer may already be well along in the urbanization and construction of the project. Often assumptions prove incorrect. In the case of "Prados de Venecia", CAESS required that the developer install a main electrical line over one kilometer long instead of accessing to an area next to the project site. An additional C.335 per unit is attributable to this electrical work. The total increment, if approved by the FNV2/, represents an increase of 5.2% from the original estimated cost per unit.

The developer of "La Toma" in the secondary city of Aguilares has a much more serious problem since the infrastructure which was required by ANDA is extremely costly. The developer planned to hook up to the sewerage lines contiguous with his project site. Because ANDA determined that those lines did not have the proper carrying capacity, the developer is currently

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finishing a sewerage trunk line which is approximately 1.5 kilometers long, built under extraordinarily difficult circumstances. The average unit cost of "La Toma" is now estimated to be C.14,700 instead of the original estimate of C.11,800, and increase of almost 25% per unit. Even with these increases, this project should be elegible under the HG, i.e. affordable to the below-median income population, but the margin has decreased substantially and there may be difficulties in marketing the more expensive units. (The final costs estimates have recently been submitted to FNV for approval.)

16. Inputs (Quality, quantity, timeliness; changes needed)

The HG Program represents just one component of the $33.35 million "Marginal Community Improvement Project" (519-0251). The distribution of the total package, slightly revised from the Project Paper, is provided below. Disbursements have been completed for the other program components.1/

	Combined DL, DG, HG & GOES Counterpart (in millions US$)
Community Basic Services	$11.850
Agrarian Reform Support	.200
Small Business Loans	2.150
Shelter (HG)	18.750
Planning Phase II	.300
Evaluation	.100
TOTAL	$33.350

*Includes $3.750 million of GOES counterpart funds.

While the conceptual framework of the HG Program was divided into two phases, this phased plan is no longer operable. The use of "Phase I" and Phase II" is misleading and should be dropped. The total HG program has been increased to $23.750 million, with the authrorization of $5.0 million in FY 1982. The counterpart funds of $3.750 million remain unchanged. Only $1.872 million of counterpart has been made available to date, from the interest earned on escrow. With the February 1983 disbursement, the escrow account was closed and the colon equivalent of interest earnings were placed in a special counterpart account. (See Annex B) Given the severe economic constraints in El Salvador, additional counterpart funds may be difficult to secure.

1/ An audit of the largest component outside the HG Loan, Community Basic Services, was conducted in May 31, 1982. At that time 87% of the programmed funds had been disbursed and the remainder was largely a matter of reconcilation of accounts. Two institutions (Direccion de Desarrollo Comunal - DIDECO - and Oficina de Recursos Especials - ORE) supervised various executing agencies which carried out a total of 431 sub-projects (roads, drainage, bridges, water, electricity lines, etc.) in approximately 18 months. Although no records were reviewed, according to Mission personnel the small business component has been fully disbursed, with demand exceeding available funds.

A. Production of Shelter and Disbursements

The following table provides an estimate of disbursements for projects which are currently under construction. It includes the IVU I projects for which there is a disbursement still pending of approximately $200,000. These projects were initiated against the first $9.5 million which was contracted in November 1980. Since the unit prices have increased, part of the $5.5 million currently is escrow will need to be utilized for these projects. The FNV has not yet approved projects for the remaining funds (of the $15 million contracted).

Projects	No. Units		Est. Disbursements*
IVU I (2 Projects)	734	Completed	$3,624,960 ($190,840 pending)
IVU (Jose Simeon Cañas)	200	est. May	1,254,000
Prados de Venecia(part)	234	est. May	1,276,430
IVU (San Martin)	133	est. Sept.	833,910
IVU (LLanos del Espino)	266	est. Sept.	1,667,820
Prados de Venecia(part)	239	est. Nov.	1,303,704
La Toma	312	est. Nov.	1,774,085
	2,118		11,734,909

*Total Cost less 5% downpayment of beneficiaries.

B. Planning Component

The component "Planning for Phase II" supports the shelter program and originally was a Condition Precedent for Phase II disbursements. The Sub-Secretary for Housing and Urban Development (HUD), established in 1979 under the Ministry of Public Works to provide guidance to the sector, is responsible for this component. The initial conception of the Program was to extend housing services to secondary cities in Phase II. However, the geographical framework of the Program was not possible to maintain since the decision to build in secondary cities has depended more on assessments of the feasibility of operating in particular zones than on estimated needs, demand and the careful programming of resources.1/ Therefore, this component's activities are no longer linked to the planning of specific projects, but rather to development of the sector's policies and structure. While overly ambitious for the short run, many of the component's objectives remain valid.

1. Develop shelter sector coordinating and monitoring procedures to guide the activities of domestic sector institutions;
2. Complete overall shelter-needs studies for at least two secondary cities;
3. Develop minimum urbanization standards and site legalization policies and procedures for secondary cities; and
4. Obtain the adoption by GOES authorities of a consistent interest rate structure for financing of new shelter solutions and home improvements. (Implementation Agreement, Section 5.04, C.)

1/ From the beginning, projects were initiated in secondary cities. Of the completed projects and those in execution, 55% of the units are in the AMSS, and 45% in secondary cities.

Top priority has been given to an analysis of the very diversified housing sector in an attempt to introduce some consistency and oversight to its many institutions. In July 1981, AID authorized HUD to carry out studies for the "National Low-Cost Housing Policy Program" (Programa Nacional de Politicas de Vivienda - PRONAVI) and extended the component's PACD one year, to April 20, 1983. The studies were completed in late 1982. The two consulting groups focused on different aspects of the sector, but both reached the conclusion that the only way to rationalize the sector was to form a Ministry of Housing and a Housing Bank which would absorb various existing institutions. Since such an action affects the "territory" of institutions and political parties, it will depend ultimately on the political climate in El Salvador. Until such time as an independent Ministry is established, the Sub-secretary of Housing and Urban Development will have little influence on the sector. However, to strengthen the bases for future action on a Ministry of Housing, an "implementation" plan is being funded, with a further extension of the PACD, to December 31, 1983. The implementation plan includes a seminar with policy-level personnel from the respective institutions to review the findings of the studies, hiring short-term consultants to refine the legal aspects of structural and financial changes, an effective demand study for low-cost housing in San Salvador and three secondary cities, a training program for selected staff, and the operating budget of the coordinating unit.

No other Technical Assistance resources are included under the HG. There have been requests from institutions in El Salvador for various activities. A number of areas have been identified which are critical to the Program and which should be funded in the near future. An estimated $30-35,000 should be budgeted for technical assistance in 1983. (See Annex C.)

17. Outputs (Progress against projected targets, Significant management experiences, problems with inputs and assumptions, Changes needed to achieve purpose)

A. Progress Toward Targets

The greatest reduction in the Project Paper's physical targets was caused by the collapse of the home improvement loans component. FEDECREDITO (Federation of Credit Unions)and FEDECACES (Federación de Asociaciones Cooperativas de Ahorro y Crédito de El Salvador) had been identified to channel at least $4 million to home improvement loans for the target population in the MASS and secondary cities. FEDECACES was excluded from the Program, and FEDECREDITO declined to participate because it considered land tenure problems insurmountable among the target population. From April-July, 1981 the GOES and AID discussed a "Plan to Accelerate the HG Program". Since there was no adequate structure to carry out a home improvement loans program, it was decided that the monies designated for home improvements would be reprogrammed for new shelter solutions. Instead of an estimated 5,300 home improvement loans in the first Phase alone, only about 1,000 new units could be built with the same funds (using average cost estimates from the PP =$3,600 per unit).

Changes in Targets

March '80 (PP)		Sept.'82 (Supplemental Auth.)	
		New Shelter	
New shelter	4,090	1rst Authoriz.	3,199
Improvements	7,245	2nd Authoriz.	770 *
Total benef.	11,785 est.	Total benef.	3,969 est.
Total Funds	$18.750 million	Total Funds	$23.750 million

*NOTE: This figure is from the PP supplement for $5.0 of new authorization, using maximum unit prices allowable under the program. If lower cost units are included in the Program, e.g. upgrading and sites and services, a larger number of solutions could be produced.

The number of units projected under the Program is being reduced because the participating institutions are constructing the highest cost solutions allowable under the Program. IVU is currently building 36M² two-bedroom units which cost C.16,500 ($6,600) and is proposing the same for future projects. These represent the lower end of the middle-income clientele which IVU has served traditionally. The tendency has been to approve such projects if they justify faster program development and subsequent disbursements.

B. Programmatic Changes

IVU has a wide range of programs, including slum upgrading, but these have not been included under the HG program. In the past, IVU has preferred to use internal resources for these projects so that it can charge only 7% interest. The A.B.C. upgrading program ("Acceso al Bienestar Comunitario") was presented to the World Bank in 1980 with a total cost estimated at C.142.888 million ($57 million). Since World Bank funding was not forthcoming, IVU proceeded with its own resources, but on a very limited scale. While C.11 million were proposed for this year, only C.4.3 million were budgeted ($1.720 million). The upgrading can cost up to C.11,000 per unit, but IVU officials say that the average cost is about C.5,500 per unit. They also indicated that the average income of families in the areas where the A.B.C. program has been carried out is about C.400. Based on the average unit cost of C.5,500, a family with much lower incomes could afford the program even at the higher interest rate of 12% which is what IVU now charges for its complete houses.1/

IVU's financial picture has changed dramatically in the past few years. Whereas previously it received low-cost funds from the government's general revenues, this source has been almost eliminated. For 1983, HG funds represent 52% of IVU's entire budget of C.18.1 million. Administrative costs are extremely high and collections are a serious problem, e.g. borrowers can be three months in arrears legally. Because of its financial difficulties, IVU officials are now more amenable to charging higher rates in all projects, and are looking for ways to become more solvent. They have indicated that some of the current upgrading projects (perhaps $1.5 million in construction), as well as future "A.B.C." projects could be financed at 12% to make them elegible for the HG Program.

1/Average Cost	Interest	Payment	Minimum Income
C.5,500	7%	C.46.00	C.184.00
	12%	C.64.00	C.256.00

For new units, IVU's 12% interest is low compared with the market rate in El Salvador. The private developers, financed through the savings and loan system, have a much more difficult time reaching the target population than IVU does since they charge the market rate, 16%, in comparison with IVU's 12%. As a result, private developers are building core units which start at C.13,000 (20M²) with higher monthly payments than the much larger units being built by IVU. (The GOES provided the guideline of C. 13,000 for the private sector builders.) The fact that there are two sets of financial conditions has made IVU's product artificially cheaper than the private sector's. The general characteristics of the completed projects and those in the pipeline are presented below:

	Completed	------------In Execution-------------		
	IVU I	IVU II	--private developers---	
Unit Cost	C.13,000	C.16,500 est.	C.13,600est.	C.14,700 est.
Payment*	C.130.00	C.180.00 est.	C.214.50est.	C.229.00 est.
Lot Size	50.0M²	90.0M²	60.0M²	55.0M²
Roof Area	25.0M²	38.4M²	20.0M²	25.0M²
(enclosed)	(19.4M²)	(36.0M²)	(20.0M²)	(19.7M²)
Interest	10%	12%	16%	16%
Period	20 years	20 years	15 years	15 years

NOTE: C.2.50 = US$1.00.
*Payment includes insurance.

IVU's legislation establishes a maximum interest rate of 12%, A raft decree is currently being prepared for introduction to the Assembly which would remove the restrictions on IVU's interest rates. If it passes, IVU's internal interest rate structure can be made more consistent with the other participating institutions and more compatible with the cost of resources.

18. Beneficiaries, Demand and Selection

A. Beneficiaries in completed projects

The scope of work called for a sample survey of beneficiaries in the first two IVU Projects. Time did not permit more than informal conversations with beneficiaries during visits to project sites and conversations with personnel in charge of beneficiary selection. Based on these brief contacts and a review of files in IVU, the evaluation team is satisfied that the target population was well served in the IVU I projects. Many of the families living in San Bartolo core units are employed in the informal sector and were previously excluded from housing programs because of both the levels and variability of their incomes.

A large number of families moved into the project before water and electrical service were provided and the units were officially adjudicated. Temporary electrical lines were built by a community action group, and water was purchased from trucks. Even without individual connections the project offered a definite improvement for families, compared with their prior living conditions. For example, one family previously lived in a centrally located "meson" (rooming house) in a room approximately $16M^2$, sharing facilities with a dozen other families. Rent was C.100 per month. Since November when services were connected, the same family pays C.130 per month for a larger room and private bath ($19.45M^2$), and covered patio with possibilities for expansion. At least half of the residents have made some improvements, and perhaps 20% have initiated or completed major expansions. Some even have built two-story additions behind the original core unit.

B. Demand

The issue of demand has been raised repeatedly because of the slow pace of project sales in the first IVU project. While there may be some problems with demand, they are minor. The reporting system, rather than the lack of clientele, was responsible for most of the concern regarding sales. In IVU 1, the units were not officially "sold" until services were connected, a title was processed and families were making payments. Meanwhile, the houses were "reserved" months before with downpayments, and many people had actually moved in prior to the formal transactions.

Personnel from IVU's Social Services Department say that the sales for the core unit project in Santa Ana (IVU I - "Los 44") were more difficult than for the nearby San Bartolo Project. Of the 200 applicants on file in Santa Ana, none wanted to opt for a core unit instead of the traditional two-bedroom unit for which they had applied. There was also a reluctance on the part of staff to promote the core units which they considered "sub-standard". Sales did not begin until technical assistance was provided and a step-by-step plan was developed. As a result, an intensive promotional campaign was started in April 1982, e.g. radio, newspapers, visits to factories, etc. The families applying for the core units tended to be informal sector workers, in contrast to the bulk of IVU applicants from the area who have salaried jobs. (About 90% of all of IVU's borrowers are salaried workers.) While all 234 units were sold by September (delivered in November when water was connected), IVU staff are still not completely convinced of the progressive development construction strategy. They do not feel that additional units of this design should be built in Santa Ana, but rather the larger units for which there is continuous demand.

According to IVU staff, San Bartolo was easy to sell and there are still more than 150 eligible applicants waiting for units. Meanwhile IVU is completing 37 additional core units units that were not included in the first HG package and is planning to build 1,400 similar units in the project area in the future. Immediate plans, however, are for 200 two-bedroom units such as those in projects under construction. (The extra core units in San Bartolo, worth perhaps $200,000, should be included in the next HG disbursement, and new core units should be included in the next programming excercise.)

The three projects currently being constructed have units which approximate IVU's larger traditional unit and the Social Services Department does not foresee any sales problems. In the San Salvador Area very little promotion is needed since there is a backlog of applications (est. at 4,700 in

The procedure of reserving specific units has disadvantages to the developer and association since if an applicant drops out or is rejected, the unit must be resold. The credit department estimates that about 10% of the applications currently on file are "doubtful" because incomes may not be sufficient to cover the higher monthly payments of the revalued units. Also, the Credit Committee must review all applications, even those which are considered risky by the analysts. (IVU system is more efficient since applicants are qualified before particular units are assigned.) Nevertheless, the developer insists that the reservation procedure is more effective since the buyer who is able to select the precise unit he or she will buy is a more serious client.

Although the developer has a number of years of experience in sales, this kind of project represented a new experience since the type of clientele is quite different than they have had in previous projects. The firm conducted a cost-effectiveness analysis of the first stage of promotions, i.e response produced by newspaper, radio and television announcements. The developer is confident that he can produce sufficient applications at relatively low cost.

The clients are also new for the association. Selection criteria, based on FHA criteria and internal guidelines, were made somewhat more flexible as a result of previous technical assistance; these criteria are undergoing more changes as a result of face-to-face meetings with prospective buyers. A large number of the applicants identified for "Los Prados" are street sellers and independent workers whose income is more difficult to verify than salaried workers who make up the majority of CASA's borrowers. Credit analysts are discovering that they need to use more subjective judgements in making their recommendations, since the new clients are less likely to have credit records and other documentation that was previously considered routine.

19. Institutional Arrangements

> "Due principally to the extreme urgency to provide assistance quickly, flexible implementation arrangements have been developed to foster speedy implementation. Funds will be channeled through the Central Bank. The Ministry of Planning will approve incremental allocation of funds for those Phase I activites which are implemented fastest." p. 4 Annex A of First IA Amendment.

Contrary to the expectations at the time of the Implementation Agreement, the structure for the flow of monies in this Program has been rigid. The structure should be reviewed from two perspectives: the GOES procedures for borrowing money from an external source, and the internal distribution of funds for projects.

A. GOES Borrowing Procedures

Some officials say that the Central Bank should be the borrower, with a Government guarantee, rather than the Government itself, represented by the Ministry of Planning. When the GOES borrows directly, the procedures for approval are longer since the National Assembly must pass a number of decrees

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Dec. 1982) although some of these applications are up to three years old. The majority of applications are for two-bedroom units similar to those in the "Jose Simeon Cañas" project. Since few core unit projects have been built, the institution's backlog does not tend to include families requesting this type of unit, but with minimum promotional efforts it has been relatively easy to generate applications.

As of February, 1983, there were 423 applicants with downpayments for the 200 units in the "Jose Simeon Cañas" project. The other two projects (399 units) are in secondary cities, 20 and 100 kilometers from the capital. About 800 families have expressed interest in these projects, although they have not made downpayments as yet.

The two private sector builders are at different stages. The "Prados de Venecia" Project (473 units) in the Metropolitan Area initiated its promotional campaign, but suspended it after two months because there was too great a response too early in the cycle. Up to 1,500 people visited the project during the campaign. A downpayment of C.090 is required to "reserve" a unit at which point the sales office begins to verify and analyze the applicant's standing, 276 families have made downpayments. The first families have become irate with delays since they had been told that units would be ready in December. Since only about 80 houses will be ready by the first of April and another 100-150 in May, the developer decided to avoid further problems until prompt delivery could be assured.

Once the the sales office is sure that information is complete, the application is sent to the Savings and Loan Association (CASA) for analysis by the credit department. According to the CASA's credit department, 164 applications were forwarded to CASA, but 10 dropped out. Of the remaining 154, the credit department forwarded 25 cases to the Credit Committee which approved 19 and rejected 6. (Three presented problems with income levels and three passed the allowable age for eligibility for insurance.)

The credit department could process at least 50 applications a month, but has been unable to proceed with the current file until final unit values are approved and the exact downpayment and monthly payments can be calculated.1/ The technical department of the association has just completed a review of the new unit values and has forwarded the revised estimates to the FNV for approval. The review and negotiations between the association and the developer took more than three months for the two projects. This process needs to be refined and shortened so that applicant selection can be carried out on a more timely basis. The FNV approval of changes is generally pro forma.

1/At the time projects are approved by FNV, agreements are signed between FNV and the Association, and between the association and the developer for specific amounts of financing. If changes are made in the amounts at a later time, as has been the case with both projects, a review process must occurr and new agreements signed.

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in order for the Government to proceed, i.e. each time the GOES requests a bid, decrees are needed both to accept and offer and to ratify the contract when it is signed. Passing a decree usually takes a number of weeks, and can delay various months. The Central Bank, on the other hand, can borrow without approval and ratification by the Assemby. All told, there are 29 steps when the GOES borrows money from an external source, compared with 14 steps for the Central Bank. According to government officials, when the HG Program was designed, the Central Bank declined to be the borrower. Even if the Central Bank were to change its position, the advantages for contracting funds have to be weighed against the delays in writing a new Implementation Agreement, which would be required if the borrower were to change. As long as new HG authorizations can be made against the original Implementation Agreement, the present system should be maintained. If, howevever, a new Program is designed in the future, the implications of the borrowing entity should be more fully explored.

As the Program currently stands, the Assembly has passed decrees which designate the FNV as the recipient of two tranches of HG money (totalling $15 million); the GOES has signed one agreement with the FNV for $9.5 million and is pressuring the FNV to sign a second agreement for $5.5 million. The FNV, in turn, has signed agreements with both CASA, the only participating savings and loan association, and with IVU for projects totaling $10.4 million (with revaluations of private sector projects the total worth of these projects is approximately $11.7 million). CASA has agreements with each of the two developers who are carrying out projects.

Another problem surfaces in the timing of contracting and disbursing money. Institutions have required advances to initiate projects which means waiting until HG funds are contracted (which can take up to three months), securing the advance and placing the remaining amount in escrow. When the GOES contracted the first tranche of HG funds ($9.5 million), the lending rate was relatively high (14%), but earnings on escrow were even higher, so that the GOES had a positive position prior to disbursements. In the case of the second contract, for $5.5 million, the borrowing rate was also 14%, but since interest rates fell, escrow earnings are lower. Therefore, the GOES is extremely anxious to move the funds from escrow to the FNV to avoid losses. However, FNV is not anxious to receive the funds since it has not yet approved projects for the entire amount.

The circumstances surrounding the bidding process for the second contract ($5.5 million) caused confusion among official circles. The first request for bids was made in early 1982 and the offer from Paine Webber was rejected by default because the Government changed hands during that period and the new Government could not respond in the required time. After a dialogue with AID, the new Government accepted a second bid from Paine Webber in September, 1982, but not all officials were convinced that it was the most appropriate time to contract the funds. For future contracts, RHUDO/LA and PRE/H should be closely involved to clarify issues and reach a consensus on timing of bids and negotiations.

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A separate but important issue is that once HG funds are contracted they are disbursed to an escrow account. Until they are released the GOES does not have access to foreign exchange dollars which it desperately needs. If the dollars were available for commercial purposes, the earning would be higher than cost. Also, if the Government were able to use the dollars with greater facility, it would be easier to separate the cost of HG dollars from the internal transactions in colones. In principal there is no reason why the GOES should pass the colon equivalent of HG funds to a participating institution at the same interest rate as the borrowed dollars. Rather, the internal rate should stem from the internal market and the operational margins needed by participating institutions. However, the GOES, based on a Central Bank policy, has made a direct connection between the colon and dollar transactions. The use of parrallel terms for the dollar and colon operations has caused confusion and disparities among participating institutions. Because of the lending rate policies of other housing institutions, in particular the Fondo Social, the costs of HG funds have seemed excessive.

B. Internal Distribution of Funds

IVU's participation caused a serious financial problem for the FNV because it was required to pass funds costing 14% to IVU at the rate at which it was lending, i.e. 10% for IVU I projects and 12% for IVU II projects. Some background information is needed to put this problem in context. The first $9.5 million contracted in November 1980 was expected to be used almost in its entirety by the Savings and Loan System and private developers. Almost $6 million was programmed for 1,600 units in "Las Cañas" Project and another $2.4 million might have been used for an additional 600 units. An executive decree was passed which directed the Ministry of Planning, the GOES representative, to sign an agreement with the FNV; once the agreement was signed, an advance of $2.225 million was passed to the FNV for "Las Cañas". For a number of reasons, "Las Cañas" had to be withdrawn from the Program and the Government decided to substitute two IVU projects (IVU I) which were close to completion, and which were to have interest rates of 10%. In October 1981, the FNV was required to formulate an agreement with IVU and to transfer the outstanding advance to IVU. FNV signed a second agreement for IVU II in March, 1982 for projects which would be developed at IVU's maximum legal rate of 12%. No arrangement was made for the government to assume the difference in the interest rates, so up until now IVU's participation has represented a direct loss to FNV. If IVU's participation was minimal, perhaps the losses could have been covered internally by the FNV. However, with the completed projects and those currently in construction, about $7.5 million or half of the first $15 million authorized will pass from FNV to IVU. According to government officials, a retroactive amendment to the original GOES-FNV agreement is now being processed which will pass funds designated for IVU to FNV at the same rate. In essence, the GOES is assuming the subsidy involved in the transaction. While this will prevent losses to the FNV, it will not provide any margin to the institution.

Although the problems described above may be alleviated in the near future, it is understandable that the FNV is unclear about the benefits of participating in the HG Program. Even when the problem with IVU is resolved, the new arrangement will not provide benefits to the FNV since money will simply be transferred at cost. In the case of the projects sponsored by the associations, FNV has a small margin during the construction period while there is interim financing, but none during the mortgage period. The association receives an adequate margin throughout the financing period, but their overall financial siturtation of the system is precarious.1/.

Interim Financing: FNV - 16% to Association - 20% to Developer.
Long-Term Financing: FNV - 14% to Association - 16% to Borrower.

20. Strategy and Recommendations

There is a clear need to break the IVU-FNV connection. For the new $5.0 million, the GOES is seeking ways to pass the money directly to IVU. Under previous operational procedures, the GOES indicated that IVU could not assume obligations for HG funds and, therefore, needed to receive funds via a separate financial institution such as the FNV. A legal opinion has been received that states that IVU's current legislation could be interpreted to allow it to directly participate in the HG Program without a go-between such as FNV. This ruling is currently passing through the Ministry of the Presidency and may have to be submitted to the Assembly in the form of a Decree. AID should make this a condition for providing HG funds to IVU in the future. Each participating agency should have a direct tie with the Government, without a go-between.

Actions must be taken on various fronts. Liquidity needs to be increased so that new projects can be initiated immediately, and the programming process must be strengthened for the medium-term. At various times the possibility has been mentioned of mixing ESF and HG funds in order to lower the interest rates. This issue has been based on the hypothesis that high interest rates were affecting demand and were a primary cause of slow production, sales and disbursements. It appears that the design/approval process itself and the lack of working capital within participating institutions are a greater problem than the lending rates. In the case of the projects currently under construction, HG advances have become de facto working capital, but this arrangement has its limitations. Given the constraints in El Salvador, very large advances should be continued, but this will not provide momentum for new projects for future HG funds.

1/ In a draft report prepared by Checchi and company on the National Economic Recovery Program, the findings on the construction sector highlight the difficulties of the Savings and Loan System. It indicates that there is an unsold inventory of housing units worth C.138.9 million, 75% of which was financed by the savings and loan associations.

A. The Use of ESF

The Mission in El Salvador has indicated that the ESF alternative is still open if it would substantially speed up the housing program. With sufficient ESF funds provided as working capital, institutions could proceed with new projects immediately, without waiting for the termination of current projects and the subsequent contracting process for new HG funds. Such funds provide the possiblity of complementing HG advances for projects under construction, as well as for initiating projects which are not yet subject to advances (until new funds are contracted). Under ideal circumstances, HG funds would be disbursed directly against completed projects, without need for escrow accounts or phased disbursements. For example, if IVU were to produce $5.0 million in elegible mortgages with ESF colones, $5.0 million in HG dollars would be contracted and disbursed directly to the GOES which would make the colon equivalent available to buy those mortgages, freeing the original working capital for other projects. The ESF funds could be established as a rotating fund which capitalizes itself over time, providing both a good return on investments to participating institutions and a margin to increase the fund for future lending.

It is recommended that such a fund be established, and that a memorandum of understanding or agreement be signed by the principal actors (AID, MINPLAN, FNV, and IVU) for the use of these funds. (See ANNEX D.) Ideally, the equivalent of about $10.0 million should be made available since IVU and FNV can absorb this amount annually. This amount would cover the $5.0 million already authorized and $5.0 million of a new HG authorization for FY '83 (the FY '83 authorization may be higher).

If fewer ESF funds are available, the flexibility to begin new projects is reduced. However, certain measures can be taken which are outlined below. The funds for IVU and the FNV have been differentiated, although disbursement transactions will take place simultaneously.

April 1983	Approval of the transfer to IVU of $190,840 pending from IVU I.
April 1983	Approval of new private sector projects worth $3.3 million to complete pipeline of $15 million.
May 1983	CASA requests disbursement of $1,276,430 against first phase of "Los Prados". Entire amount disbursed to FNV for continuation of current projects and initiation of new projects (Total outstanding advance to FNV - $4,160,830 or 65% of the value of projects ($6.343 million).
May, 1983	IVU finishes 200 units (Jose Simeon Cañas) - Value $1.254 million
	Disbursement of $[illegible] from escrow to IVU against request of $1,444,8[illegible]; $558,750 of IVU's current advance is liquidated. Outstanding advance = expected disbursements of $2,501,730 (2 projects/399 units expected completion in September).

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May, 1983	Decision made on amount of ESF funds available.
May, 1983	Decision made on use of counterpart fund colones. ($1.6 - $1.8 million). If GOES agrees, these could be designated to IVU.
June, 1983	Contracting Process for FY '82 $5.0 million begins.
June, 1983	ESF funds disbursed to IVU and FNV (if available). IVU begins work on new projects with combined funds from ESF and May disbursement, and possibly with counterpart funds. Given availability of ESF, FNV requests the submission of new project proposals.
Sept. 1983	IVU II projects completed and previous advance liquidated. New $5.0 advance contracted. 40% advance to IVU of $2.0 million.

B. <u>The Inclusions of the Fondo Social de Vivienda in the HG Program</u>

Since the Fondo Social de Vivienda (FSV) is the largest housing institution in El Salvador, it has been suggested that it should be used as a channel for HG resources. Because of this interest, the evaluation team analyzed the institution and found the following:

1. In building new projects, the FSV is no more agile in construction than either IVU or the Savings and Loan System. Actually, the FSV uses the capacity of the System to implement projects. Therefore, nothing would be gained in terms of construction time. On the other hand, the FSV's projects tend to be large scale and would represent large disbursements.

2. The FSV has a large clientele, primarily because of its subsidized interest rates, rather than due to its expertise in promotion and sales. However, because it is a closed system, many low-income families are excluded from the housing services of the FSV, and many of the clients within the system are not families below the median income.

3. The FSV's lending policies provide for subsidization at all income levels. Its interest rate policy both distorts the market and precludes a sound structure for housing finance. For example, through the FSV a family with a monthly income of C.600 can purchase a house worth C.25,000. The same family applying through the channels of the savings and loan system could afford a house worth only C.14,800 because the associations use the market rate of interest. If the HG Program were to support the FSV without changes in its lending policy, it would contribute to further disarray within the housing sector in El Salvador. The FSV is not amenable to changing those policies at this time.

4. The FSV is the only housing institution in El Salvador which has a large source of funds which are both obligatory and cost-free. Annually, the FSV receives more than C.50 million ($20 million) and should be collecting C.10 million ($4 million) on its portfolio. The fact that it currently has problems with liquidity has to do with its lending policies and administrative deficiencies, e.g. almost 40% arrears, rather than the lack of capital.

In summary, the FSV is not an appropriate vehicle for HG resources. These funds should be used to strengthen the institutions which are currently participating in the Program. These entities have made considerable progress in establishing sound financial mechanisms, and in the long-run may better serve the housing sector of El Salvador.

ANNEX A

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Fondo Social de Vivienda (FSV)
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ANNEX B

Key Events/Transactions to Date

Date

June 1980 Implementation Agreement signed
Aug. 1980 $15.0 million HG Authorized
Nov. 1980 Las Cañas Project Approved (1,600 units)
Nov. 1980 $ 9.5 million contracted

	$ 9.500	million
less	.950	HG fee
	$ 9.405	principal
less	2.225	advance to FNV for Las Cañas
	$ 7.180	to escrow

July 1981 Agreement signed GOES-FNV
Oct. 1981 Two IVU projects approved to replace Las Cañas
Oct. 1981 Agreement signed FNV-IVU (IVU I) for $3,435,120 of HG funds

	$3,816.8	value of construction
less	381.6	10% downpayments of beneficiaries
	$3,435.1	

$2.225 million advance transferred from FNV to IVU

Nov. 1981 5 new projects approved; 1,384 units to be built by both IVU and Private Developers, worth $7.7 million.
Request for advance of $3.775.

	$ 7.180	principal in escrow
less	3.800	advance*
	3.380	remain in escrow

*Escrow agent required to disburse in multiples of $100,000.

March 1982 Agreement signed FNV-CASA
March 1982 Agreement signed FNV-IVU (IVU II)

	$3,800.000	advance to FNV
less	3,060.480	advance to IVU (total outstanding $5,285,480)
less	714.520	advance to CASA
	$ 25.000	remain in FNV

Sept. 1982 Supplemental authorization of $5.0 million.
Nov. 1982 IVU completes 2 projects (734 units)
Dec. 1982 $5.0 million contracted; to new escrow account.
Feb. 1983 First escrow account closed.
$1,872,357 in interest earned is used to provide dollars for payments of previous HG Programs - $1,651,775. The remaining $220,000 dollars may be used to provide CASA with foreign exchange to purchase a computer. A counterpart colon account was established equivalent to $1.872 million.

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$3,380.000 principal in escrow
less 1,210.120 to IVU (total outstanding $3,060.480*)
less 2,169.880 advance to CASA (total outstanding $2,884.4)
- 0 - principal

*With this disbursement against the $3 435.120 in mortgages agreed to in Oct. '81, IVU liquidated its original advance of $2.225 million. It should be noted that IVU is claiming a total of $3,624,960 for these mortgages since it required only 5% downpayments from beneficiaries instead of the 10% which was estimated ~~at~~ the time ~~the~~ agreement was signed with the FNV. The additional $190,840 must be approved by FNV and another agreement signed.

ANNEX C

Technical Assistance Requirements

Inputs are needed for IVU and the FNV, to clarify the role of the HG Program within those institutions and to stengthen their global housing programs. Of immediate importance is the determination of the appropriate levels of new HG authorizations for FYs '83 and '84 and to better define the strategies that should be followed over the medium term.

I. Technical Assistance for the FNV

There has been confusion at various levels of the FNV regarding the purposes and procedures of the HG Program and how low-cost shelter programs fit into the structure of the system. This confusion may increase since a series of personnel changes are expected in the savings and loan system in late April or early May. Once the personnel configuration is known, the FNV and associations should be approached with proposals for a policy level seminar and workshops for operational staff.

May 1983 a. Policy level seminar: For top-level officials of FNV and associations to present the objectives of HG programs, explain guidelines and procedures, and to discuss the financial benefits of participating in low-cost shelter programs.

2 days
Potential Candidate - Pedro Lusa

May 1983 b. Review of procedures for project analysis, approval, and cost revaluations; Workshop on recommendations for streamlining process.

5 days
Potential Candidate: Josefa Arroyo

June 1983 c. Review of procedures for promotion, and applicant qualification/ selection; Workshop on recommendations for streamline process.

2 weeks (in combination with similar assistance to IVU)
Potential Candidate: Benigna Magallon

August 1983 d. Initiation of investigation on future structure for home improvement loans program.
2 weeks (with second stage set for later time)
Potential Candidates: Antonio Reyes (CACEN/Bolivia)
Jaime Bordenave, CHF

II. Technical Assistance for IVU

IVU has two departments which should be involved in the HG Program. The A.B.C. program concentrates on community upgrading and up until now has been completely separate from the "Production" department which develops new shelter units. Technical assistance should be used to coordinate the work of these departments as well as to help IVU to strengthen its internal financial structure. The existing portfolio does not produce adequate revenues because of past interest rate policies. The administrative structure, programming and budgeting need analysis. Administrative costs are extremely high and collections are also a significant problem.

IVU should be approached immediately with proposals for the following activities.

May 1983 — a. Definition of a medium term program which coordinates HG and other resources for both A.B.C. projects and new shelter. The result of this work will provide much of the justification for the next HG authorization.

b. Analysis of IVU's administrative structure and project budgeting procedures to seek ways to reduce overhead costs and to determine the most efficient operational procedures.

4 weeks
Potential Candidates: Josefa Arroyo
Tova Solo

June 1983 — c. Review of promotion, selection, etc. (See c. above.)

July 1983 — d. Analysis of IVU's collections sytem and recommendations for reducing arrears.

1 weeks
Potential Candidate: Benigna Magallon

Sept. 1983 — e. Financial analysis of IVU's portfolio and interest rate structure, recommendations for improving financial position and development of curriculum for selected staff members for training in financial analysis.

2 weeks
Potential Candidates: Eliacer Fernandez
Eugene Brady

III. Other Technical Assistance Activitie

May 1983 — a. Meetings with the Ministry of Hacienda, MIPLAN and the Central Bank to explain the HG Program and to discuss the separation of HG dollar transactions and internal colon transactions.

2 days
Potential Candidate: Pedro Lasa

b. Review of reporting system for HG program to clarify production and budget reports from participating institutions to the Mission and from the Mission to RHUDO/LA and AID/Washington.

3 days
Potential Candidate: to be identified

ANNEX D

Agreement on Use of ESF

The agreement reached between the Mission, MIPLAN, and participating institutions should specify how funds will be used and their operational structure.

1. The projects financed with ESF must be directed at families below the median income and the mortgages or loan terms must be compatible with the HG Program. In the case of IVU, 12% interest must be used until such time as that institution's interest rate ceiling is changed or eliminated. When that occurs, new interest rates must be determined for proposed projects. The Savings and Loan System must continue to produce mortgages at the market rate of interest.

2. In the first tranche of ESF, IVU must include sites and services, upgrading and other low-cost solutions, along with the higher cost projects it is currently proposing. For the second round of projects, the lowest cost solutions will be given priority.

The FNV will continue to build core units (and serviced lots if proposed). Efforts will be made to establish a structure for a home improvement loans program during 1983. When the first round of projects is completed, ESF will be used to finance such loans as well as new projects.

3. Assuming that the cost of ESF will be approximately 3%, the following margins are suggested:

	FNV
Cost to FNV	3%
Admin. Spread	2%
Cost to S&L	5%
Admin. Spread	4%
Capitalization	7%
Construction finance	16%

	IVU
Cost to IVU	3%
Admin. Spread	6%
Capitalization	7%
Construction finance	16%

4. Funds should be transferred in a lump sum to the respective institutions. Since in the Savings and Loan System they may not be utilized immediately for construction, the agreement should stipulate that these funds may be put in time deposits and that at least 7% of the earnings generated will be destined to capitalization of the fund. Since time deposits pay 12%, earnings will cover costs and provide for capitalization. For example, if an association receiving funds cannot place them immediately, a 12% time deposit will cover costs to FNV (5%) as well as provide 7% for capitalization of the fund. The association will have incentive for moving the funds into projects in order to earn the administrative spread indicated above. In the case of IVU, there should be less delay in initiating projects. However, the same stipulation should be made regarding time deposits and 7% capitalization of funds.
NOTE: At 7%, the fund will almost double over a ten year period.