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Country Development Strategy Statement

FY 1986

HONDURAS



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I. Country Situation and Background

A. Political, Economic, and Social Situation

Honduras is one of two functioning democracies and the poorest country in Central America. Of its 4.1 million people, 2.6 million live in rural areas. GDP per capita income in 1981 was estimated at \$675. The economy's real GDP growth rate dropped from an average of 7% during the late 1970's to a negative rate of over 1% in each of the last three years. Average real per capita income has declined by almost 14% from 1981. In 1978, the average per capita income was \$155 in the countryside and \$496 in the urban areas. In the same year, the estimated poverty line income per person was \$230. Some 77% of rural residents and 34% of urban residents had per capita earnings below that level.

Honduras' impoverishment is evidenced by most of the characteristics normally associated with underdevelopment. The literacy rate is 60%, life expectancy is 57 years, infant mortality is 87 per thousand, the average age is 16 years, and the population is growing at 3.4% yearly. The human resource base is very weak, and infrastructure and public services are woefully inadequate. Unemployment is estimated at 20%, and underemployment at an additional 30-35%.

Honduras' long-term social and economic development is impeded by a rugged and mountainous terrain often unsuited for cultivation, use of a high percentage of the most fertile and tillable land for cattle raising, a fragile and deteriorating natural resource base, an economy largely based on tropical export agriculture subject to large swings in the terms of trade, the second highest population growth rate in the Western Hemisphere, weak private sector organization and aggressiveness, and government institutions with limited ability to effectively formulate and execute policies and programs.

Despite its underdevelopment, Honduras has traditionally enjoyed social stability. Its relative internal peace and harmony are largely the result of its pluralistic society, traditional respect for human rights, measures taken by development-oriented governments over the last thirty years to provide a more equitable distribution of land and social services, and the promise of progress engendered by major investments in infrastructure and productive activities. High population growth has been partially absorbed by an agricultural frontier, which is rapidly disappearing. The country has been assisted in maintaining limited but steady social and economic progress by the government's willingness to cooperate with external investors and donors.

The country's present economic recession and the turmoil in Central America have begun to seriously threaten its relative peace and harmony. Honduras' nervousness about the intentions of its southern neighbor, the guerilla war in El Salvador, social and political instability in Guatemala, a limited domestic market and a contracting external sector, and declining foreign and domestic investment levels have resulted in a downward trend in production. Low prevailing prices for the traditional commodities which make up 77% of Honduras' exports, an unfavorable shift in the terms of trade, sharply reduced

capital inflows and a 9% rate of inflation over the last few years have led to disruption of traditional economic activities and diminished convertibility of the country's currency. Hondurans' traditional lack of confidence in

economic situation has deteriorated and the possibility of a spillover of the unrest in neighboring countries remains high.

Without major economic policy changes, significant external assistance, and an improved political environment in the region, prospects for a revival of economic growth in the near future are poor. Prices for agricultural commodities are still low and little improvement is projected for the next few years. Central Bank foreign exchange reserves are now about negative \$115 million, and would be lower were it not for strong Central Bank control over the allocation of hard currencies. The Government's fiscal deficit grew from 8% of GDP in 1981 to 11% in 1983. Without GOH action to curb it, the 1984 deficit is expected to be around 10% of GDP. Access to foreign commercial bank resources has been severely curtailed. The pending rescheduling of \$121 million in commercial debt arrearages and red-lining of Central America by foreign banks promises little near-term relief from the lack of sufficient foreign commercial credit. There is a growing recognition that the import substitution growth model engendered over the last two decades by the Central American Common Market (CACM) is inhibiting the country's economic development and that a different strategy must be designed and implemented to restore economic growth.

representatives from both the U.S. Embassy and USAID/H, has been developing a comprehensive analysis of the country's economic situation, and is exploring adjustments to the GOH's macroeconomic policies which would promote short-term economic stabilization and set the base for sustained growth. A new IMF Stand-by is expected to be negotiated in the next few months, and its implementation should further help strengthen the country's ability to carry out the needed economic adjustment and minimize the human suffering that accompanies such changes. The World Bank has indicated its willingness to negotiate a structural adjustment loan, once the Stand-by has been agreed to. The Stand-by should also facilitate completing renegotiation of the small portion (10%) of Honduras' external debt mentioned above.

Honduras has made a major commitment to continue with the democratization process initiated in 1980, and is counting on U.S.G. support for continuing the process, strengthening the country's economy, and defending itself against external threats. In the long run, the country's ability to maintain its democratic form of government and its commitment to private initiative will depend on its ability to provide for improved living standards for its people by increasing participation in the benefits that come from modernizing the economy and increasing exports which are competitive on world markets. Greatly increased external commercial and concessional financing will be needed over the CDSS period to restore economic growth, design and implement a new development strategy, and return Honduras to the path of sustained social and economic development.

B. U.S. Objectives

The USG's long-run objective is to support a traditional trading partner and ally. Over the CDSS period, and perhaps beyond, there are three more specific U.S. objectives: to assist Honduras to further advance the democratization process, restore and then increase economic growth, and preserve its territorial integrity.

Restoring economic growth, and thereby increasing employment, improving living standards, and meeting the basic human needs of the country's overwhelming poor population, is a sine qua non to success in consolidating the democratic process. The country's territorial integrity must be preserved in order to ensure that the democratization process is not disrupted by terrorism or armed conflict, and to provide a secure environment within which economic growth can resume. As the democratization process is consolidated, Hondurans in all walks of life would increasingly feel they have a stake in their society. This should help to increase their confidence to invest their time, energy, and resources in their own and their country's future.

C. Rationale for U.S. Assistance

The rationale for U.S.G. support to Honduras is based on four interrelated factors. First, as stated in the report of the National Bipartisan Commission on Central America (NBCCA), Honduras is of great strategic importance to the U.S. in its efforts to maintain free, democratic societies in the western

hemisphere. Second, Honduras is worth helping. Third, it is willing to help itself. Finally, assistance to Honduras holds reasonable promise of producing the desired results.

As a free, democratic society, Honduras is surrounded by countries whose stability is threatened by externally supported interests hostile to the Honduran and the U.S. way of life. Honduras wants and needs U.S. assistance to maintain its constitutional democratic form of government and improve its defense capabilities. It is currently cooperating effectively with the U.S. on security matters, and probably more than any other, is an ally on which the U.S. can count for regional cooperation over the long run.

Honduras is worth helping because it is a close neighbor which shares U.S. democratic values and ideals. It is making a serious attempt to live as closely to those values and ideals as possible under very trying conditions of social tension, economic distress, and external threat to its democratic institutions. It is a natural ally and traditional supporter of the U.S. in world fora. It has shown it is willing to help itself by its strong push to develop itself over the past three decades and its recent progress in establishing democratic, constitutional government. Finally, assistance to Honduras holds reasonable promise of success. There is nothing basically incurable in Honduras' current economic malaise, and the recent U.S. commitment to its security has helped to mitigate Hondurans' doubts about the country's future. With appropriate and adequate assistance and effective government economic policies, the Honduran economy can be turned around and its traditional steady progress in improving living conditions restored.

II. Goals

A. Short-term (1985-87)

Our short-term goals are essentially to help Honduras restore equilibrium to its economy, develop the policy base for long-term growth, and maintain social peace and tranquility during what promises to be a period of sacrifice and retrenchment. The degree of adjustment needed to restore equilibrium in the fiscal and balance of payments accounts cannot be predicted with precision. However, a reduction of the budget deficit from 11% of GDP at the end of 1983 to 8% and 5% by the end of 1984 and 1985, respectively, would appear necessary. As well, balance of payments equilibrium should be achieved and the system of foreign exchange controls progressively dismantled and eliminated by the end of 1985. The GOH should gain effective control over decentralized public entities and divest itself of as many productive activities as possible. Where public interest dictates government operation and/or management of production activities, their management and performance should be significantly improved. The GOH's basic laws and policies regarding investment, tariffs, and export development should be revised to favor increased exports. Informal barriers to investment and exports, such as required government approvals for normal business transactions, should be significantly reduced.

GOH implementation of a stabilization program will probably lower living standards and may well increase unrest among the country's already impoverished people in the short term. The painful and wrenching adjustments that will take place during the retrenchment will temporarily dash the hopes of many for improved living standards. Low income rural families will see their earnings diminish to the extent that the cost of transportation, imported agricultural inputs, and consumer goods rise in relation to the prices they can obtain for their products. Low and middle income urban families are likely to be hurt the most, as they consume more imported goods than their rural counterparts and derive more of their income from salaries. The urban unemployed are the most likely to give up hope and look for solutions that threaten political stability.

The GOH realizes that an effective stabilization program is needed. It has called on the USG, the International Monetary Fund (IMF) and the World Bank (IBRD) for assistance, and all have expressed a desire to help. The GOH expects to obtain from these institutions about \$180 million in FY 1984 and about \$220 million from FY 1985 through FY 1987 for its stabilization program.^{1/} The USG, given the broader nature of our relationship with the GOH, has a special role to play. In view of the objectives set forth above, the short-term stabilization program must represent a reasonable balance between achieving economic stability and maintaining political stability. Thus, some of our assistance must be aimed at helping the GOH to minimize social unrest during this difficult period. Accordingly, a major effort to increase employment in the short run forms an integral part of the short-term strategy. Rather than adopting a defensive posture, we propose to collaborate with the GOH in development of a "first offensive" against unemployment with up to \$100 million of AID funds to create up to 40,000 person years of employment during this period.

B. Long-term (1985-90)

Over the longer term, a significant increase in investment and modest real GDP growth must be achieved. The benefits of growth should be shared more equitably, and reflected in improved living conditions for the large majority of Hondurans. The goals to which the strategy contributes are:

- an increase in employment by 250,000 jobs by the end of 1990, which will accommodate labor force growth during the CDSS period;

- an increase in average per capita income of the rural poor from \$155 at present to \$200 in 1990; ^{2/}

- an increase in primary school enrollment from 87% of the primary school age group in 1982 to 93% by 1990;

^{1/} These figures include \$112.5 million of ESF funds from AID in FY 1984, and \$180 million in FY 1985 through FY 1987.

^{2/} This assumes that per capita income for the rural poor has changed little since 1978.

- a reduction in infant and child mortality from 87 per thousand to 70 per thousand by 1990;

- an increase in access to potable water from 60% to 85% in major cities and from 50% to 70% in rural areas by 1990;

- an increase in the prevalence of contraceptive usage from 27% to 45% of fertile women and a decline in the rate of population growth from 3.5% to 3.0% per year by 1990;

- an increase in the number of standard housing units from 150,000 to 200,000 by 1990; and

- continued progress toward permanent institutionalization of democratic electoral and judicial processes.

DA and ESF resources, PL-480 commodities, and USG guaranteed housing loans and trade credits totalling \$767.1 million are proposed for FY 1985 through FY 1990 to help achieve these goals. In addition, at least \$1.5 billion of new Honduran and external private sector investment and \$1 billion of other donor resources will be needed to facilitate reaching the above objectives. The kind and magnitude of support from these sources is described in Section III below.

C. Assumptions

In attempting to help Honduras reach these goals, the Mission has made several key assumptions. They are that:

- the U.S. continues to have high political and military interest in Honduras;

- Honduras will not be drawn into open conventional military conflict with neighboring countries, or forced into putting down a significant domestic insurgency;

- the results of political unrest and attempts at subversion do not retard the GOH's ability to implement an economic recovery program; and

- the U.S. Congress provides the funds and guarantees required.

III. Program Strategy

A. Overview

The Mission's program strategy is to help the GOH stabilize the economy and decrease social pressures from rising unemployment during the first three years of the CDSS period, and progressively increase investment in long term development throughout the CDSS period. Economic stabilization will be achieved through GOH implementation of important macroeconomic policy changes

aimed at correcting current economic disequilibria and creating the policy base for a long-term, export oriented growth strategy. Maintenance of social stability will be furthered by the "first offensive" against unemployment. Long-term development efforts will be aimed at increasing employment, providing a minimum of food security, improving equity and participation of the poor in the country's economic and social development, and strengthening public and private services to better meet the basic human needs of the poor. This will be accomplished by improving sectoral development policies, expanding private sector production, fostering technology transfer, and developing a much stronger human resources and institutional base.

Sectoral emphasis (not in order of importance or priority) will be on private sector production; agricultural development; education; health and population; and housing and related infrastructure. Efforts in each of these five sectors support both growth and equity objectives to varying degrees, and are therefore not classified as falling under either a growth or an equity mantle. In our judgment, assistance in these sectors will have the greatest impact on helping Honduras to reach the short- and long-term goals. They are the sectors through which the situation of the poor can be improved most directly. Both the Mission and the GOH have substantial interest in improving their functioning and effectiveness to promote long term development and equity. They are areas in which both we and the GOH have gained significant expertise through our ongoing assistance program. They are logical areas on which to concentrate attention both in terms of Honduras' long term development needs and the types of assistance available from other sources. Finally, the interrelationships between these sectors are such as to require, insofar as practical considerations allow, a simultaneous attack on all of them.

A total of \$947.1 million in USG assistance is proposed to support this strategy. A breakdown is included in the resource requirements tables at the end of this document. ESF balance of payments assistance of \$180 million is proposed for FY 1985 through FY 1987 to support the stabilization program. It is proposed that Development Assistance funds, ESF (starting in FY 1988), HG loans, and PL-480 Title I and II resources totalling \$737.1 million be provided for the long-term development program. ESF funds which support the long-term development program are programmed for both balance of payments support and development projects. Their use as balance of payments support will be linked to the accomplishment of specific policy reforms which are needed to ensure the success of AID supported long term development projects. In addition, it is proposed that \$30 million of ESF funds be used for a Trade Credit Insurance Program, as recommended by the National Bipartisan Commission on Central America (NBCCA), to insure payment to U.S. banks for lines of credit they extend to Honduran importers.

Balance of payments support for the stabilization effort are programmed at a high and constant level during the first three years of the CDSS period and then progressively decline over the last three years. The heavier emphasis on balance of payments support in the earlier years reflects both the GOH's and our own short-term priority for stabilizing the economy and minimizing social

unrest. The funds programmed for long-term development programs increase steadily over the planning period. Yearly adjustments in the relative magnitude of resources destined for each program area (stabilization, sectoral policy reforms, and long-term development) will be made based on progress in achieving agreed on program objectives. For example, should a satisfactory economic stabilization program not be agreed upon, or not fully implemented, funds now destined for that program will be used for long-term development program. Alternatively, if a well conceived and well implemented stabilization program has not produced the desired results within the projected time, it may be necessary to continue support in this area for a longer period than projected. In comparison to historical levels, a much higher proportion of grant financing is requested. Honduras' status as the region's second poorest country, and the strong emphasis on technical assistance and major economic policy changes in the long-term development strategy justify a higher portion of our assistance through grant rather than loan financing. The program as a whole is neither a high-risk nor a low-risk venture. There are some potential pitfalls, and realistically we must be prepared to take moderate risks in view of the importance of Honduras to U.S. strategic interests.

B. Economic Stabilization Program

1. Macroeconomic Situation

For the past four years, Honduras has had unusually large budget and the balance of payments deficits. The deficits have been financed mainly through domestic and external borrowing. A combination of external borrowing, restrictions on imports, and a recent policy change allowing importer-financed goods to enter the country have helped to relieve short-run pressure on the balance of payments.

To address its macroeconomic problems, the GOH has obtained assistance from the International Monetary Fund twice over the last five years. An Extended Fund Facility Agreement was signed in 1979 and a Stand-by Agreement was arranged for the 14 month period ending in December 1983. The duration and magnitude of the balance of payments and budget problems, and less than adequate GOH action on implementing policies to contain them, resulted in incomplete compliance with both agreements.

The Mission believes that a new IMF agreement is key to the implementation of a stabilization strategy. The GOH must undertake significant policy reforms and administrative improvements to curb continuing fiscal and balance of payments disequilibria. The fiscal deficit for the Central Government for 1984 is projected at \$325 million, which is over 10% of GDP, and is likely to continue at a high level during the 1985 election year. If restrictions on imports were lifted, the balance of payments deficit in 1984 would increase by a projected \$183 million (imports gap). Full financing of deficits of this magnitude is not an option. Foreign banks are unlikely to help in view of the country's unpaid debt and the region's political instability. Domestic borrowing cannot substitute for foreign borrowing to meet foreign exchange

requirements. Moreover, domestic borrowing from the banking system to meet domestic budget requirements would add to a stock of monetary assets that is already far in excess of the amount consistent with containing pressure on prices and the import bill. The issues to be resolved in negotiating a new Stand-by are the size of the fiscal deficit, the monetary overhang created by bank financing of past fiscal deficits, and the use of import restrictions in lieu of exchange rate adjustment to contain the balance of payments situation. Resolving these issues will undoubtedly require stringent limits on overall credit creation, the budget deficit, and credit to the public sector. Some action on the exchange rate will also be needed.

The successful conclusion of a new IMF agreement will be difficult. The lack of compliance with the past two agreements has made the Fund wary of the Honduran government's willingness and ability to successfully implement a rigorous stabilization program. Past drawings on IMF resources have placed IMF holdings of Lempiras well above 400% of Honduras' IMF quota, thus limiting the amount that the GOH could draw under a new agreement. Public reaction to strenuous adjustment measures in other Latin American countries has heightened concern within the governing Liberal Party that major policy reforms will lead to its defeat in the 1985 Presidential elections. The Suazo Administration's lack of internal policy consensus on economic policy, particularly on the exchange rate issue, may also make reaching an agreement difficult.

2. Strategy

To assist Honduras in adopting and implementing a stabilization program which will lay the basis for achieving self-sustaining economic growth, the Mission, through the Joint Economic Working Group (JEWG), will continue to help the GOH to develop an appropriate set of macroeconomic policies. The JEWG is evaluating different combinations of fiscal measures, non-bank deficit financing, and more flexible foreign exchange regulations. The design of a preliminary adjustment program is nearing completion, and its approval and initial steps towards its implementation are expected shortly. At present, the plan calls for a combination of tax increases, better control of spending, and a reduction of the money supply through increased bank reserve requirements. The Mission expects the measures adopted to be sufficient to allow some of the ESF funds now obligated to be disbursed, and to provide a basis for obligating the ESF funds included in our FY 1984 OYB. The measures should also facilitate negotiation of a new Stand-by Arrangement with the IMF during mid-1984. If an IMF agreement is reached, AID will support its implementation by providing continued technical assistance and ESF balance of payments support linked to progress in implementing the agreement and accomplishing specific reforms. Once the Fund agreement is in place, the GOH will concentrate on completing negotiations with the IBRD for a Structural Adjustment Loan of between \$40 and \$50 million. Presumably, this will require policy reforms in the industrial development, external debt management, and public sector investment areas, inter alia. As in the case of the Fund agreement, the implementation of reforms adopted by the GOH would be supported by ESF balance of payments assistance.

Although we believe that agreement on a new Stand-by will eventually be reached, it is possible that negotiations will not be concluded soon. Also, it is possible that, if the agreements are reached, the GOH for one reason or another, may fail to fully implement them. Finally, it is also possible that, despite full compliance by the GOH, the tandem objectives of stabilizing the economy, and laying the bases for a resurgence in long-term growth may not be realized. Several options will be held open for dealing with these possible outcomes. If the GOH fails to reach agreement with the IMF on a new Stand-by, and/or with the IBRD on a Structural Adjustment Loan, the Mission will continue to work with the GOH on development of a stabilization program. If an acceptable program is not reached, or if the program agreed to with AID, the IMF, and the IBRD goes badly out of kilter and efforts to develop a new one hold little promise of success, some or all of the ESF funds planned for balance of payments support may be projectized or linked to specific policy reforms in sectors where AID is supporting long-term development efforts. In the early years of the CDSS period, projectized ESF would be used to support the "first offensive against unemployment." Sectoral policy agendas are discussed in the context of each sectoral development strategy, which is part of the long-term development program.

3. "First Offensive" against Unemployment

The "first offensive" will be aimed at reducing the social problems building in the country's primary and secondary cities. Up to 40,000 person years of employment would be generated from 1985 through 1987. This would amount to one person year of employment for every six presently unemployed labor force members. Water systems and home connections, electric energy distribution systems and service drops, and other urban infrastructure improvements in marginal communities of Honduras' major cities would be constructed. The program would be negotiated with the Ministry of Finance, and, assuming agreement is reached, the improvements would be carried out by the Autonomous Water and Sewer Authority, the Electric Energy Company, the Ministry of Public Works, and the Autonomous Municipal Bank. They would be selected on the basis of criteria which emphasize high labor intensity in the construction process, highest financial return (if they generate revenues), greatest utilization of domestically produced materials, and reasonable geographical distribution in relation to perceived unemployment levels. Design and construction would be carried out to the maximum degree feasible through individual contractors and private construction firms. The construction industry is now operating at about one-third of capacity and could quickly take on the additional work. In addition, an effort will be made to attract some of the unemployed into reforestation and water conservation efforts in rural areas through a California Conservation Corps-type program. The Mission anticipates financing the "first offensive" with a combination of ESF, to the extent that imported goods and technical services are needed to carry out the improvements, with the bulk of the financing coming from local currency generations. However, if ESF funds are not disbursed in support of an economic stabilization program, the "first offensive" would be wholly financed with ESF through project assistance.

C. Long-term Development Program

1. Overview

Short-term unemployment abatement must be replaced by increased permanent employment and improved equity over the CDSS period. Employment is the sine qua non for individuals to have a sense of self worth and for the maintenance of social harmony. To develop full-time employment for 90% of the expected labor force in 1990, approximately 400,000 new jobs would be needed - roughly a 40% increase in total employment over 1983. Given the situation in the region, Honduras would do well to maintain its present level of 20% unemployment over the CDSS period. This will require creation of approximately 250,000 new jobs. The Mission believes this goal is more realistic and could be achieved. Reaching even this goal will require a gross investment of over \$1.5 billion in productive activities over the CDSS period. On an annual basis, this would require an investment rate about 25% higher than the 1983 level.

The programs proposed in this CDSS may create as many as 50,000 jobs. The remainder will have to be generated from private domestic and foreign investment. Perhaps as much as half of the \$1.5 billion of investment needed will have to come from direct and guaranteed USG resources. These resources would come through institutions such as Eximbank, OPIC, CCC, CABEI, and the Trade Credit Insurance Program. The NBCCA recommended the expanded availability in OPIC insurance, and the formation of a privately owned venture capital company for Central America. Implementation of these recommendations are crucial to achievement of the employment goal. They have the Mission's full support, and we are willing to use ESF resources to support the Trade Credit Insurance Program, if necessary.

With its present limited domestic market and resources, Honduras' long-term growth depends in good measure on its ability to increase its exports and apply its capital inflows to modernizing production operations and making them more efficient. Agriculture and non-agricultural private sector production are the areas in which the greatest growth and employment gains can be expected. Efforts aimed at increasing production and employment will be concentrated in these areas during the CDSS period. These efforts will be complemented by programs in education, and health and family planning which will increase living standards, equity, and the ability of the labor force to contribute to achieving and maintaining increased production levels. Improved family planning services will also help to reduce the investment needed in productive activities in future years by eventually lowering the number of new labor force entrants. Production of an increased number of standard housing units will both provide additional employment and improve family health standards, further complementing progress in the other sectors. The sum of the proposed efforts in these five priority areas constitutes a major push for employment and equity.

2. Private Sector Production

The Mission's CBI Implementation Plan analyzed the possibilities for increasing private sector production, and concluded that the export and small business areas held high potential for increasing production and employment.

a. Structure of Export and Small Business Operations

Honduras' principal exports - bananas, coffee, lumber, meat, sugar, shrimp and lobster, and mineral ores - are commodities which are sold mainly outside the Central American Common Market (CACM). These traditional exports account for about 77% of export earnings. Marketing of these exports is controlled by a relative handful of domestic firms and three U.S. transnationals, which export bananas and mineral ores. Over the years, Honduras' producers and marketers have found that producing and selling commodities is more profitable than investing in processing facilities.

Manufactures account for less than 15% of total exports. Manufactured exports are almost all sold in the Central American Common Market (CACM). The producers of manufactured exports have become wealthy under a protectionist mantle they will not willingly relinquish. Many of their exports would not be produced today had that mantle not existed. There are strong business and personal ties between the country's largest industrial firms and the largest banks, and industrial investments tend to be tightly held among a relatively small group of investors.

The structure described above accounts for a sizable share of the country's production and the bulk of its exports. However, most Honduran businesses are neither exporters of traditional products nor large industrial firms. Over 95% are small-scale operations, most of which produce for the domestic market. Small enterprises use capital and credit relatively efficiently, and they are the major employers of workers with minimal formal education and training. They provide essential services to our target group in both urban and rural areas. In general, potential new exporters lack an understanding of international markets and international trade practices. Furthermore, the GOH does not provide the right kind of incentives to induce them to risk their capital in export operations. Both exporters and small producers lack access to credit sources, and have a limited understanding of administration, marketing, finance, and appropriate productive technologies.

b. Export Development Strategy

To achieve a major increase in exports to outside the CACM, a transformation of the country's productive apparatus will have to take place. First, an export mentality must be created in both the public and private sectors. Second, a policy environment must be created which favors export development and helps the private sector to take advantage of that climate immediately and over the longer run. Among necessary policy changes are improved incentives for investment in export production operations, enabling legislation for private free zones, elimination of bonding requirements for drawback

industries, an expedited process for opening businesses, and a reduction of red tape for normal exporting transactions. Third, the private sector's capability to identify and analyze potential market opportunities, and link up with outside firms in new productive and marketing arrangements, must be developed. Finally, services, such as financing, transportation, and skills and management training, must be made more accessible to exporters and their costs must be lowered.

With AID assistance, the Honduran private sector has recently created two new organizations - the Entrepreneurial Research and Development Foundation (FIDE) and the Agricultural Exporters Federation (FEDPROEXAH) - to assist individual entrepreneurs and producers' associations to analyze and exploit new export markets. They will be helped in their endeavours through a five year Export Development and Services Project (522-0207), which is planned for authorization in FY 1984. The non-traditional exports developed through the Project mainly will consist of fresh and processed agricultural and seafood products, furniture and other secondary wood products, clothing, and assembly of electronic goods. These efforts will be directly supported by the many CBI activities sponsored by the Department of Commerce, AID and other actors in the CBI process. Non-traditional exports will be increased from a 1982 level of about \$130 million to \$300 million per year by 1989, and about 20,000 new jobs, or 8% of the goal, will be created directly and indirectly through the project. Local currency generations will be made available for credit as needed to ensure that achievement of the employment and export sales goals is not frustrated by a lack of domestic commercial credit. Depending on progress and market conditions, initiation of a second export project late in the CDSS period may be needed.

c. Small Business Development Strategy

The Mission's strategy for assisting small-scale enterprises will be to progressively open financial and technical assistance channels to smaller and smaller businesses, starting with those firms which, while commercially viable, are unable to increase production due to limited technical or management knowledge and experience, and lack of access to adequate financing. Our efforts to develop more accessible sources of financial and technical assistance for small businesses will begin with the FY 1984 Small Business Development Project (522-0205), which is now authorized. A new small business-oriented finance company and a PVO-based technical assistance system for small businesses will be developed through this project. The credit resources will come from local currency generations, and the technical assistance system will be developed with DA funds and financed with the interest rate differential on the credit funds. It is expected that about 1,000 jobs will be created through the project by 1987. Additional assistance for small businesses, especially those located in rural areas, will become available through the Alternative Credit Channels Project described in the Agricultural Sector Strategy. Those small businesses which are interested in and capable of entering export markets also will be assisted through the Export Development and Services Project.

3. Agriculture and Rural Development

a. Agricultural Sector Structure

There are approximately 450,000 families living in rural areas, of which approximately 300,000 derive their incomes primarily from agricultural production. Over 60% of the economically active population is employed in agricultural and mining. Approximately 30% of the GDP is directly attributable to agriculture. Agriculture has provided and will provide a living, however meager, for the majority of the rural poor in Honduras.

Agricultural production in Honduras is characterized by low productivity, stagnant production of basic grains, and a narrow export commodity base highly dependent upon the vagaries of the international market. Over the past few years, weak demand and prices for the principal export crops, coupled with increased input costs and natural disasters, have reduced both foreign exchange earnings and net farm incomes. Declining per capita production of basic grains (except for rice) appears to be due to a combination of high production costs, rainfall variations, plant diseases and pests, income and marketing constraints, and possibly a higher percentage of marketable production due to improved post-harvest handling. Crop production is difficult and depends largely on highly fluctuating rainfall and natural control of pests and diseases. In the case of livestock, low nutritional intake levels during dry periods depress birth rates, milk production and weight gain.

There are several major constraints to increasing incomes from agriculture. The structure of land tenancy and lack of a land market have led to high concentrations of farm families in areas of low land quality. Only a third of the land suitable for annual and perennial crops is used for that purpose. About 25% of rural residents are landless or nearly so, and two-thirds of farm units are 3.5 hectares or less, which is an uneconomical size for production of many crops. Lack of access to, and tenure on, good quality land is a major constraint to increasing income for most farmers.

Production and technology levels are low, and marketing systems poorly developed. The use of improved seed, fertilizers, appropriate farming practices, and farm machinery is minimal. Indicators of technology intensity are among the lowest in Central America. The limited technical knowledge and organizational and managerial skills of agricultural producers are a strong constraint to improving production efficiency. Low membership levels in poorly managed farmer organizations and agricultural cooperatives have limited the effectiveness of these organizations, which have made large investments in input, credit and marketing operations. Although some 14% of peasants have obtained land through the agrarian reform program, assistance in making that land productive has not been provided to most of them.

Both input and product marketing structures, except for traditional export crops, are poorly developed, and transportation is often erratic and expensive. The country has limited processing capability and, despite

improvements over the last few years, post-harvest losses are still too high. Honduras' potential for rapidly increasing non-traditional exports is constrained by the complexity of the export development process, and the fact that the Honduran private sector has not been particularly aggressive about exporting.

Access to credit is also a major constraint to agricultural sector development. It is estimated that only 10% of the country's farmers regularly obtain credit from commercial banks and the National Agricultural Development Bank (BANADESA). The lack of land titles and mortgageable assets hampers small farmers' abilities to secure credit and invest in on-farm infrastructure. In real terms, credit supplied to the agricultural sector declined steadily from 1979 through 1982, and has only recently turned upward. Present real levels are now approximately what they were a decade ago.

While some investment has been made in productive infrastructure such as roads, drainage, flood control, irrigation, and soil and water conservation, and in providing access to, enhancing and protecting the land resource base, it has not been enough. The lack of infrastructure is also a major constraint to development of the sector.

There are a number of reasons why continued efforts should be made to overcome these constraints and attempt to raise incomes among the large number of low income families who depend on agriculture for a living. First, the GOH has adopted and maintained a generally favorable policy framework toward the sector based primarily on private initiative and market prices. Second, sufficient productive land is available. Third, the recent passage of the CBI legislation has opened a number of important market opportunities. Fourth, it has been demonstrated that productivity can be rapidly increased for many products when the required input financing, training and market access are provided to farmers. Finally, farmers have shown that they can maintain and enhance the productive capability of their land through proper farming methods, and are quick to do so when shown appropriate land use technologies.

b. Agricultural Development Strategy

Due to the high percentage of Hondurans who derive their income from agriculture and the country's large potential as an agricultural producer, a high percentage of AID's long-term development program has been and will continue to be concentrated on improving the functioning of the sector. Our target group includes traditional subsistence farmers, small- and medium-sized commercial operators, and the landless. The strategy will be to help the commercially oriented farmers move progressively into higher value crops for domestic and export markets and processors. This should increase labor demand for the landless and create expanded market opportunities for traditional farmers who produce basic grains.

The Mission is well positioned to assist Honduras in overcoming its major constraints in the agricultural sector. Over the last few years, we have jointly begun addressing each of them, and we are increasingly seeing signs of

progress. We and the GOH have learned a lot in the process, and we intend to apply our knowledge carefully to ensure continued and increasing target group impact. The areas in which we are working, progress to date, and proposed activities during the CDSS period are described below.

i. Land Access and Tenure

The GOH's principal tool for providing access to agricultural land over the last twenty years has been the agrarian reform program. Some 42,000 families have received land under the program and the Agrarian Reform Institute has applications from many thousands of additional families. In 1982, the Suazo Administration, in a significant policy change, initiated, with AID assistance, an effort to improve security of tenure on national lands, where most of our target group lives. At the end of 1983, 8,000 of the country's approximately 230,000 farm units had fee simple titles, and 4,500 of those were issued during 1983 under the Small Farmer Titling Project (522-0173). In 1983, the GOH and AID agreed that another channel for improving access to land was needed, to provide an alternative to INA's expropriation and distribution of land under the Agrarian Reform Law. A pilot project financed with local currency generations was initiated to facilitate private purchases of agricultural land by providing mortgage financing. Each of these programs will help some percentage of the target group to obtain secure tenancy. However, none of them is a sufficient answer to the problem and additional effort is needed.

During the CDSS period, we will continue with the titling project, and finance a follow-on effort. It is still too early to judge the results of the pilot mortgage financing program. If the results justify a broader effort, we will help the GOH to stimulate the private agricultural land market by increasing mortgage financing through private channels. Finally, we will evaluate with the Agrarian Reform Institute (INA) the feasibility of a homesteading program to cover those cases that cannot be resolved through the other channels. If feasible, AID support for implementation will be provided. INA will play a major role in all of these programs except for private land sales. Its administrative capability is heavily taxed with its present load and it needs to improve its management procedures and organization. A top priority is attending to the many pending applications for land under the Agrarian Reform Law. INA is now beginning to reorganize itself based on recommendations from an AID-financed study. We expect to continue to help INA improve its institutional capability for the next few years.

ii. Technology, Marketing, and Production Assistance

The Mission's experience indicates that these constraints are best addressed on a product-specific basis, and that efforts are most successful when a private producers' association plays the major role in providing assistance to the producers. Efforts now underway to improve small farmer production of two traditional export products - coffee and beef - through the Small Farmer Coffee Improvement (522-0176) and Small Farmer Livestock (522-0209) Projects. Both of these products have reasonably stable, long-term marketing prospects.

A crop diversification component will be added to the highly successful coffee project early in the CDSS period. Both projects are long term efforts that will continue throughout the CDSS period.

Honduras has a significant opportunity to increase its export earnings from a third traditional product - lumber. At present, lumber is exported almost exclusively by an autonomous GOH corporation - COHDEFOR. The Presidential Agricultural Task Force recommended that marketing of lumber be returned to the private sector and that COHDEFOR concentrate on regulation of the lumber industry and long-range forest management. We will pursue the twin objectives of increasing the country's income from lumber sales and establishing more appropriate roles for the public and private sectors through a Forestry Development Project planned for initiation in FY 1985. The project will focus on implementing specific policy changes recommended by the Presidential Agricultural Task Force, and putting a management plan into effect in a major forest district.

During the CDSS period we plan to expand the product-specific, private sector led approach and apply it to export of non-traditional agricultural products. This will require a highly specialized and intensive effort to improve the capability of small landholders and private firms in the production, marketing, and processing of a small number of carefully selected commodities with good marketing prospects. The effort will be carried out through private producers' associations and a private agricultural research institute whose principal focus will be on non-traditional commodities. AID assistance will be provided through the Export Development and Services Project mentioned above and an Agricultural Research Project (522-0249), both of which are planned for authorization in FY 1984. These projects call for major inputs from U.S. PVO's, business firms and individuals, especially in the technology transfer, marketing, and research areas. It is the right time to initiate a program to increase non-traditional agricultural exports, as Honduras' recent designation as a CBI beneficiary country has greatly increased their potential profitability, and strong U.S. and third country buyer and investor interest is already apparent.

While our main focus during the CDSS period will be on exports, we will continue to help small farmers who produce mainly for the domestic market in order to achieve minimum food security for as many low income families in the sector as possible. Appropriate production technologies, improved farming practices, and land conservation techniques are now being introduced to small farmers through the Rural Technologies (522-0157) and Natural Resources Management (522-0168) Projects. The benefitting farmers produce mainly for domestic consumption, although a few export crops are being produced on a small scale through the Rural Technologies Project. After slow starts, implementation of both projects is proceeding well, and they are having a very positive effect on the incomes of benefitting small farmers. They will continue well into the CDSS period, and follow-on projects are planned. The research institute mentioned above will carry out some research on basic grains and an improved technology transfer system will be developed to further enhance the effectiveness of both of the above projects. Finally, to ensure

that income gains are not diminished by temporary overproduction or low prices, we will continue to finance technical assistance to the GOH's Grains Marketing Institute (IHMA) to help it improve its marketing policies and operations, and initiate an effort to improve the highly inefficient domestic food marketing system during the CDSS period.

iii. Credit

At present, the credit constraint is being addressed through resource transfers and technical assistance aimed at strengthening non-bank institutions that could play a stronger role in making credit accessible to the target group. Credit is being provided to small farmers with local currency generations through model cooperatives under the Agricultural Sector II Project (522-0150), and to small coffee producers (Small Farmer Coffee Improvement, 522-0176) through private banks and the National Agricultural Development Bank (BANADESA). The capability of the regional cooperatives to serve as credit channels is being strengthened under the ANACH Consolidation OPG (522-0203), and the rural credit union system is being improved through an OPG to the Federation of Credit Unions (522-0177). However, these programs are very limited in scale. Even taking into account the credit provided by BANADESA with its own and IFI resources, not more than 10% of our target group has regular access to credit.

A large increase in credit resources will be needed to increase small farm production efficiency and reach the increased income goal by 1990. BANADESA will provide some of it with resources it expects to obtain from the IDB and the World Bank. However, BANADESA has recently stiffened its lending criteria, and will probably continue to do so to ensure its financial viability. It is likely to continue to be an inaccessible lending source for most of the target group. We will attempt to develop several accessible sources through an Alternative Credit Channels Project planned for authorization in FY 1985. The project will attempt to reach small agricultural producers and rural businesses through a variety of non-bank financial institutions and PVO's. These will include PVO's with successful credit management experience, those credit unions and regional cooperatives that are both market-oriented and well managed, and new finance companies. AID resources will finance technical assistance aimed at strengthening the management and technical assistance delivery capability of these institutions. Credit resources will come from both ESF and PL-480 local currency generations. Special emphasis will be placed on continuing to help the ANACH regional cooperatives and the model cooperatives to become strong, well managed, multi-purpose service organizations. The alternative channels would also provide agricultural land mortgage financing to increase access to land.

iv. Productive Infrastructure

Productive infrastructure and market access are being improved under several ongoing projects. Roads are being built and upgraded under the Rural Trails and Access Roads Project (522-0164), local markets and slaughterhouses have

been developed under the concluding Municipal Development Project (522-0165), and irrigation systems are being developed through the Water Resources Activity of the PL-480 Title I/III program.

During the CDSS period, we will target our investments in rural infrastructure to those elements necessary to support the above productive activities. The roads project is being successful in integrating large numbers of small farmers into the market economy, and a follow-on project will be needed during the CDSS period. A major project to develop small-scale irrigation systems will be initiated as soon as obligation of new funds is warranted based on the results of the present PL-480 Title III activity. This may take place as early as 1985. A rural electrification project is planned to provide energy to those areas where agricultural and agro-industrial development is constrained by lack of electricity, and low financial returns require highly concessional financing.

v. Human Resources

The human resources base for managing the sector's public institutions has been improved through the Agricultural Sector II Project (522-0150). The major human resources development activity under that project has been development of the National University's Atlantic Coast campus (CURLA) as an agricultural university. Basic facilities and U.S. training of 240 instructors will be completed within the next year. However, continued efforts will be needed to establish a standard of excellence in utilizing the human and physical infrastructure developed to date. This can best be accomplished by the involvement of U.S. universities in staff development and teaching. To ensure maximum benefit to the country, the present open admissions policy and student influence over university decisions would have to be curtailed, so that attention could be concentrated on achieving academic excellence and training the most capable and serious students. The link to U.S. universities and the policy objectives will be pursued through a planned FY 1985 Agricultural Education Project. An attempt will also be made to link the agricultural research foundation with CURLA and other agricultural education programs in Honduras.

vi. Development Channels

The ongoing projects have been started at different times, are being carried out at present in different areas of the country by different public and private institutions, and are benefitting different members of our target group. The GOH is the principal immediate recipient of assistance for the sector, and will continue in this role for some time. However, some 15 PVO's are either direct recipients of AID funds and/or are implementing activities financed under one or more bilateral projects. They act as the glue that binds the diverse ongoing efforts together at the local level and ensures that the assistance gets to the target group in a coordinated fashion. During the CDSS period, private businesses, including cooperatives, and PVO's will play an increasing role in implementing AID-financed programs. These organizations are best equipped to expand successful programs, integrate them with new

efforts, and maximize their benefits to the target group. At present, the PVO and cooperative structures are not broad or strong enough to carry this load. They will be strengthened during the CDSS period (see Section IV. C).

vii. Development Policies

Improved policies are needed to ensure the success of specific programs and the strategy as a whole. The legal basis for defining riparian rights and providing incentives for the establishment of private irrigation systems needs to be developed. Articles in the forestry laws which have caused massive disinvestment in the sector over the last 10 years need to be modified. The Forestry Corporation needs to shift its focus from state control of marketing to regulation of the forestry sector. The opening of Central Bank discount facilities to responsible non-bank lenders, where such lenders accept a reasonable degree of regulation from the Central Bank, would help to achieve broader target group access to credit. As well, specific regulations and policies which limit the recoverability of loans to small agricultural sector enterprises need to be changed. Legislation to allow for bonded warehouses and enforceable crop liens is needed. Finally, rationalization of basic grains support pricing is needed to minimize the cost of the system to the state and improve market functioning. These points make up our agricultural policy agenda with the GOH. Assistance to the GOH in analyzing them and other needed reforms will be provided through a Policy Analysis/Technical Support Project starting in FY 1984 or FY 1985. Necessary changes in government policies which serve as disincentives to production and investment will be addressed, as appropriate, through linkage to balance of payments support and development projects.

viii. Expected Results

This strategy fully responds to the NBCCA's recommendations to accelerate agricultural development, broaden land ownership, provide financial resources to supplement credit and investment programs, and increase economic support for cooperatives. With the proposed policy reforms and implementation of the above projects, we expect the following changes to take place by the end of 1990. Over one third of all small farms in the country will have fee simple titles, and the institutional base for completing the title issuance process by the year 2000 will be in place. Small farmers with access to land will rise from 75% at present to over 85%. Credit will be accessible to at least 25% of the country's small farmers through banks and non-bank financial institutions. Improvement in basic grains farming techniques will have been carried out through dissemination of appropriate technologies and farming methods. About \$100 million per year of the \$170 million per year target for additional exports will be non-traditional agricultural products, and commercially oriented small landholders will be achieving a great share of that market. The efficiency of domestic production and marketing will have been increased, with traditional small farmers achieving some of the resulting income gains. Total net farm income will be at least \$40 million higher in 1990 - an average increase of \$175 per farm unit over the 1980 level of \$765. Small landholders will increase their incomes from a 1980 level of \$200 to an

average of \$245 in real terms. Even with the anticipated progress in increasing smallholder incomes, a large number of families will not reach the level needed to provide minimum food security during the CDSS period. Donations of PL-480 Title II at approximately present levels will continue to be necessary for the nutritionally most-at-risk population. Occasional extraordinary Title II contributions may be needed when emergency situations, such as crop failures or natural disasters, occur.

4. Education and Skills Training

a. Status

The Honduran education system is not building the human resource base needed to increase the productivity of the labor force and provide a reasonable return on the country's sizable investments in its educational institutions. It is weak from top to bottom. The public education system is beset by the rapid expansion of the school age population; perennially short of resources; lacking policy orientation; weak in planning; short of adequately trained teachers, administrators, textbooks and materials; and constantly under pressure from highly political teachers' unions. Some 87% of primary school age children are enrolled, and 30% of secondary school age children. About 5% of people in the 20 to 29 year age group attend a domestic university. Overall, of 100 first grade entrants, 28 finish the sixth grade, 14 finish secondary school (one third of secondary students go to private schools), and one obtains a university degree.

The average educational attainment is under two years in rural areas where, because of drop-out and repeater rates, it takes 18-19 years of classroom time to produce one sixth grade graduate. Rural areas have 65% of the primary school-aged population and an enrollment of 80%. By comparison, enrollment in urban areas is 97% of school age children. Of the country's 5,035 public schools in rural areas, less than half offer six grades. Approximately 85% of urban and 25% of rural classrooms have some basic texts on hand, but many of them are worn out while others are simply not used because teachers continue to use traditional blackboard and rote memory exercises.

Non-formal education services are not filling the gaps left by the formal education system. Adult literacy in rural areas is low and had been neglected until the recent inauguration of a rural adult literacy campaign by the Ministry of Education. Two recent studies of Honduran enterprises show that lack of management and skills training is a major constraint to the improved efficiency of private productive activities, and the effectiveness of public and private skills and management training programs is limited by poor quality instruction and lack of relevance of their programs to the productive technologies used by Honduran firms.

b. Strategy

Improving rural primary education has been a major GOH objective over the last 30 years, and the Mission's top human resources priority in recent years. Primary education is so basic to improved living standards for the poor that

efforts to improve it must continue in spite of budgetary and other problems. And progress has been made. Primary school enrollment increased from 51% in 1961 to the present 87% level. AID played a role in this success through several classroom construction and teacher training projects in the 70's.

During the CDSS period, USAID/H will assist the Ministry of Education to come as close as possible to universal enrollment of primary school-aged children. The NBCCA noted that providing universal access to primary education is a realistic objective for the 1980's for the Central American countries. To reach the target of 93% enrollment by 1990 and simultaneously improve quality, the following will be needed: nearly universal access to six years of education and an overall enrollment of 85% in rural areas; acceleration of the certification of the remaining uncertified teachers; printing and distribution of books and other instructional materials to all public primary schools; and continued improvement in the Ministry's administrative, data gathering, planning, and resource allocation methods.

AID assistance is already being provided to address some of these needs. Construction, repair, and maintenance of rural classrooms, and in-service teacher training are being carried out under the Rural Primary Education Project (522-0167) - the only active, donor-supported, rural school construction program in Honduras. PVO-administered community feeding programs, using PL-480 Title II commodities are improving nutrition of the school aged population, and are being used as a means of improving nutrition curricula for rural schools. The lack of books and educational materials in rural schools continues to retard efforts to improve educational quality. A recent World Bank study showed that the degree of literacy and numeracy attained through public education systems correlates closely with the availability of textbooks and educational materials. Starting in FY 1985, we plan to provide financing for a major textbook production and distribution program, and teacher orientation in the use of the texts.

The enrollment and quality improvement targets are achievable. The Mission estimates that \$25 million for about 5,500 classrooms, \$30 million for texts, \$5 million for teacher training, and \$5 million for administrative improvements would do it. Of this \$65 million needed during the next six years, we plan to provide up to \$50 million. The remainder, mainly for classroom construction, will require other donor support. The Mission will encourage the other donors, especially the IDB, to help complete the job.

We recognize that the recurrent costs of reaching the goal will be high. Budget increases of 10% or more a year may be needed. The possibility of resolving the recurrent cost problem may well depend on the outcome of our ongoing dialogue with the Ministry of Education regarding GOH policy on relative per student expenditures for primary, secondary, and university education. At present, the GOH spends on university level instruction more than ten times what it spends per student year on primary school education. University students, most of whom work full time, pay only minor registration fees. Other alternatives, e.g., community contributions for rural teachers' salaries and school maintenance, and minimum charges for textbooks and materials, will also be examined in detail.

As reaching the goal of near universal primary education grows closer, a major bottleneck is starting to build at the secondary school entry level. In early 1984, there was a near riot in Tegucigalpa as parents desperate to get their children registered for secondary programs flooded the schools and the Ministry of Education. Many were turned away by the schools for lack of space. It is both a political and an educational imperative that access to secondary education be improved. The GOH is increasingly facing a situation where it will have to accept full responsibility for providing public secondary education. The Mission will encourage the other IFI's to finance improvement of the secondary education system. However, absent such assistance, the Mission would propose AID funding for a secondary education improvement program near the end of the CDSS period.

Success in reaching employment objectives will depend in part on a better trained work force. An improved in-country capacity to provide modern management and skills development will be developed through two OPG's that will be authorized in FY 1984. Under one, the American Management Association (AMA) will become affiliated with a Honduran PVO - the Associated Managers and Entrepreneurs of Honduras (GEMAH) - and introduce AMA's excellent management development program into the country. Under the other, an effort will be made to introduce skills certification procedures for blue collar workers, and to initiate skills training programs in private companies under the auspices of a recently created Advisory Council on Human Resources Development (CADERH). These programs will be expanded throughout the CDSS period as needed to further facilitate reaching our employment goals.

The above projects will mainly improve the training of the managers and workers who are presently employed or who find employment during the CDSS period. More emphasis is needed on building for the future. The Mission will explore with the San Pedro Sula (SPS) University, a small and struggling private college in the country's industrial capital, the possibility of developing a joint program with a major U.S. university. This will provide a political counterweight to the traditionally leftist dominated National University as well as a quality center of learning in the dynamic north coast. The curricular emphasis would be in the skills areas most needed for improving Honduras' competitiveness in world markets: management, finance, international marketing, business law, and the physical and agricultural sciences. The U.S. university could also act as a "brain trust" for Honduran industry through consulting work and research. If an agreement is reached, the Mission would assist the SPS University with development of its curriculum, teaching staff, and physical plant. USIS supports this concept and could provide US professors and training for staff development.

The Ministry's present modest effort in adult literacy will continue to be implemented. The Mission expects the scope of that effort to be enlarged with the assistance recommended by the NBCCA, and may contribute some local currency generations to support the program.

5. Health and Family Planning

a. Health

i. Status

Poor health status continues to limit the productivity and earnings of our target group, and lessen their general well-being. Hondurans suffer from the same health problems prevalent throughout the developing world. However, conditions here are worse than in almost all other Latin American countries. Malnutrition is estimated to affect 70% of the population. Diarrhea is the number one cause of morbidity in all ages, and of infant mortality.

Respiratory and vector-borne diseases, malaria in particular, are also principal causes of morbidity. These factors and others have resulted in an infant mortality rate of 87 per 1,000 live births and a life of expectancy of 57 years.

Unhygienic environmental conditions and poverty complicate the ability of Honduras to respond to its health problems. Although gains have been made in the installation of drinking water systems in both rural and urban areas, better than 45% of the people, almost all of them in our target group, still do not have reasonable access to potable water. As a result, active disease transmission persists, despite the Ministry of Health's (MOH) immunization and vector control programs. Preventable health problems become chronic because of unsanitary home environments, limited access to health care, lack of health education, and lack of the knowledge and funds needed to improve them.

To address these problems, the MOH has established a pyramidal health care system with a large number of volunteer community health workers and auxiliary nurses at the base, and a few well-equipped hospitals at the top. AID has supported MOH programs to improve community level care starting in the 1970's. In 1980, the GOH, with AID support, initiated efforts to improve health system planning and management and rural water and sanitation conditions. As well, appropriate technologies, such as Oral Rehydration Therapy (ORT), vector control, and expanded immunization have since been adopted by the MOH. The IDB has assisted the MOH to strengthen its curative, hospital-based health system, and the number of hospitals and hospital beds has dramatically increased over the last decade. As a result of these efforts, about 60% of all Hondurans now have reasonable access to basic medical attention.

ii. Health Strategy

In the mid 1970's, the Mission was instrumental in obtaining a major policy change which led to a significant shift in emphasis from hospital-based curative care towards preventive medicine and practice. When the Ministry of Health (MOH) adopted the policy of concentrating on primary health care, AID agreed to support it as the most cost-effective way for a government with limited financial resources to provide health care for the country's poor. We have the policy we want, and it requires continued support if it is to achieve

its objective. Our strategy is to strengthen the institutional capacity of the MOH to enable it to provide more effective primary care to the people it is now serving, and then expand the base of the health pyramid to serve a greater percentage of the country's population. This strategy will be supported by continuing and expanding present efforts to provide safe drinking water to the target group and thereby both lessen the need for more expensive curative care interventions and make primary care efforts more effective. It will be complemented by further research into the nutrition situation leading to the development of a comprehensive nutrition strategy. Projects in the health, agriculture, and education sectors will be modified to take into account the results of this research.

The MOH's strategy is basically sound, and is now being supported by two major AID-funded programs - Health Sector I (522-0153) and Rural Water and Sanitation (522-0164). Under Health Sector I, we are concentrating on improving the MOH's management and support system - the weak point in its efforts to get the broad, community-based, primary care system now in place to provide more effective health care. The system is being improved through a major technical assistance program in areas such as management, planning, maintenance, logistics, supervision and continuing education. We will also support a major expansion of the use of the highly successful ORT throughout the country. Through FY 1986, these efforts will be funded under the ongoing Health Sector I (HSI) program, which is currently being redesigned to expand some activities and introduce new ones, such as nutrition surveillance and treatment for acute respiratory infections. Others now completed or found to be less critical will be dropped.

Starting in FY 1987, we will assist the MOH to further strengthen its ability to manage health services and provide for increased rural coverage under Health Sector II. We expect the initiation of this program to coincide with a GOH decision to charge a minimal amount for consultations and for low-cost drugs through the MOH and/or local retail stores. Experimentation with diverse payment schemes for drugs is now ongoing in several areas. Finally, in order to meet the needs of urban workers and reduce dependency on high-cost hospital services, the availability of clinic-based services in marginal urban areas will be increased through the use of local currency generations starting in FY 1985. The MOH's efforts, with AID and other donor support, should enable the GOH to provide primary care to 75% of the country's population by 1990. These programs respond directly to recommendations of the NBCCA to expand technical assistance programs, eradicate vector-borne diseases, and train primary health care workers.

Good progress is being made under the Rural Water and Sanitation Project in installing simple gravity flow water systems in small rural communities. Household sanitation is being improved through installation of water seal latrines or pit latrines in conjunction with the rural water systems. Funding was recently added to this project, and it should be completed in FY 1987. At that time we expect to initiate a continuation program - Rural Water and Sanitation II. These efforts, plus those supported by other donors, are giving Honduras a reasonable chance of achieving the target of 90% coverage

for drinking water set at the beginning of the decade. AID must continue to contribute to the achievement of that goal.

b. Family Planning

i. Status

High fertility, combined with declining mortality rates, have produced a very high population growth rate in Honduras. Between 1960 and 1982, the crude birth rate fell by only four points, from 51/1000 to 47/100. During the same period, crude death rates fell from 20/1000 to 12/1000. Honduras' population more than doubled between 1955 and 1982, to an estimated 4.1 million. The current rate of natural increase is 3.4%. If that growth rate continues unchecked, the population size will once again double, to 8.2 million, by 2000.

The estimated total fertility rate (TFR) per woman in Honduras averages 6.5 live births. As in most developing countries, rural women average twice as many live births (8.2) as their urban counterparts (4.1). This high fertility rate has adverse effects on mother/child health. Many pregnancies occurring closely together weaken mothers physically to the point that future children are themselves born at risk. Such high fertility translates into a dependency ratio of slightly less than 1:1; that is, for every person of economically active age (15-64) there is slightly over one economic dependent. Given this age structure, overall population growth momentum will continue, even as fertility rates decline.

The Mission estimates that approximately 166,000, or 31%, of the 535,000 married women of reproductive age (MWRA), which includes unmarried women in union, are active contraceptive users. A contraceptive prevalence survey conducted in 1981 showed that 68% of the MWRA did not wish to have more children. Of these, 91% could name at least one modern contraceptive method, and 27% were actively contracepting. However, 24% did not know where to obtain contraceptives. This large need for family planning services is concentrated mainly in rural areas. The reasons for the presently low level of contracepting women are varied, and include religious beliefs, lack of knowledge, and lack of reasonable access to services.

ii. Family Planning Strategy

To reach the goal of 45% contraceptive prevalence among the MWRA by 1990, approximately 138,000 additional women will need to become continuing users. Of these, some 36,000 can be expected to become users without any additional program effort. Our target is to reach the remaining 102,000, which will require a new acceptor rate of 3.1% per year. The strategy for reaching this target is to attack the supply side problems through an increased number of contraceptive distribution and sales points, and improve management and logistical capability of family planning service providers. These improvements will be supported by targetted mass media campaigns which identify distribution points. The yearly increase in the number of contracepting women has been approximately 2.7% over the last few years. With

the improved logistics and management of service providers and mass media efforts, the Mission believes that this can be raised to the 3.1% yearly increase required to achieve the goal.

Both private and public sector channels will be used. The Honduran Family Planning Association (ASHONPLAFA) will continue to be the major private service delivery program. Specifically, programs in community-based distribution, voluntary sterilization, and contraceptive social marketing will be strengthened administratively and expanded geographically to incorporate increasing numbers of contraceptors. An average annual increase of 10% in the number of active ASHONPLAFA users of contraceptives is projected. The number of community distribution points will increase from over 1,000 at present to 1,500 by 1990. Under the contraceptive social marketing program, four contraceptives (two orals, condoms, and a vaginal foaming tablet) will be commercialized at affordable prices in 600 retail outlets by the end of 1984. The Mission will also seek to expand and develop service delivery through other PVO's, local associations, and private clinics and pharmacies through a multi-year umbrella OPG.

In the public sector, the MOH, with AID encouragement, recently has made a major change in its policy regarding family planning. The MOH has decided to take an active role in promoting family planning throughout the country through its network of regional hospitals, health centers, and health posts. To support this basic policy change, the MOH has also authorized auxiliary nurses to prescribe pills and professional nurses to insert IUD's. It has reduced the age-parity requirements for voluntary sterilization. Furthermore, it is carrying out a major mass media campaign to further the cause of family planning. Finally, the MOH has officially approved a family planning service delivery program for 1983 to 1986. It plans to do periodic updates of the delivery program.

AID has waited many years for the MOH to treat the family planning issue with something more than benign neglect, and we have now have the policies we want. In support of those policies, AID will help strengthen the MOH's family planning service system. The Ministry's expanded role in delivering family planning commodities and services will place its already weak logistics planning and execution capability under further stress. Achieving the goal will depend in large measure on rapidly improving this capability. The Mission's on-going Health Sector I program is addressing this problem through training of personnel, building the MOH's logistics planning capability, and constructing necessary warehouse space. In addition, the ability of the MOH at both the regional and central levels to better plan and coordinate its family planning programs is being strengthened through the sustained application of operations research methodologies to this area. These efforts will be expanded and continued under Health Sector II.

6. Labor-Intensive Housing and Infrastructure

a. Status

Honduran housing conditions are very poor. Approximately 75% of the country's

housing is considered substandard using GOH norms of physical condition and overcrowding. Half of the capital city's 400,000 residents live in urban slums, 40% lack piped water, 50% lack electricity, and 45% have no sanitary facilities. A similar situation is found in other population centers. In the villages and hamlets where two thirds of the country's population and 80% of its poor live, housing conditions are worse, and access to water and electricity is even more limited. About 50% of rural homes have access to potable water. However, only 10% have electricity and that percentage has not improved significantly over the last decade. Despite the successful effort now being made through the Rural Water and Sanitation Project, only about 30% to 40% of the rural population use basic sanitation facilities, most of which are simple pit and water seal latrines.

As with most developing countries, Honduras is experiencing rapid urbanization. The two largest cities are growing at a rate of 6% to 8% per year. At current rates of growth, Tegucigalpa will reach almost a million people by the year 2000 and San Pedro Sula will have over 800,000. Some smaller cities are growing at even faster rates. The rapidly increasing urban population is putting already deteriorated shelter and related infrastructure under even more stress.

Two GOH institutions are addressing the housing problem - the Housing Institute (INVA), and the National Housing Finance Agency (FINAVI). After many years of inadequate performance, INVA has made great strides in increasing its production of low-cost shelter solutions over the last few years. It is now producing over 2,000 units a year, most of which are being financed under the Shelter for the Urban Poor Project (522-HG-005). It has successfully implemented turnkey projects with the private sector, and is producing a broader range of lower-cost solutions. As well, INVA is competently administering a DA-funded Rural Housing Improvement Program (522-0171) which is providing small loans for progressive shelter development in rural areas through PVO's. However, INVA continues to depend almost entirely on external financing for construction of new units.

FINAVI was created in 1973 to serve as a secondary mortgage financing source for the then fledgling private savings and loan system. Despite AID assistance at present through the Private Sector Shelter Program (522-HG-007), FINAVI is in a financial crisis it may not survive. It is unlikely to be a major source of long-term mortgage financing during the CDSS period. Without access to additional mortgage funds, it is possible that one or more of the country's six private S&L's may fail.

There is domestic political pressure for the creation of a Social Housing Fund, as promised in the Constitution, and it is likely to be created within the next year or so. The degree to which its function would complement those of existing institutions remains to be worked out.

There appears to be an ample market for well located, low cost shelter solutions in the major cities, and there is evidence of a good sized market in the secondary cities. There is a strong need for shelter related services

such as water, sewer, electricity, and street paving in all of these cities. Development of additional housing and related infrastructure can both meet these needs and absorb relatively large amounts of unskilled labor, and provide semi-permanent employment for many low income families. With some minor improvements, the institutional capacity of the major actors - INVA, SANAA, and ENEE - should be sufficient to enable implementation of a much larger program in housing and related infrastructure. Long-term financing is the major short-term constraint. Improved utility planning and development of mechanisms for mobilizing domestic resources for investment in housing through private sector mechanisms will be needed over the longer run.

b. Strategy

In the short run, the Mission's strategy will be to provide the GOH with a modest level of long-term HG financing for shelter and related infrastructure programs in the country's major population centers. To address the longer-term needs, we plan to provide additional HG financing and local currency resources for shelter and related infrastructure, and DA financing for technical assistance aimed at improving the functioning of the sector. The technical assistance will be for improving utility systems planning and the institutional capability of INVA, SANAA, and ENEE in delivering services to the urban poor, and developing a better system for mobilizing domestic resources for shelter. The assistance in utility systems planning will be aimed at helping Honduras obtain financing for major infrastructure improvements from other IFI's with greater access to lending capital than AID. As much as \$1 billion for major infrastructure projects will be needed from the IFI's during the CDSS period. The technical assistance will be provided through the Policy Analysis/Technical Support Project to be initiated in FY 1984 and a follow-on project late in the CDSS period.

Implementation of the short term strategy will start with a \$25 million HG loan in FY 1984 to follow up on the successful Shelter for the Urban Poor Project. This project will emphasize progressive development of minimum cost shelter solutions, expand INVA housing into a number of secondary cities, and continue the use of the turnkey construction system through private contractors. A new mechanism for ensuring that INVA, SANAA, and ENEE coordinate their efforts under the project will be developed. An additional HG is planned with the Social Housing Fund, if it is created, in FY 1985 or FY 1986. In support of the longer-term strategy, additional HG loans will be needed in FY 1987 and FY 1989. The former may be a follow-up to the ongoing Urban Upgrading Project (522-HG-006), through which water and sewers are being installed in squatter settlements in the two largest cities. These programs respond to the NBCCA recommendation that an enlarged housing and infrastructure program be undertaken in the region. The proposed program should create a semi-permanent demand for labor in the construction industry, and over time absorb some of the workers employed under the "first offensive" against unemployment.

The major policy issue is the elimination of subsidies traditionally provided by the GOH for housing and related infrastructure projects. The GOH can no

longer afford the subsidies implicit in its past financing practices, and must introduce greater financial discipline into its investment decisions. We will work towards the progressive elimination of subsidies, and toward the full application of project development costs in calculating cost recovery factors. New cost recovery methods, e.g., special assessments, project-specific user charges, general rate adjustments, will be needed for implementation of the new policies, and assistance will be provided in their design and implementation. The HG financing and local currency resources will be progressively linked to the development of private sector market mechanisms for mobilizing domestic resources for housing.

Assuming that the mechanisms designed to mobilize domestic investment in housing are moderately successful, a major improvement should take place in the shelter and related infrastructure sector. The HG resources alone will create over 7,500 person years of employment, and finance over 10,000 new shelter solutions and improvements in 25,000 more. Development of appropriate market mechanisms for long-term financing could easily double these figures, which would convert almost 20% of the country's substandard units into acceptable dwellings. Houses without water and electricity in Tegucigalpa, San Pedro Sula and some secondary cities would be significantly reduced.

D. Strengthening Democratic Institutions and Respect for Human Rights

1. Status

Honduras is now in its third year of government under a popularly elected civilian government. It is our expectation that the process of free elections and civilian government will continue in 1985, and result in the institutionalization of regularly elected democratic governments. It is quite possible that Honduras now has the political maturity needed to ensure that its present constitutional system is maintained and improved. The Central American political situation has put Honduras into an international fishbowl where the strength of its democratic institutions will be severely tested and its furtherance of human rights subjected to significant international scrutiny. Honduras is no longer a virtually unknown "banana republic."

Over the short and long run, an economically and politically sound Honduras will depend as heavily on further growth and development of free, democratic institutions. Fortunately, Honduras' open economy and pluralistic society over time has allowed for the development of many such institutions. They include a vigorous and independent trade union movement active in industry, the banana plantations, and small farm and agrarian reform agriculture; a politically strong cooperative movement; an increasing variety and number of local PVO's; some 50 private sector trade associations and professional guilds; a private banking system with 15 commercial banks, including four which are branches or affiliates of major U.S. banks, and six savings and loan associations; and two old-line political parties and several newer ones.

Honduras' large number of private voluntary organizations and interest groups taken together give the country a special character and strength. Their

existence, and indeed the combination of them, gives Honduras a distinct flavor - its use of consensus resulting from the interaction of interest and pressure groups to regulate a wide variety of social and economic affairs. All of the groups have some voice in making Honduras work, and their views on issues of national significance often diverge a great deal. They seem content to lose once in while as long as they win often enough to stay in the game. Honduras' traditional tolerance of diverse views and pacific methods of resolving issues provides a strong basis for success in the democratization process.

Honduras' record on human rights is also highly positive. The most recent Department of State human rights report gave Honduras a favorable rating. Honduras does not have a history of political assassination, political prisoners, torture, or death squad murders, and the press reports widely any charges of police mistreatment. Freedom of press, speech, religion and assembly are respected. Occasional detentions beyond the 24-hour period permitted by Honduran law have been noted, and the government is attempting to adhere more closely to established legal requirements. The legal rights of women in marriage, family relations and divorce are inferior to those of men, but a new family code which will provide enhanced legal rights for women is being actively debated in Congress, and is expected to be approved this year. In practice, women are playing an increasingly important role in Honduran society. There are a number in high government positions, including at present those of Minister of Education and Attorney General, and many more in banking and business as owners and employees. Regardless of their legal rights, the poor in Honduras find legal remedies almost prohibitively expensive to pursue.

2. Strategy

With the exception of the private banks, Honduras' numerous free democratic institutions have a common weakness - they are neither well managed nor well funded. The management and financing of some of the cooperatives, PVO's, business groups, campesino organizations, and credit unions will be improved through their participation in the programs discussed elsewhere in the CDSS. Particularly important among these is the National Association of Campesinos (ANACH) - the principal spokesman for about 10% of the country's most vocal small farmers. Further development of these organizations should contribute to keeping Honduras a free and pluralistic society.

In addition, other specific efforts which are important to reaching U.S. objectives will also be supported. The National Elections Tribunal will be aided in planning and carrying out the next election with support from local currency generations. A campesino newspaper will be developed with support from an LAC regional project. Opening of the legal system to more effectively serve the poor will be sought through a regional program to professionalize the judicial system, through legal training for Hondurans in other countries, and a local currency funded legal reform program aimed at modernizing Honduras' outdated basic legal codes. We will attempt to stimulate a national debate on legal reform through a domestic organization with local currency generations.

A massive training program at the non-degree technical level, B.A. and graduate level will be carried out by USAID/Honduras and USIS under a centrally-funded scholarship program. We intend to target the gifted but less privileged, and to do so in ways which simultaneously accelerate the development process and serve to further our political objective of a democratic, pro-US Honduras in the future. The democratic trade unions will continue to receive support and training from the American Institute for Free Labor Development (AIFLD) through its regional project.

IV. Special Concerns

A. Absorptive Capacity

The country clearly has the ability to absorb additional outside assistance, both financial and technical. Its recent negative economic growth suggests that increased resource flows are needed. The question is where they can be effectively absorbed and provide maximum benefit in view of the growth and equity objectives of the strategy. The weaknesses in certain GOH ministries e.g., health and education, will be improved through significant technical assistance. Indeed, the assistance provided to date in both these ministries seems to be having the desired effect. The GOH has additional absorptive capability in infrastructure development. While it could have difficulty meeting cash counterpart requirements, reasonable acceptance of in-kind contributions and the use of local currency generations can help ensure rapid absorption of assistance. The country's overall indebtedness has grown rapidly over the last few years and may cause strain on the GOH budget in the short run. However, the overall favorable terms of existing debts (average maturity of 27 years, average interest rate of 5%) should allow for considerable additional borrowing on concessional terms during the CDSS period.

The private sector has additional absorptive capability, but it needs to be encouraged to assume a more active stance as a development channel. Industrial plant and labor utilization rates are low, in general, and there should be little overall problem in expanding aggregate output if the right products are produced. What is needed are well conceived, realistic production projects, based on good marketing information and careful study. Assistance aimed at these projects can be absorbed easily and quickly, and can make a major contribution to solving the country's high unemployment and low production problems.

The matter of recurrent costs is a bit more difficult. Carrying out the strategy will increase government operating costs, especially in the health and education sectors. The additional budget that will be needed cannot now be estimated, and the level of budgetary resources that might be available will depend, to a large degree, on macroeconomic factors such as overall GDP growth and fiscal policy. The matter comes down, in the end analysis, to the propensity of the GOH to spend for social services. In this respect, its past record is quite good. During the mid and late seventies, at a time of relatively robust economic growth, budgets for health and education regularly increased at rates of 10% to 15% a year. The politically strong, aggressive,

and well organized teachers and health workers can be expected to push for higher budgets in these areas. The cost recovery efforts discussed in the health, education, shelter and urban infrastructure activities should help in lessening the recurrent cost burden. In sum, the GOH's past high propensity for spending on social services coupled with appropriate policies regarding pricing of services provide a basis for expecting that government service levels will be maintained.

B. Relations with Other Agencies

While the proposed strategy calls for a major effort administered through AID to address Honduras' development problems, this effort will be insufficient by itself. Both significant other donor resources and complementary efforts by other USG agencies will be needed in order to ensure its success. The most important are:

1. CADO

Clearly regional stability is needed to reach the goals outlined above. To the extent that CADO encourages the countries of the region to minimize their differences, it could play an important role in determining the success of each of the Central American Countries in furthering their own and the region's development. Until more is known about CADO and the U.S. commitment to its success, it is hard to judge how effectively it will be able to play the role envisioned for it in the NBCCA report. The Mission would expect to play a supportive role, if and when CADO is created.

2. CACM Instrumentalities/ROCAP

The NBCCA report proposed a significant strengthening of the Central American Common Market. Among other ideas, the Commission recommended that the U.S. join CABEI, that the Central American Clearing House be strengthened and recapitalized, and that a Central American Venture Capital Company be created. ROCAP's strategy, which is based on these recommendations, includes a preliminary policy agenda. While the strategy is a good start, USAID/H does not believe the proposed policy agenda goes far enough, as it provides no arrangement for resolving chronic intraregional trade imbalances over the longer term in the absence of positive net dollar reserves in each member of the CACM. The Mission believes that a currency adjustment arrangement similar to that used by the EEC will be needed to ensure long-run adjustment of trade balances among the five countries. It also does not address the issue of Nicaragua's benefits from implementation of the strategy. As a practical matter, we believe that the issue of excluding Nicaragua as a beneficiary country may prove to be an insurmountable stumbling block to negotiating the proposed policy reforms and to implementation of the proposed programs.

3. Other IFI's

Success in reaching the goals will require a high level of other donor financing. As much as \$1 billion just for major infrastructure investments

will be needed from the World Bank and the IDB. Coordination of policy issues, especially with the IMF and the World Bank, would also help to facilitate success. To achieve the kind of coordination needed, the Mission expects to make greater use of existing communications channels, especially the offices of the U.S. Executive Directors in those agencies. At a minimum, a regular once-a-year program and issues meeting will be needed. The burden will fall on AID/W to arrange timely meetings, keep communications channels open and follow up on the results of such meetings.

4. Other USG Agencies

Some complementary efforts that will be needed to maximize the developmental impact of Mission funded projects were proposed in the NBCCA report, including an adult literacy campaign, a Central American Teacher Corps, and a major program of short- and long-term scholarships in the United States. USG efforts to increase adult literacy should be directed to supporting and improving the Ministry of Education's ongoing campaign, which appears to be working well. Extensive coordination with USIS and the Peace Corps will be needed to ensure that AID programs and these efforts reinforce each other to the maximum extent. We will continue to work closely with these organizations, and expect that adequate coordination can be achieved through regular program reviews at the field level. More specific measures to ensure close cooperation with other USG agencies will be worked out as more becomes known about the specific arrangements for implementing each program.

C. Role of the Private Sector, including PVO's and Cooperatives

1. Role of Private Profit Making Firms

The Mission has been increasingly using private firms, especially the more liberal and aggressive local banks, as channels for administering resources under AID financed projects. A completely new private organization, the Cattle Fund (Fondo Ganadero), was developed to implement the Small Farmer Livestock Project, which was authorized in FY 1983. The Export Development and Services Project will provide initial support to several new private sector organizations, one of them profit oriented, which have been formed to help Honduran entrepreneurs begin to expand their horizons, obtain outside contacts and technical resources, and take advantage of new incentives (CBI trade provisions, Honduran Export Incentives Law) to production for export. We expect to expand contraceptive availability through private businesses, as described in the population sector strategy. Most construction work carried out under AID projects is done by private contractors. We intend to continue looking for every reasonable opportunity to carry out our strategy through the private sector.

2. Role of PVO's and Cooperatives

At present, some 20 U.S. and domestic PVO's are carrying out activities in all five priority areas under OPG's and AID funded government to government programs. Support for productive activities and services is being provided

with AID funding through four model cooperatives, 14 regional cooperatives, and the consumer owned credit union system. Two of the model coops are fresh fruit and vegetable operations with sales of over \$500,000 each annually. Several new activities are scheduled for approval during FY 1984. These activities are funded with both DA funds and local currency generations. In sum, we are already making extensive use of PVO's and cooperatives in carrying out AID supported programs.

The long-term development strategy calls for increasing use of PVO's and cooperatives as channels for AID assistance. We have found that dollar for dollar we get more mileage from these organizations than from most other development channels. However, the more experienced and capable PVO's are now close to saturated, and we will have to help new ones develop their institutional capability before they can serve as effective development channels. We expect to help 20 more PVO's to reach developmental maturity by the end of the CDSS period. To this end, we intend to initiate, during FY 1984, a local currency financed PVO development program to finance specific development projects and further increase the capacity of PVO's to play a key role in implementing AID financed projects in all sectors. Assistance will be provided in institutional development of new and existing PVO's. A key aspect of this institutional development will be significant training for field agents and promoters in project development and service delivery. PVO and contract personnel now working under AID financed projects will play an important role in providing this training.

D. Management and Staffing

The composition of the proposed portfolio and the greatly expanded assistance levels required for its implementation have occasioned major restructuring of the Mission and will definitely require expanded personnel and operating expense budget. Present estimates for USDH include a private sector officer and procurement specialist during FY 1984 and FY 1985 and a project development/finance officer, general development officer and regional legal advisor later in the CDSS period. Additionally, we estimate a need for the following U.S. contractors: training officer, agricultural information/extension specialist, private sector advisor and forestry advisor. FSN personnel will need to be expanded by hiring professionals in population, economics, agriculture and education, as well as three additional accountants/financial analysts and an assistant management officer. We are presently exploring the possibility of setting up a local currency trust fund to defray some of our longer term local expenses. Nevertheless, our operating expenses will require an immediate restoration of \$750,000 in FY 1984 to permit expanded project development and normal implementation activities to continue to proceed smoothly. Increments which reflect the costs of the proposed higher personnel levels and inflation will be needed in subsequent years.

E. Monitoring and Evaluation

Monitoring of the program will be accomplished through normal Mission

procedures. The stabilization program will be monitored through the participation of Mission Program Economists in the Joint Economic Working Group. Project implementation will be reviewed on a quarterly basis, and any lagging efforts will be evaluated and reprogrammed as necessary. Regularly scheduled project evaluations will continue to be held as defined in the authorizing document or otherwise dictated by project needs. Program reviews will be carried out in the course of preparing program documents and updates of the CDSS as needed.

Appendix:

Resource Requirements Table