PN-AAU-679

Country Development Strategy Statement

FY 1986

Dominican Republic

January 1984

Agency for International Development
Washington, D.C. 20523

TABLE OF CONTENTS

No. of
Pages

EXECUTIVE SUMMARY

The Dominican Republic faces the mid-1980's and beyond with both hope and apprehension. The country's political foundations continue to be strengthened by a series of peacefully elected democratic governments. Political pluralism is a reality in today's Dominican Republic. The country's economic and social fabric, however, faces increasing strain from inward looking economic policies and continuing deficiencies in agriculture and human resources. In response to severe Balance of Payments problems, the IMF is entering the second year of a 3-year EFF agreement, and the IBRD is involved in discussions for a major sector loan. AID involvement is substantial and, to a large degree our policy dialogue parallels and supports these agencies efforts. However, AID will pursue a distinct policy dialogue concentrating our resources on priority areas of structural change in foreign trade and exchange, agriculture, and human resources.

Negotiations with the IMF for the second year of the EFF program have encountered difficult obstacles, with the IMF proposing transfer of most official exports to the parallel market, further reduction in public sector budget deficits, and an overall BOP surplus in 1984. The GODR is resisting, claiming a politically unacceptable inflation rate will result. Negotiations are continuing, and every expectation is that an agreement will be reached as the costs for not are unacceptable. FY's 1984 and 1985 ESF resources will be tied directly to this accord.

AID strategy involvement over the planning period will draw its major impetus from the now-enacted Caribbean Basin Initiative (CBI), with the major emphasis placed on strengthening the private sector's role in development of the country's resources.

In the area of foreign trade and exchange, AID strategy is aimed at making exports as profitable as imports, to be accomplished through foreign exchange policy changes, institutional reforms and technical assistance.

Agriculture strategy will focus on increasing incentives to private farmers, reform and reduction of a bloated and inefficient public bureacracy, and continued involvement in the protection of the natural resource base so vital to this island's productivity.

Human resources will focus on continuing the nascent primary education reform effort, strengthening of the newly created school of management, and institutional strengthening of the country's democratic institutions.

Areas of continuing concern, albeit at a declining level, will be health and energy, where ongoing major AID programs will be consolidated.

To accomplish these ends, AID proposes a mix of resources from DA, ESF, and PL-480 accounts in the range of approximately \$70-\$80 million per year through 1989, plus HG resources of approximately \$20 million every two years.

AID programs will incorporate an approach emphasizing the private sector and policy dialogue, as well as institution building and technology transfer. To an increasing degree, Peace Corps and AID programming is focusing on several areas of common concern.

I. ECONOMIC AND SOCIAL OVERVIEW

A. Recent Economic Performance

Following the period of political instability in the early 1960's, the Dominican Republic entered upon a period of extremely rapid economic growth. Industrial development, stimulated by easy access to domestic and foreign credit, generous investment incentives, and high levels of tariff protection, led to a boom which saw a rate of overall economic growth almost unprecedented in the western hemisphere. Between 1971 and 1974, GDP expanded in real terms at an average annual rate of more than 11% per year. In spite of persistent high unemployment, this import substitution structure worked fairly well in the Dominican Republic as long as world prices and the domestic production of traditional agricultural and mineral export commodities were reasonably high and opportunities for industrial capital expansion were not exhausted. When this situation prevailed, virtually every sector benefited. The agricultural sector received higher profits, the manufacturing sector obtained an abundant supply of foreign exchange to import raw materials and capital goods mainly to satisfy consumer demand in the domestic market and the government sector collected higher tax revenues to finance social overhead investment.

In recent years, however, the Dominican economy has been hit by adverse events beyond its control: (1) the 1979 hurricanes, which caused extensive damage to the nation's infrastructure, housing, and agricultural crops; (2) the sharp increase in world oil prices raised the import bill of petroleum products from 9.6% in 1973 to 60% of export earnings in 1982; and (3) the decline of sugar prices after 1976, especially in 1982. Beginning in 1978, the Dominican Republic's overall balance of payments has suffered successive and increasing deficits; in the 5-year period, 1978-1982, the overall balance of payment deficit cummulated to $768 million as compared with a surplus of $42 million during the previous 5-year period (1973-1977). In 1983, the balance of payments deficit is projected at about $100 million.

Even though economic growth performance has remained relatively good in recent years, the above-cited evidence on erosion of external accounts suggests strongly that this growth is not sustainable. During

1979-1982, the average annual growth of GDP was 3.9%, with a declining trend. The basic productive sectors (agriculture, manufacturing, construction, and electricity) grew at 3.0% per annum, and service sectors grew at 4.6% per annum. Bouyed by strong growth of public sector consumption, overall consumption grew at a rate of 5.5% per annum, and gross investment declined by 2.9% per annum. In absolute value, private consumption grew by 21.4% from 1978 to 1982, while public consumption increased by 53.3%. However, private investment declined by 7.6% and public investment declined by 28.7%. Even with the shift in public expenditure toward consumption in recent years, gross domestic investment has exceeded 20% of GDP in recent years due, in part, to a sustained loan and arrearage driven net foreign resource inflow.

By 1981, the Dominican Republic's adverse trend in the public sector financial situation was clearly evident. Public sector savings deteriorated sharply from 1.5% of GDP in 1980 to 0.5% in 1981, and to a negative 3.3% in 1982. Although some improvements are expected in 1983, the level of public sector savings is projected to be negative. The adverse fiscal trend was a consequence of several factors. Public sector wages and employment grew sharply during 1978-1980 and, as a result, central government current expenditures grew by 25% per annum during this period. On the revenue side, receipts barely kept pace with inflation. Current revenues as a percent of GDP declined mainly due to import growth related to increased petroleum prices and increased food imports, that were largely tax exempt. Public sector current revenues averaged 17.6% of GDP in 1976-1977 and averaged 13.6% of GDP in 1978-1981, but declined to an estimated 9.4% of GDP in 1982.

The poor performance of public finances in the period 1977-1982 was essentially determined by the failure to enact new tax legislation, a major increase in government current expenditures, and the increasing deficits of decentralized agencies and state enterprises. By mid-1980, the fiscal crisis emerged as President Guzmán instructed budget officials to hold fiscal expenditures in line with revenues virtually on a month-to-month basis. Consequently, planned 1981 expenditures were cut back and, in some cases, so severely that counterpart fund shortages developed for large externally-financed projects, which, in turn, contributed to reduce the effective inflow of external resources as well.

The substantial deficits on the state enterprise sector also contributed to the 1982 monetary-fiscal crisis. This crisis took the form of a rapid increase in the domestically-financed public sector deficit -- as percentages of GDP from 1.6% in 1980 to 4.3% in 1981 to 7.1% in 1982. The inability/unwillingness of the public sector to forego domestic financing of its deficit is confirmed by growth and composition of net domestic credit (based on year-end data), as follows:

	1979	1980	1981	1982	1983*
Growth of Net Domestic Credit	14.0	20.4	20.5	27.0	11.0
—To Public Sector (% Growth)	29.6	18.1	52.5	46.6	13.7
—To Private Sector (% Growth)	7.7	17.0	- 2.3	8.3	11.0
GDP in Nominal Prices (% Growth)	16.5	20.3	13.5	6.0	11.0
Composition of Net Domestic Credit (%)	100.0	100.0	100.0	100.0	100.0
—Public Sector (%)	33.9	35.1	44.5	51.3	52.6
—Private Sector (%)	54.8	56.2	45.6	38.9	38.9
—Other (%)	11.3	8.7	9.9	9.8	8.5

The pattern of 1981 and 1982 are clear and unmistakeable: the increasing growth of net domestic credit is linked to the growth of banking system credit to the public sector. The negative impacts are: (1) credit to the private sector was clearly reduced in real terms in 1981 and 1982, and (2) the overall growth of net domestic credit in 1980-1982 was clearly beyond the limit in regard to maintenance of a dollar-pegged invariate exchange rate.

After achieving a moderate balance of payments surplus in 1977, the Dominican Republic experienced increasing balance of payment difficulties in the following five years. The overall balance of payment deficit

---

* Data for year-end 1983 are based on the performance targets under the GODR-IMF arrangement.

increased from $95 million in 1978 to $337 million in 1982, and to about $100 million in 1983. The B/P current account deficit increased from about 6% of GDP in 1978 to 10% of GDP in 1980, but declined to a level of 5.5% of GDP in 1981 as a result of an expansion in sugar export earnings and a decline in imports, mainly because 1980 imports associated with the reconstruction effort after the 1979 hurrricanes were not repeated in 1981. Although the non-traditional exports showed some promise by growing at about 17% for the past few years, its impact on the balance of payments was relatively insignificant due to its small size. Nevertheless, the overall deficit increased in 1981 due to somewhat higher oil import prices, increased interest payments associated with higher interest rates in international financial markets, and reduced availability of foreign credit for both the public and private sectors. In 1981 and 1982, the government undertook corrective actions by reducing the availability of official foreign exchange through quotas, temporary import prohibitions, the tightening of exchange controls, and by granting exchange incentives to some exports. In 1982, exports and imports declined; the net capital inflow also declined sharply; and the overall deficit more than doubled to a level of $397 million. In 1983, the overall deficit is projected at approximately $100 million. The balance of payments deficits of 1979-1983 were substantially financed by the accumulation of external payments arrears and the net reduction of the international reserves of the banking system to minus US$863 million by the end of June 1983.

The Dominican peso remained pegged to the U.S. dollar at par in the official market. In the parallel (street market), the U.S. dollar had been quoted at a premium of 20-25 over par for several prior years up to 1981. By the third quarter of 1982, this premium had maintained at 50%. In October 1983, however, the dollar premium jumped and reached 90%. In real terms, by 1981, the parallel market D.R. peso depreciated by 12% from its 1977 level, by an additional 10% in 1982, and by another 17% in October 1983.

Placed in longer term perspective, two aspects of the Dominican Republic's balance of payment deterioration merit additional consideration: one is that the net inflow of private capital declined markedly in recent years, reflecting the impact of escalating commercial arrears on perceived external creditworthiness. Related to this is the domestic interest rate control, particularly a low time deposit rate maximum that has been an important incentive for Dominicans to hold liquid funds abroad. The other aspect of the deterioration of external accounts is the lack of export dynamism. Dominican exports are characterized by heavy dependency upon four primary agricultural commodities and three mineral products with relatively minor domestic processing.

The structural composition of 1979-1983 commodity exports was as follows:

Structure of Exports
(In Percentages)

	1979	1980	1981	1982	Est. 1982
Agriculture	59.6	50.8	62.7	62.1	61.2
Sugar & by products	26.7	33.9	47.0	40.0	39.3
Coffee	18.1	8.0	6.4	12.5	9.4
Cocoa	8.4	5.3	3.8	6.9	7.2
Tobacco	6.3	3.6	5.5	2.8	5.3
Mineral	31.3	39.4	28.1	25.2	28.5
Bauxite	2.4	1.9	1.3	0.7	-
Ferronickel	14.2	10.5	9.3	3.2	7.4
Gold-Silver alloy	14.7	27.0	17.5	21.3	21.1
Others	9.0	9.8	9.2	12.7	10.1
TOTAL EXPORTS ($ Millions)	869	962	1188	768	792

More than 60% of export earnings was derived from four traditional agricultural products--sugar, coffee, cocoa, and tobacco. Additional 30% depended on mineral resource exports and only about 10% came from the other category. That is, approximately 90% of all export earnings has been derived from commodity exports that are well known for their wide price fluctuations in the world market. The export value increased from $869 million in 1979 to $1,138 million in 1981, plunged 35% to $768 million in 1982, and is projected to rise somewhat to $792 million in 1983. This instability in the foreign trade sector should be brought under control if the Dominican economy is to avoid disequilibrium in the balance of payments.

Furthermore, even more serious problems of the shortage of foreign exchange loom ahead. It is reported that the reserves of gold-silver oxide at the Rosario gold mine, the source of all doré exports to date, will be depleted in five years at the current rate of production. After five years, gold and silver might be recovered from the sulfide ore, which will require major investment in the extractive process. It has yet to be determined whether the new process will be economically feasible. The significance of the implication of this prospect is clear. About 20% of earned foreign exchange will be lost to GODR in five years, if appropriate measures are not taken soon.

The Dominican Republic's external public sector debt (on a disbursed basis and including publicly-guaranteed debt) increased from $844 million at year-end 1978 to $1,747 million estimated for year-end 1982. Adding commercial arrears, a defacto responsibility of the Central Bank, brings the 1982 estimate to $2,183 million and signifies a 159% increase during the 4-year period (1979-1982). In 1981, total external debt service payments (public and private) amounted to $372 million or about 25% of exports of goods and non-factor services. The estimated 1983 debt service ratio is 38%, due to higher service payments ($440 million) and also to low export earnings. Compared to the 1980 debt service ratio of about [illegible], this ratio is considered to be high and is expected to decline as exports pick up.

B. The IMF Arrangement

The Jorge Blanco administration, which took office in August 1982, was confronted with a heroic task: it had to design and implement measures to alleviate the pressing fiscal and balance of payment problems, and also to address the underlying longer-term problems which contributed to the present situation. It took immediate emergency measures to reduce imports and to reduce public sector expenditures and increase public sector revenues. It also initiated negotiations with the IMF and foreign commercial banks to obtain substantial financial resources to reduce external payment arrearages and restore external creditworthiness. Negotiations with the IMF culminated in an SDR371.25 million net 3-year Extended Fund Facility (EFF), signed in January 1983.

The IMF agreement contains the usual performance criteria, specified one year at time, related to expansion of net domestic credit of the Central Bank and the Reserve Bank, net domestic assets of the Central Bank, net reduction in external payment arrears, Central Bank net international reserves, as well as limits on the contracting of new external loans by the public sector, a $100 million reduction in Central Bank external payment arrearages, and a $85 million transfer of official imports in 1983 to the parallel exchange market. The IMF arrangement did not require devaluation of the official exchange rate, but encouraged legalization and utilization of the parallel exchange market. It was hypothesized that a policy of broadening the scope of the parallel foreign exchange market would facilitate unification of the exchange market at some future time at a realistic rate.

1/ By year, the net flow of IMF resources is as follows: SDR123.75 million (1983), SDR123.75 million (1984), and SDR123.75 million (1985). At a 1.2 US$/SDR conversion rate, the U.S. dollar equivalent is $148.50 million each year.

The first year of the EFF aims more at the restoration of orderly external payments and confidence than upon improvements in price-directed resource allocation. The IMF/GODR arrangement places strong attention at reduction of the public sector financial deficit. The Jorge Blanco administration sponsored several measures to increase revenue: a 10% <u>ad valorem</u> surtax on imports, a capital gains tax on property sales, modification of the income and other taxes, and enactment of a 6% sales tax (to take effect in November 1983). In addition, central government expenditures are to be reduced by 8.6% in nominal terms in 1983 and programs have been adopted to reduce the deficits of state enterprises, in particular CEA, CDE, CORDE, and INESPRE. The overall public sector deficit is to be reduced to about 4% of GDP in 1983, as compared with a 7% deficit estimated for 1982. In this regard, the President scrutinized the financial operation of CEA, CDE, CORDE, and INESPRE and reported that their deficits had been reduced between 44 to 74% during the January-June 1983 period, compared to those during the same period in 1982. <u>The deficit of the central government has also declined from RD$140 million in the first half of 1982 to RD$85 million during the same period in 1983--a reduction of 39%.</u> This remarkable outcome is primarily due to the stepped up effort in tax collection initiated by the Jorge Blanco administration.

Monetary restraint in the form of a targetted growth of net domestic credit for 1983 of 11% as compared with a 27% growth in 1982, serves to reduce growth of aggregate demand and, in this manner, import expenditures. The 1983 B/P current account is estimated to have improved by approximately $80 million. The rest of the $315 million targetted reduction in the 1983 overall B/P deficit results from increased net capital inflow to the public sector related to reduction of rescheduled arrearage payments under the GODR/commercial bank debt renegotiation. <u>Thus, upwards of two-third of the targetted 1983 B/P improvement depends upon non-exchange rate forces--principally upon GODR negotiative skill. The real economic sector, however, has not yet increased production and exports in response.</u> For the IMF arrangement is essentially a stabilization program. The IMF conditions, which limit net domestic credits, net domestic assets of the Central Bank, net external payment arrears, net international reserves of the Central Bank and place ceilings on foreign borrowing by the public sector, prevent the GODR from adopting an expansionary economic policy for the duration of the agreement. Without the initiation of expansionary policy measures, it is unlikely that a new wave of investment and production will be forthcoming. In addition, the commercial debt rescheduling provides only a 1-year grace period (1984). Thus, the GODR must find ways of increasing its export earnings in the short- to medium-run to meet the new debt repayments and expand the economy.

The negotiation for the second year IMF EFF program seems to have encountered difficult obstacles. The IMF delegation proposed, in early November 1983, another stabilization program which includes continued transfer of official imports to the parallel market, further reduction in public sector budget deficits, and an overall balance of payments surplus for 1984. The GODR, on the other hand, objected to the new IMF proposal for being too restrictive and constraining for the well-being of Dominicans. The proposed transfer to the parallel market of all official imports over 1984-1985 includes imports of medicine, baby foods, news prints, oversea travel, fertilizer inputs, some essential raw materials for manufacturing, and petroleum. The transfer of these imports is unacceptable to the GODR on grounds that it is too inflationary. On the fiscal side, the IMF officials expressed their concern over the excessive 1984 fiscal deficits. It was reported at that time that the 1984 budget was set at about DR$1,400 million with the expected tax revenue of only DR$800 million. The huge fiscal gap was entirely unacceptable to the IMF.

The actual 1984 budget indicates that the GODR is prepared to increase substantially the capital budget which has been depressed at low levels during the past two years. The proposed 1984 budget is set at DR$1,385 million, up from DR$1,017 million in 1983. Of the DR$368 million increase in the budget, more than DR$250 million will be earmarked for capital expenditures. This increase is to be financed from, in addition to foreign resources, the increase in public revenues from the new 6% value added tax which went into effect on November 23, 1983; the new tariff measure which evaluates the value of imports based on the parallel market exchange rate rather than the official rate; and proposed new taxes. They are: capital gains tax on transfer of real estate, tax on horse racing, tax on local alcoholic beverages, tax on the ownership of firearms, and tax on insurance premiums. It is expected that additional DR$200 million in tax revenues will be generated if the new tax measures are implemented early in 1984.

The IMF team is scheduled to arrive in the middle of January 1984 to begin the second round of negotiations for the second year IMF EFF program. Whether or not the GODR and IMF will come to an agreement at the January meeting is uncertain. What is certain is that the continuation of the IMF program is absolutely essential for the success of the economic recovery program for the Dominican Republic.

C. The Foreign Exchange Rate/System

The foreign exchange system of the Dominican Republic is two tiered. There are two exchange rates, the "official" rate of one peso to one dollar, and a "parallel market" rate running at near DR$1.80 to one U.S. dollar since October, 1983. In principle, foreign exchange at the official rate is available from the Central Bank for meeting the government's own obligations, for annual profit remittances on registered foreign investments, for petroleum imports, and for imports of raw materials and semi-finished inputs up to a quota equal to 55% of the 1979-1982 actual usage of foreign exchange by the firm. The sources of "official" foreign exchange include registered foreign investment, export proceeds, peso purchases by free zone companies, and international transactions of the GODR. Since 1979, all access to foreign exchange at the official rate through the Central Bank is subject to long delays: approximately one year for raw material imports, approximately two years for profit remittances and debt collections, and several months on the partial return of foreign exchange proceeds on non-traditional exports.

Until November 17, 1983, there were essentially no restrictions on private sector access to foreign exchange on the parallel market. For a price, exchange is available for any purpose on the parallel market at rates which vary day by day. The sources of foreign exchange for this market included tourist expenditures, private transfer payments from Dominicans living abroad, expenditures by foreign residents, and perhaps a certain amount of under-invoicing of exports. The volume of imports financed through the parallel market is substantial, probably amounting to over 50% of non-petroleum imports.

However, faced with a rapidly rising parallel market exchange rate and some evidence of capital flight, the GODR suspended on November 17 for three days the operation of all exchange houses and issued a new set of regulations governing foreign exchange transactions. They are:

- Cessation of operation of all exchange houses (about 400) throughout the country;
- Some designated Exchange Banks are allowed to buy and sell foreign exchange at a predetermined exchange rate;
- All imports must be carried out through issuance of letters of credit by commercial banks;
- Prohibition of the transfer of foreign currency out of the D.R. in amounts exceeding $5,000;
- The new Exchange Banks must transfer to the Reserve Bank at the end of each working day the excess of foreign exchange;
- The Reserve Bank is authorized to intervene in the parallel market to stabilize the exchange rate.

It is still too early to tell the degree of success of the latest GODR measures to control the parallel market. Since November 17, about one dozen authorized Foreign Exchange Banks have been buying dollars at the maximum allowed bying rate of DR$1.79 = US$1.00, but they are not selling at the maximum allowed selling rate of DR$1.81 = US$1.00. Not much black market activity, however, has been reported as feared by many observers. The association of former exchange houses petitioned the President to reconsider the Presidential decree and to provide means for its members to continue to earn their living. One positive effect is that the Central Bank and the GODR tax authorities can obtain import data based on payments rather than arrivals. Since all imports require letters of credit through the commercial banking system, the import data and the tax base will be more accurate and up-to-date.

There is widespread agreement that the Dominican peso is overvalued at the official exchange rate. These differences concern three major issues: the symbolic advantage for political reasons of maintaining the one-to-one official rate, the ability to manage a devaluation so as not to trigger a massive increase in costs and prices, and the viability of traditional exports and export expansion. Maintaining a one-peso to one-dollar link is doubtless an anchor to windward, which makes stern economic policies more palatable politically. In terms of domestic costs, imports have been subject in recent years to defacto devaluation in the form of overdraft charges that Dominican importers must pay because of Central Bank delays in delivering foreign exchange. Also, the average peso cost of imports of raw materials, capital and consumer goods has increased due to continuous shifts from the official to parallel market.

It is generally acknowledged that the 90% of export earnings that come from primary agricultural commodities, which are subject to an 80% surrender requirement at the official rate would not expand much due to the fact that Dominican supply response would be slow due to the need for substantial time for new investment to produce most traditional exports. In addition, even though non-traditional exports receive partial exemption from the official rate surrender requirement, this system is administratively discretionary and subject to delay and potential abuse.

An asymetrical trade-exchange system is difficult to correct and the temptation is to hold back from any adjustment. The correct but difficult approach, and one we intend to encourage in conjunction with IMF, is to recognize that when an exchange rate is over-valued, the economy is living above its means, and that a cut in the standard of living may be a necessary part of the adjustment process. With a fiscal-monetary program put in place to reduce aggregate demand, a realistic adjustment of the exchange rate can serve to reduce the demand for imports without expanding the quota/licensing/prohibitions system (which also invites abuse), and to enhance the viability and profitability of exports, which is essential to the strengthening of the balance of payments.

II. AID STRATEGY INVOLVEMENT

A. The Caribbean Basin Initiative

The enactment of the Caribbean Basin Initiative (CBI) by the U.S. Congress and the designation of the Dominican Republic as a beneficiary country establishes the CBI as the major U.S. foreign policy instrument for the Dominican Republic for the foreseeable future. The existence of a democratically elected government, pluralistic society, absence of civil strife and close commercial, cultural, and political relations with the United States combine with the country's geographic location, installed industrial capacity, agricultural potential and generally peaceful labor force to constitute the Dominican Republic as one of the countries most likely to benefit most from two of the three CBI incentives--trade and investment. We propose that the third leg in the CBI's triad of benefits---the U.S. bilateral assistance program--draw its inspiration from and direct its major emphasis toward the CBI's successful application to the pressing development needs of this country.

As it enters the mid-1980's, the Dominican economy faces an impending crisis of major proportions. Within the gamut of problems and needs throughout the Dominican economy and society, there are four major goals to which the U.S. assistance program should aim its policy dialogue and resources in the next several years:

—Equitable growth within a strengthened democratic framework, resulting from

--Expanded employment opportunities, derived from

—Increased foreign exchange earnings, and

—Increased domestic and foreign investment.

The pursuit of reform and progress in these areas will require a major commitment from the Dominican public and private sectors as well as the donor community to redirect efforts and resources from inefficient to productive sectors. The role of the private sector—both domestic and foreign—is critical. Accordingly, the overall development strategy of the U.S. bilateral assistance program for the next several years will be predicated upon the central tenet of increased and strengthened private sector development with a concomitant reduction in public sector involvement and hindrance.

B. Strengthening the Private Sector

Inevitably, in defining the Dominican private sector, one begins by saying what it is not; that is, by defining the public sector. The public sector in the Dominican Republic is large and extends through many sectors of the economy. In addition to the various levels of government and decentralized agencies, it includes the electric company (CDE), the largest producer of sugar (CEA), and a variety of publically-owned enterprises, including the national airline, which are organized under the Corporation for State Enterprises (CORDE) and the Rosário gold and silver mining operation acquired in 1979. The country's oil refinery is one-half government-owned but managed by the GODR's multinational partner. In addition, CORDE owns a minority position in several enterprises. The large share of state enterprises in the economy was a result of the nationalization of the Trujillo family holdings in 1962, rather than a result of any desire for a substantial public sector participation in the economy as such.

Nevertheless, the private sector employs approximately 80% of all employed persons, a proportion which has remained relatively constant in recent years. Within this sector, agriculture accounts for the largest single share, 61.7%. Distributive activities account for 9.2%, while manufacturing employs only 4.7% of all employed workers. Within the public sector, the various levels of government account for the largest share of employment, 15.5% of the employed labor force, while CEA employs 5.3%.

In the past, the attitude of the GODR to the private sector in general and to foreign private investment in particular has been complex and sometimes contradictory. On the one hand, the Dominican Republic has a large, vigorous, and politically assertive private sector which the government has attempted to foster through an extensive and financially costly system of incentives. On the other hand, the administration of government programs in general, including investment incentives, has been characterized by a substantial degree of administrative discretion and case-by-case review, often by several agencies, with considerable doubt as to the outcome. Moreover, the government has on a number of occasions taken economic measures (such as price and export controls, delays in payments of foreign exchange for letters of credit, and delays in providing foreign exchange for authorized profit remittances) which have adversely affected private firms with little apparent consideration of such effects. As the current economic crisis worsened, the impact of such government policies on the private sector became magnified. To its credit, the Jorge Blanco administration has embarked upon a major effort to improve the business and investment climate, and has stated publicly and repeatedly that the private sector must take the leading role in revitalizing the stagnant Dominican economy.

For its part, it stated categorically that the public sector could not increase its employment rolls, instituted a salary cut to public employees, reorganized deficit-prone public enterprises to be more efficient, and placed the expansion of public sector expenditures and credit within the confines of an IMF agreement. More positively, in the first year in office, the new administration has taken concrete measures directed at strengthening the private sector. Some of the most important include:

--Amendment to the Foreign Investment Law to increase profit remittances to 25% of invested capital to allow registering in any free convertible currency, and to include registering of value of imported equipment and capital goods.

—Creation of a Commission for Foreign Investment Promotion, with a permanent staff and budget, and led by a board of private sector individuals.

—Revitalization of the moribund Dominican Export Promotion Center (CEDOPEX), appointment of a private banker as Director, and constituting its Board of Directors as a decision-making body under twice-monthly Presidential leadership.

—Revision of the Industrial Incentive Law to extend import duty exoneration of raw material imports to all producers.

—Establishment of the regulatory procedures necessary to implement the Agro-Industry Law.

—Establishment of an Agricultural Crop Insurance Program for private rural producers.

—Elimination of prohibition of private sector investment in mining, and initiated joint ventures with foreign private investors in mining exploration.

—Elimination of need for presidential authorization for foreigners to purchase real estate for tourism development.

—Reform of foreign exchange transaction regulations to authorize commercial bank transactions on the parallel market, use of parallel rate for credit cards, establishment of local dollar savings accounts, and transmittal of remittances through commercial channels.

—Drastic reduction of bureaucratic and administrative paperwork required to obtain export licenses.

—Authorization of the retention of increased portions of foreign exchange earned by non-traditional exporters and eliminated the surrender requirement.

—Renegotiation of the private commercial bank debt to allow the opening of new lines of credit.

—Establishment of an export promotion fund within the Central Bank with initial capitalization of $25 million.

Perhaps more importantly, it has recruited from the private sector a series of influencial individuals to fill important policy and administrative positions within the GODR. The two key individuals are the new Secretary of Industry and Commerce—a private businessman who was influencial in the umbrella private sector organization, Consejo Nacional de Hombres de Empresa--and the new Director of CEDOPEX, who is a banker. Both individuals are confidants of the President, have advised him since his nomination, have the complete confidence of the leadership of the private sector, and have embarked upon a concerted effort to effect significant change in government policies regarding the private sector. We expect to see increasing private sector participation in government. In addition, we understand that the government is drafting legislation to establish a national economic policy board, comprised of government and heads of leading private sector organizations, to advise the President and the administration on economic policy, especially in regard to the relationship between existing import substitution policies and the new emphasis on export promotion.

It is precisely in this policy area that the largest constraint lies. The past year has been devoted almost entirely to crisis management, largely related to international debt renegotiation and stabilization efforts. In the process, all sectors suffered. Moving beyond that stage will require a willingness of the government, and its private sector partners, to carry out a program of policy adjustments to emphasize reorientation of the economy towards export expansion and diversification, and establishment of clear and equitable guidelines for more aggressive private sector participation in the economic recovery program. This will result in a loss of priviledges and protection to some powerful private sector interests. The need to balance these short-term losses against medium-term gains will be a major test of the Jorge Blanco administration in the coming year.

C. Priority Areas of Structural Change

Notwithstanding GODR efforts made to date, which we believe are substantial, progress in establishing a meaningful dialogue on economic policy has been slow. After the initial reforms proposed at inauguration last year, the GODR has adopted a sequential approach to its management of short-term stabilization efforts and debt rescheduling negotiations. The IMF agreement, approved in February 1983, approved a $450 million EFF arrangement involving reduction of the public sector deficit through new taxes, a reduction in salaries, and reduced subsidies to public enterprises. Balance of payments deficits would be met through reduced imports. The parallel foreign exchange market would be expanded to include a greater share of imports and export receipts and arrears of foreign payments reduced through rescheduling. At this writing, the GODR is in compliance with the IMF agreement, although several complications have arisen. The first is a GODR 3-year $250 million program in middle-class housing undertaken to reduce social pressure and increase employment. This program threatens to utilize fully the expected net increase in revenues from the new value added tax, and result in constraints to other public sector investment. The second is an unexpected and protracted delay in concluding the rescheduling of $660 million of commercial short-term debt, for which Congressional approval is now expected in late October 1983. The third is the delay by the Paris Club in rescheduling the official debt, now scheduled for late 1984. The net effect of these factors has been an almost total preoccupation by the GODR on short-term actions, and a conviction on their part that the step-by-step measures taken to date have been sufficient. Consequently, it has been difficult to focus their attention on the need for a coherent medium-term economic program.

The IBRD with tacit U.S. support, has been the leading advocate of engaging the GODR in a structural change dialogue. However, the IBRD as well as the U.S. and other donors has been sytmied to date by the above circumstances. There are now signs that such a dialogue has begun. The IBRD is moving ahead with a co-financing Sugar Rehabilitation loan within the context of the commercial debt rescheduling. An IBRD draft economic report has been completed and presented to the GODR for comment. From the IBRD's view, the main content of a GODR medium-term economic program, as supported by preliminary conclusions of the draft report, should include:

1. More realistic trade and pricing policies, particularly exchange rate management through the gradual expansion of the parallel market, and improvements in agricultural pricing policies.

2. Additional tax measures to generate public savings, to support the recovery of public investment.

3. Rationalization of new public sector investment.

4. Elimination of the discretionality of present incentive law so as to improve the predictability of economic policies.

5. Actions to improve further the efficiency of the public sector administration, particularly of the CDE and of the CEA.

We believe these issues represent the basic GODR agenda for economic reform, and propose that the U.S. bilateral assistance program reinforce the IBRD discussions now underway. Discussions between the USAID and IBRD staff have resulted in the tentative agreement to coordinate our approaches to the GODR so as to avoid misunderstandings and conflicts, not only between USAID and the IBRD, but also between the GODR and each agency. The IBRD, assuming agreement with the GODR on a medium-term program, intends to concentrate its lending on projects with a direct impact on balance of payments and institutional development. This could take the form of a $150 million Structural Adjustment Loan (SAL), or lacking full agreement on conditions for a SAL, a $50 million export sector loan.

However, within this framework, AID will pursue a distinct policy dialogue with the GODR on a range of issues related to the three priority areas of AID involvement identified as key elements in revitalizing the Dominican private sector:

—Foreign Trade and Exchange

—Agriculture

—Human Resources

Each of these areas has its distinct set of circumstances and time frame. They are presented herein in rank order of urgency and priority. The discussion within each area will also be presented in rank order of importance.

In addition, this CDSS perforce concentrates its discussions on the 1984-1985 period. As will be seen, the USAID will be shifting its focus to the three priority areas. During this period of transition, several major analytical efforts will be undertaken to establish the specific parameters of each area. Results from these studies will be used to elaborate specific steps in the out-years beyond 1985. The broad policy guidelines, however, will remain as presented herein.

1. FOREIGN TRADE AND EXCHANGE

a. Objectives

It is generally agreed that one of the most difficult constraints facing the Dominican Republic is the shortage of foreign exchange. The Dominican economy, which is structured around import substitution, has not been able to cope with the recent adverse terms of trade of Dominican export commodities. Given the unpromising future outlook for reversal of the terms of trade, the Dominican Republic must find alternative means of earning more foreign exchange. With the approval of the

CBI, the country is in a position to promote a substantial increase in exports of non-traditional goods and services.

The major long-term goal of the USAID/DR in the area of foreign trade and exchange pertains to no less than the overall restructuring of the existing Dominican economy from import substitution to export expansion. In the short- to medium-term, however, our goal is to create a favorable export climate in which a large number of private entrepreneurs compete in exports of labor intensive goods and services, thus creating jobs and productive income for many unemployed Dominican workers.

To achieve this goal, the USAID/DR adopts a strategy that is aimed at making exports as profitable as imports. This will be done through foreign exchange policy changes, institutional reforms, and technical assistance. When this strategy succeeds, we foresee the Dominican economy transforming from the current import substitution mode to export oriented competitive economic structure. Under this new system, the profit margin per unit of production may be low, but the profit level and the rate of return to investment will be high due to large sales volume and high labor productivity. We foresee active foreign investment in the Dominican Republic to take advantage of profitable opportunities created by the strategy.

b. Policy Dialogue Agenda

Specifically, the policy changes and structural reforms we wish to bring about are as follows:

(1) All non-traditional exporters should be allowed to retain 100% of their earned foreign exchange. That is, the foreign exchange surrender requirement at the official rate to the Central Bank must be eliminated for all non-traditional exports. In early October 1983, the Monetary Board has made a giant step forward toward the elimination of the surrender requirement. For 83 items of non-traditional agricultural exports (melon, cucumber, etc.), the foreign exchange surrender requirement has been lifted. Although this is a positive step, we consider the revision too limited in scope and plan to push for the elimination for all non-traditional exports, including manufactured products.

(2) Reduction of administrative obstacles to export and import activities. Excessive documentation requirements for exports and imports for exports must be simplified and streamlined. In this regard, the CEDOPEX (GODR export promotion organization) has already simplified documentation procedures for obtaining export license from 18 to 4 essential documents. Similarly, to qualify for the benefit under the Export Incentive Law 69, exporters need to submit only 4 essential documents. The most difficult and important obstacle is in the Customs Office, which will take some time before effective measures can be devised.

(3) Reduction of prohibition of non-traditional exports. Certain commodities are prohibited from exports. The number of prohibited export items must be limited to the most essential ones.

(4) CEDOPEX should concentrate on becoming an export promotion organization by providing information on foreign markets and foreign consumer trends. It should also inform foreign buyers availability of Dominican products. In this regard, we plan to provide a long-term export advisor in CEDOPEX.

(5) Free zone firms should be allowed to purchase in dollars raw materials and intermediate goods from Dominican suppliers. The Dominican sales to the free zone should be considered as exports, and the exporter should receive non-traditional export benefits under Law 69.

(6) Encourage foreign investment for exports. The newly formed Foreign Investment Commission should supply expeditiously essential information necessary for making investment decisions. The USAID/DR will provide a long-term technical advisor to the Commission. The Commission also should investigate the foreign investment law to revise, if necessary, disincentives or impediments.

(7) Revision of the existing tariff schedule for imports should be undertaken. The average import duty rate as well as its variance must be reduced. Furthermore, special import duty exoneration should be restricted to insignificant cases.

(8) Public sector investment must be rationalized and overall development planning strengthened. The quality of analysis and

planning must improve, and the nature of government involvement must shift from interference to support of the private sector, especially exports.

(9) Current mining legislation. The new legislation, while an improvement over the past, still retains strong GODR participation, as well as limits on foreign exchange earnings conversions. Greater incentives must be provided.

c. Vehicles for Policy Dialogue

The major institutions in foreign trade and exchange, which are the vehicles for USAID policy dialogues, are in place and have ongoing relationships with AID programs and personnel.

The major public institution is the Secretariat of Industry and Commerce, which has titular precedence over two of the other primary institutions, the Dominican Center for Export Promotion (CEDOPEX), the Commission on Promotion of Foreign Investment (Commission), and the General Directorate of Mining (DGM). Each of these institutions is headed by young new, vigorous leadership drawn from the private sector and committed to taking steps to revitalize private sector participation in government, and to structural change necessary to expand investment and exports. In addition, the Board of Directors of CEDOPEX, nominally under the charge of the Secretary of Industry and Commerce, now meets twice monthly under Presidential direction.

The private sector institutions are the National Council of Businessmen (CNHE) and the Dominican Association of Exporters (ADOEXPO). Both of these organizations are led by prominent and respected private sector individuals who have ready access to GODR policy makers.

The GODR Monetary Board, comprised of a majority of private sector appointees, and its operating arm, the Central Bank, also constitutes a policy vehicle for AID dialogue. The current Governor of the Central Bank is a key policy advisor on financial and foreign exchange affairs, and is respected by the private sector, especially the banking community, and is the main architect of the debt rescheduling process.

These institutions, all of which are executing programs involving AID funds, provide an excellent institutional framework for policy dialogue.

d. <u>AID Interventions/Action Programs</u>

The proposed AID program in the area of foreign trade and exchange concentrates almost exclusively on the complementation of the CBI, focussing policy dialogue, and financial resources on increasing exports and investment. The following discussion lays out the USAID's action program for the FY's 1984 and 1985:

(1) The Dominican Republic has taken some important steps towards improving the environment for development of exports.

In order to assist the GODR in continuing this progress, <u>an Export Sector Assessment will be carried out in FY-1984.</u> Local currency generated under the ongoing $49 million ESF loan program will finance the assistance of a local consulting firm, and AID PD&S funds will fund the cost of the firm of Arthur D. Little in this effort.

(2) Using the Export Sector Assessment, AID during FY-1985 will undertake <u>an Export Promotion and Investment Project,</u> estimated at $12 million, designed to address policy constraints, and deal with currency control and promote free zone expansion. The project will provide a $8 million credit to the <u>Export Promotion Fund of the Central Bank</u>, which will increase the volume and smooth the flow of credit and investment to and within areas of the private sector which are not adequately financed for export promotion. <u>Credit will be available for investment in special export related facilities</u>, such as fumigation and cooler warehouse facilities, and for construction of infrastructure and plants for free zones. Emphasis will be placed on satisfying pre-export, short-term, working capital needs for private sector production of non-traditional exports, especially to small and medium enterprises which normally receive only limited help from the formal banking system. Grant funds ($4 million) will also be provided to finance: <u>(a) policy analysis aimed at improving the climate for export, (b) investment promotion to attract foreign capital and stimulate domestic investment in export oriented projects, (c) research and identification of investment opportunities and development of new markets, (d) administrative and institutional upgrading including training for public and private organizations involved in export promotion, and (e) long-term technical assistance for key</u>

institutions involved in foreign commerce and investment, such as the Investment Promotion Commission.

(3) The agricultural economy is dominated by sugar and the GODR is very reticent about diversification. As a result, investment and development in non-traditional agro-industrial activities have been limited by the lack of any concerted program and by an investment climate which has favored import substitution and which has been characterized by contradictory policies and unnecessary regulations. To address this constraint, AID will start a $9.8 million Agri-Business Promotion Project in FY-1984 aimed at creating a favorable investment climate for export oriented industries. Critical issues which hamper the development and growth of agri-business will also be addressed through the implementation of a variety of activities, including the provision of: (a) credit for investments in plant and equipment, production, and marketing; (b) technical assistance to conduct pre-feasibility and/or feasibility studies aimed at identifying new markets and investment opportunities; (c) pilot activities to identify and develop non-traditional products for exports; and (d) training, seminars, and demonstrations to introduce new varieties and farming techniques to small growers through the expertise of agro-business firms.

In addition to the $9.8 million agri-business project anticipated to be initiated in FY-1984 discussed above, approximately RD$19 million in local currency counterpart will be made available under the FY-1984 ESF loan program. Its purpose will be to increase the capitalization of the credit facility (FIDE) within the Central Bank, thus increasing the volume of credit to the private sector for expansion of agri-business and export activities.

(4) Overall, the mining sector possesses considerable potential as a source of future output and foreign exchange earnings or savings. The country is judged to have substantial untapped potential mineral resources. Preliminary studies suggest significant copper deposits in the central part of the island and the possibility of significant copper and manganese further to the west. Alluvial gold occurs in various parts of the island, and various non-metallic minerals are abundant

in the southwest. The recent discovery of commercially exploitable lignite deposit holds out a possibility for a reduction in oil imports, and exploration for petroleum is being undertaken in several parts of the island, thus far without success (although natural gas has been found). More detailed studies are needed, however, for the country to be able to effectively exploit this potential export resource. Accordingly, AID proposes to finance preliminary studies by the U.S. Geological Survey aimed at assessing the potential for additional exports of minerals as well as identifying policy constraints which impede exports or investments in the mineral sector. AID expects to finance, beginning in FY-1984, a $5 million Minerals Export Promotion Project aimed at producing a complete classification of all mineral resources in the Dominican Republic as to the type, location, estimated reserve quantity and quality, and commercial viability. It is expected that this classification will become a base for attracting foreign private investment which will enhance the exports of minerals. In addition, the project will assist the GODR to review and reform the mining sector to meet its future need.

(5) A fundamental requirement of business is the existence of the basic infrastructure necessary to produce, transport, and market their products. In many areas of the Dominican Republic, these facilities do not exist, thus inhibiting not only the expansion and development of these areas, but also the private sector. In order to assist the GODR in removing this basic infrastructure constraint, GODR counterpart from the FY-1984 AID ESF loan will be programmed for this purpose.

(a) The RD$10 million originally allocated for "productive infrastructure" under the original 1982 ESF program as counterpart to major multilateral funded infrastructure projects has been disbursed. The additional RD$5 million provided under the 1983 $8.0 million amendment to this ESF program for this purpose will be fully committed shortly. There still exists, however, a substantial need to provide counterpart resources to support other infrastructure projects which are critical to the expansion of the Dominican private sector. The GODR estimates that there exists an immediate need for approximately RD$27 million to support various critical infrastructure projects funded by IBRD, IDB, and AID. Accordingly, it is expected that RD$10 million, to be provided under the FY-1984 ESF loan, will be utilized in support of productive infrastructure, including a critical highway project funded by IBRD and rural roads projects funded by IDB and AID.

(b) The GODR and the private sector have created free zones in different parts of the country to stimulate industrial development. Four free export zones are currently in operation (two privately owned and managed). Some of these free zone sites offer considerable opportunity and potential in the short-term for increasing employment and foreign exchange. Thus, the GODR intends to use up to RD$2 million, made available under the amendment to the FY-1982 ESF program, to expand the Puerto Plata free zone facility. There still exists, however, much opportunity to develop the country's free zones. Accordingly, RD$6 million in local currency proceeds will be made available under the FY-1984 $40 million ESF loan for free zone development.

(6) Activities to establish a viable GODR Export Promotion Institution:

(a) From counterpart resources made available in conjunction with the CBI loan, RD$100,000 was made available in support of CEDOPEX operations. From the amendment to this loan, RD$1 million is earmarked to support a series of key promotional activities to be carried out by CEDOPEX.

(b) During FY-1984, the Mission plans to arrange for the short-term training of up to four CEDOPEX staff members. This training will be financed with AID PD&S funds, and will be carried out by a U.S. training institution specializing in trade development. The training will cover the planning, design, implementation, and evaluation of export activities.

(c) Under the AID-funded FY-1985 Export Promotion Project, the Mission plans to provide technical assistance to develop the institutional capability of CEDOPEX to organize and carry out effective export promotion activities. This technical assistance will likely include both short- and long-term advisors to help CEDOPEX structure an urgently needed program to identify potential export markets, products, and distribution systems.

(d) In order to help CEDOPEX identify the export production capability available in the Dominican Republic, a study will be undertaken during FY-1984 of the information included in the recently completed small industry sub-sector assessment. The current study, also financed by AID, will identify export opportunities in terms of products and plant capacities.

(7) Activities to establish a strong GODR Investment Promotion Commission:

(a) The National Investment Commission was established by President Jorge Blanco in June 1983. In support of its operations and activities, RD$100,000 from the counterpart funds resulting from the initial CBI program were provided. Recently, the GODR has appointed an executive director and sub-director, both of whom have had considerable organizational and other appropriate experience. The Commission is now hiring staff and developing an implementation program. In support of its continued development and expansion of activities, the GODR and AID are prepared to provide additional resources to this organization.

(b) Before the end of November 1983, the Investment Commission will complete its detailed work program for 1983-1984. It is expected that this plan will include a member of activities which can be financed from the local currency proceeds available under the FY-1984 $40 million ESF loan. These activities include: the development of investment opportunity information and assistance packages for distribution to potential foreign investors, establishment of a data bank to provide information on existing Dominican firms and identification and promotion of potential joint venture participants, development of an information system to promote free zone development, and preparation of studies of the legislative and administrative constraints to investment.

(c) During early FY-1985, it is anticipated that AID will finance with PD&S (or project grant) funds the short-term training of up to two Investment Promotion Commission staff members in the basic skills and techniques for promotion fo foreign investment. This training may be provided through a U.S. training institution specializing in trade development.

(d) During FY-1985, AID will finance, under the Export Promotion and Investment Project, long- and short-term technical assistance to develop the institutional capability of the Investment Promotion Commission. Consultants will assist the Commission in developing and implementing immediate impact action programs to stimulate foreign investment.

(e) The Mission will also make available another RD$1 million from counterpart resources resulting from the FY-1984 ESF loan to finance a series of essential studies needed to support the development of important private sector initiatives.

(8) PVOs bring a unique perspective to development and can provide a grassroots dimension not always attainable under regular loan/grant programs. There is considerable scope in the Dominican Republic for such activities. A number of private U.S. organizations are currently active here in various fields, including agriculture, small business, housing, health, and education. Further, there are a number of Dominican private development institutions, many of which are highly qualified to develop and implement projects, which support CBI objectives. Accordingly, USAID plans to program an additional RD$4 million in counterpart to: (a) expand the ongoing CBI PVO program, and (b) explore with the PVO community possible new OPG activities that will promote CBI goals and complement and reinforce the Mission's program.

(9) Activities to develop a core group of entrepreneurs:

(a) The UCMM School of Business and Public Administration (Project No. 517-0157) opened its doors in August 1983. The school now has a staff of 6 Dominican and 3 American professors. The first class includes 110 students (60 business and 50 public). During the next 18 months, the construction and equipping of the additional facilities (financed by RD$3 million of FY-1982 ESF proceeds) should be completed, the student body should have increased to 220, and the first class of MBA's should have graduated. In addition, the school should be offering 10 Executive Training seminars each year to the highest levels of entrepreneurs, business managers, and public officials. USAID will continue to finance this ongoing project through FY-1989 for a total of $5 million.

(b) Under the LAC Regional Training Project, $40,000 was allocated to finance short-term management courses in the U.S. for participants identified by the American Chamber of Commerce. Participants are now being identified and placed. During FY's 1984 and 1985, the Mission expects that both short- and long-term training activities will be expanded to include more private sector participants.

(c) Export promotion seminars will be held involving the Dominican-American Chamber of Commerce, the Association of Industries of Herrera, the Association of Industries of the Dominican Republic, the Association of Dominican Exporters, the Dominican Export Promotion Center, the Chicago Association of Commerce and Industry, and AID.

(d) The ongoing Small Industry program will continue the successful experience of the PROAPE Micro- and Small Industry Trade Fair in Santiago and the Dominican Development Small Industry Trade Fair in Santo Domingo. It is anticipated that these fairs will be repeated on an annual basis. As the Micro- and Small Industry program increases in size geographically, with Technical Assistance Centers being established in secondary cities, it is anticipated that such fairs will also be held in those secondary cities in the near future.

(e) Under the AID-funded Small Industry program (Project No. 517-0150), it is expected that short-term technical assistance will be provided during FY-1984 to improve the design of handicraft products, i.e., textiles, straw products, ceramics, etc. Also, assistance will be provided to help identify foreign markets and channels of distribution.

2. AGRICULTURE

a. Objectives

The importance of the agricultural sector as a source of employment, output for domestic consumption, and export earnings is substantial. Some 2.8 million people live in rural aras in 340,000 farm families. Agriculture directly employs slightly more than 60% of the nation's employed labor force. In recent years, the production of all agricultural commodities has tended to stagnate. During the period 1976-1980, output of non-export agricultural commodities increased by 2.8% annually, while production of sugar, coffee, cacao, and tobacco actually declined by about 1.5% per annum. Within the agricultural sector, the sugar industry is by far the key component.

Public participation in the agricultural sector bulks large because of CEA's predominance in the sugar industry. Sugar export earnings have been highly variable in recent years due to world price movements, Dominican success in anticipating some of these movements, and more recently the U.S. quota system which yields a higher than world price to Dominican producers (in 1983, approximately 13 cents per pound versus 7.8 cents per pound on the world market). The long-term outlook for Dominican sugar export earnings is inauspicious. These negative trends relate mainly to increasing U.S. production of sugar substitutes.

The agricultural sector's overall potential is highly dependent upon the adequacy of incentives (including prices), and the provision of infrastructure and services to thousands of individual farmers. Estimates of private investment in the sector show a decline in private investment in recent years, and this decline has been occuring at a time when the public sector has been making massive investments in the sector, particularly in irrigation infrastructure.

Also, since the 1960's, there has been a steady and major expansion of public sector agencies, as well as increasing interventionist policies which have resulted in a bloated and inefficient public bureaucracy administering a wide range of uncoordinated and often conflicting set of programs at increasing cost. There are now eight large autonomous public institutions administering major development programs in the agricultural sector. Recurrent costs are exceeding the GODR's ability to provide adequate counterpart to ongoing programs or provide adequate incentive to public employees. Much of the energies and resources of these institutions and staff have been directed at the provision or distribution of free or subsidized inputs to agricultural producers, in part to compensate for a wide array of artificial price incentives designed in part to protect urban consumers, and in part to implement an approach which involves a predisposition of public sector involvement in agricultural production and marketing. There is a pressing need to reassess the agricultural sector's priorities and policies and improve its performance within a framework of increased rural incomes and balance of payments considerations.

Finally, expanded agricultural production must depend upon an adequate resource base. An extensive Country Environmental Profile (CEP) documented the widespread and increasing rural deterioration of the natural resource base and predicted that, if not arrested, a Haitian--type situation within two decades. The CEP analysis gave by far the highest priority to the watershed degradation problem.

b. Policy Dialogue Agenda

The overall development strategy in the agricultural sector is based on the principle of comparative advantage of the Dominican agricultural production in the framework of an open economy. USAID/DR will concentrate on the development of export markets for farm products that have relative advantage in terms of price and quality in the world market. These products include fruits and vegetables, such as melon, pineapple, pepper, cucumber, garlic, tomatoes, etc.; basic food grains, such as rice, beans, plantains, root crops, etc.; and import substitution crops, such as sorghum, peanuts, soybeans, and corn. A three-pronged approach will be followed in pursuit of export market development: market feasibility studies, applied research through variety trials and commodity testing, and technical assistance to agri-business firms. In addition, USAID/DR will provide financial support to agri-business organizations, both domestic and foreign, which are engaged in promotion of business ventures to produce and market the above mentioned products, and will directly assist agri-business firms through provision of credit for investment (see section on Foreign Trade and Exchange).

The ultimate outcome of the USAID/DR strategy in the agricultural sector is to create a large number of efficient private small and medium commercial farmers who can compete in domestic as well as world markets for the production and export of fruits, vegetables, and basic grains without public sector nterference. These commercial farm entrepreneurs will be encouraged to adopt new product varieties that will yield the highest return for their nvestment. This will require the creation of a more favorable agricultural production environment.

Accordingly, we propose to pursue structural change and policy reform in the agricultural sector in the following areas: Pricing, Policy and Administrative Reform, Rural Savings and Investment, Natural Resource Protection, and Land Use Planning.

(1) Agricultural Pricing: The USAID/DR's ultimate goal in agricultural pricing policy is no price control at all. Price control should be phased out. Price will be determined by market forces with minimal interference from price stabilization and control institutions. In the short- to medium-term, however, USAID/DR will encourage GODR to adopt a price policy based on rationalization of cost-price determination and as much as possible on indirect measures.

The USAID/DR agricultural pricing strategy consists of three basic approaches:

(a) No official foreign exchange will be made available to INESPRE. Instead, INESPRE will purchase foreign exchange necessary for imports in the parallel market. At the same time, USAID/DR will push for revision of INESPRE's monopoly for imports of certain grains. Private sector importers should be allowed to provide meaningful competition for importation of grains that are prohibited now.

(b) The Office of Price Control should be redirected and reorganized to rationalize consumer price control.

(c) A price policy unit will be established to conduct analysis on production costs and profit margins to provide sufficient profit incentives to farm producers.

(2) Agricultural Policy: The recent history of public involvement in the agricultural sector is characterized by a multiplication of agencies embarking on ever expanding activities. The most prominent organizations are involved in such diverse activities as resettlement of farm families, establishment of commercial outlets for agricultural commodities and production inputs, provision of machinery services, production of

improved seed, purchase and marketing of agricultural products and management of farming operations. While these undertakings have achieved some positive results, the efficiency and necessity of conducting them through public institutions can be questioned. Moreover, the diverse interests of the various institutions involved have led to countervailing interventions which have placed a drag on the performance of the agricultural sector as a whole. In some cases, public interventions intended to promote development have interfered with private sector initiatives; in others, public interventions have served as implicit taxation of agricultural production.

The USAID's goal in agricultural policy is the restructuring of the GODR policy making apparatus to orient policies and programs towards increased private sector investment and involvement. The first step is to strengthen the role of the previously moribund National Agricultural Council (CNA). The second is to assist the CNA establish national priorities for agricultural development for the mid-1980's and beyond and establish means by which these priorities are incorporated within the diverse public sector entities now operating. The third is to assist the GODR to restructure its research and extension functions to incorporate an inter-disciplinary approach involving universities, the private sector, and the State, somewhat akin to the U.S. Land Grant system. The central theme is that public sector institutions and policies concentrate on activities legitimately assigned to government, and that the past propensity to seek a public sector solution to every problem be replaced by a private sector oriented philosophy.

(3) Rural Savings and Investment: Private producers require credit. Today, only approximately 20% of the nation's farmers receive institutional credit, largely through the Agricultural Bank. The GODR, AID nor the other donors are able to provide adequate credit for small commercial farmers from public funds, which have been the primary source of capitalization to the Agricultural Bank. Additional necessary capital for investment in agricultural production can be mobilized through increased incentives to encourage savings in rural areas. Until recently, low interest rates on savings (5% annual) encouraged capital flight from the countryside to more lucrative urban investments or abroad. The

Monetary Council recently increased regulated interest rates somewhat for formal financial institutions. There are reasons to believe that these increases may not be adequate. Accordingly, the USAID's goal is to seek a change in the country's interest rate policy to improve the viability of rural financial institutions and expand access of small and medium commercial farmers to savings and credit services. This will require authorization by the monetary authorities to allow rural credit institutions to increase the rate of interest they charge over the current maximum legal rate of 12%. At the same time, these institutions will need to be reorganized and strengthened to offer deposit facilities and manage expanded credit portfolio. These changes are expected to be gradual and the result of experience gained over a period of years.

(~~3~~ 4) National Resource Protection: The essence of the natural resource degradation problem is that most agricultural producers are "mining" the resource base for short-term needs and profits, with little consideration for its disasterous impacts on near future generations of both producers and consumers. The CEP provided the country with its first comprehensive analysis of environmental degradation. Only 14% of the country remains in forest. Approximately 22% of the land area is considered to be seriously threatened by high erosion rates. Massive watershed erosion on the order of 95 to 500 metric tons per hectare per year is literally drowning the reservoirs with sediments. In many watersheds erosion is so advanced that destruction of the entire soil base could easily be completed within two decades. This is a moot point, however, since most fertile soil, which is only a few centimeters in depth, would be washed away in the next few years. The impact of this soil and water, which literally roars off the hillsides during periods of high rainfall, causes great damage downstream. The silt and gravel-laden waters scour their way downstream causing extensive damage to farmer's fields, roads and bridges until they are slowed by dams or lose their kinetic energy in the flat lands. There, they deposit silt, rocks and debris, which fill in reservoirs and deposit thick layers of silt in the irrigation canals. The resulting damage to agricultural productivity, energy generation, and overall environmental conditions is so great as to merit immediate and emergency measures. AID has assisted the GODR in establishing the programs and methodologies necessary to attack this national problem as a central part of its agricultural strategy since 1980. Priority on this CDSS will be given to completing the effort in a timely and efficient manner.

The remaining structural change required in this area is two-fold.

The first reform element involves changes in human behavior which must be effected through training, demonstrations, development of alternative energy sources, new techniques, methodologies, cropping patterns, etc. These are incremented in nature, and middle- to long-term in their impact. The principal resources of most concern--soil, water, and forests--are inseparably combined in space and as objects of misuse. However, the institutional structure responsible for their stewardship is divided, uncoordinated, and often works at cross purposes. At the same time, the involvement of private sector entities and the public in decision--making concerning natural resources utilization and conservation is extremely limited. Once public interest is effectively constituted in the process of natural resources decision-making, the competing objectives of resource utilization versus conservation can be brought into play. The opposing interests represented by diverse users of land, water, and forests will inevitably define the policy agenda. That is, short-term interests of hillside farmers must be reconciled with long-term interests of society in a stable resource base; and immediate needs for irrigation water must be reconciled with those of hydroelectric power. Issues such as these, implicitly involve natural phenomenon and biological complexities which almost exceed comprehension, yet they must be addressed for fear of devastating consequences. For this reason, high priority has been assigned to the natural resources theme.

The second element of reform involves changes in government regulations and enforcement. These include a revision of the Forestry Law to allow tree farming for profit, elimination of corruption and abuses in application of current tree cutting regulations, and development and application of water-user rates in irrigation. The increased public comprehension of the issues described above, as well as the establishment of priorities and programs which allow competing interests to express their needs fully and defend their institutional and functional interests within an open dialogue, will aid greatly this process.

(4) Land Use Planning: The sugar industry represents the largest source of foreign exchange earnings for the Dominican economy; it is the largest user of cropland and the major employer of agricultural workers.

Sugar and its derivatives generated an average 57% of the total value of exports over the 1971-1975 period, although over the 1976-1980 period earnings have been only 33% of total exports. Wide variation in sugar prices during both periods caused earnings to decline over 50% in poor years versus good years. The average value of sugar exports in current dollars was approximately $300 million in the 1971-1975 period and $250 million in the 1976-1980 period. The 1981 earnings were approximately $550 million, in 1982 they had dropped to $309 million. From 1971 to 1981, the area devoted to sugarcane expanded to an estimated 275,000 hectares or 15% of national cropland area.

There are an estimated 45,000-50,000 workers involved in the field harvesting operations of the sugar estate. At least half are Haitian workers contracted for the harvest season. The sugar milling operations and permanent management provide employment for another 40,000 persons. In addition, backward linkages with other sectors of the economy may provide as many as 40,000 jobs.

World market prices for sugar have hovered around 7 cents per pound level for the past year. Although it rose lately to 11-13 cents per pound indicating a recovering world market, it will probably never reach the highs of years past. In addition, the continued erosion of the sugar market by high fructose commodities (HFCs) seems to indicate a necessity for the Dominican Republic to seek out alternate uses for some of the estimated 275,000 hectares now planted to sugarcane. Estimates of how much of this land could be diverted to other agricultural uses range from 15% to 50% depending on the alternative uses of the land. It is important to point out that none of the alternate uses have been studied sufficiently to determine if they would provide the same foreign exchange earnings and employment opportunities as sugarcane. The subject itself is highly controversial, with many influential sectors and individuals in the country strongly opposed to shifting land out of sugar into other crops or uses. There has been some discussion about the need to diversify, but this has generally been confined to the need/interest in alcohol plants and increasing the production of sucro-chemical. Given the high cost of initial investment in such activities, diversification of the industry along these lines seems unlikely in the near future.

Recently, the CEA has agreed to a joint venture with United Brands Company in a scheme to raise pineapples for export using land currently devoted to sugarcane production. These types of opportunities need more promotion and investigation of other crops/activities which could take the place of sugarcane need to be thoroughly investigated. The goal of the USAID is to seek greater comprehension of the scope and nature of the problem and provide technical and policy analysis necessary to establish a public dialogue.

In terms of concrete measures, the USAID will promote increased investment in the type of agri-businesses represented by the pineapple venture which, because of their profitability, will result in a gradual shift of sugar lands to higher value crops. The relationship with IBRD lending to CEA will be an important element. IBRD is seeking greater efficiencies in CEA operations and a rise in the domestic price of refined sugar sufficient to eliminate the current subsidy. AID fully supports this effort.

c. Vehicles for Policy Dialogue

The major policy vehicle in agriculture is the National Agricultural Council (CAN) which is presided over by the President twice monthly in differing locations around the country. The CAN brings together the heads of the major public sector organizations operating in agriculture. It is expected that all of AID's policy dialogue in agriculture will involve the CAN, including pricing, administrative reorganization, natural resource protection, and land use planning.

While a member of the CAN, the National Price Stabilization Institute (INESPRE) wields sufficient influence so as to merit special attention. INESPRE is the key institution in setting agricultural producer prices and controls most agricultural imports, including PL-480 and CCC. Policy dialogue directly with INESPRE on these issues will have high USAID priority, although much of our dialogue will be channelled through the Technical Secretariat of the Presidency (STP), which is the coordinating GODR entity for discussions on PL-480 issues. Within STP, a price policy unit will be established. The Office of Price Control in the Secretariat of Industry and Commerce has also requested AID assistance in liberalizing current price control regulations. As can be seen, the dialogue on pricing will be complex, involving several different GODR entities, and will most likely raise issues which will be addressed at the policy level by the CAN under general agricultural policy considerations. From the USG side, the Embassy has a PL-480 Working Group, under the DCM, involving AID, AGATT, and the Economic Counselor to coordinate the USG position on PL-480.

Rural Savings Mobilization will involve a multi-institutional arrangement led by the Central Bank, and involving the Monetary Board, the Agricultural Bank, and the Credit Cooperative Movement.

d. AID Interventions/Action Programs

Apart from those agricultural-related programs in agri-business described above, the USAID plans the following Action Program for FY's 1984 and 1985 in agriculture:

(1) Pricing and Policy: GODR price policies have either ignored the effects of inflation on agricultural prices or attempted to combat inflation through agricultural price controls, which have been costly in terms of loss of agricultural production. In addition, an over-valued official exchange rate not only became a tax on export products but introduced a bias towards imports. The GODR has recognized the need to revise these policies as a pre-requisite to production increases. In order to provide a mechanism for facilitating the required analysis, during FY-1984 AID will finance the Agricultural Policy Analysis Project (No. 517-0156) with $1 million in grant funds. This project will work to strengthen the CAN on a reorganization of the public agricultural sector.

Included in this effort will be technical assistance to develop an adequate capacity to provide unbiased price data and analyses to decision-makers. To assure the capacity to use this analysis, formal and non-formal training will be made available to decision-makers. The basic activity will be the development of a GODR Agricultural Policy Analysis Unit, which will require a core staff of well-trained economic, agricultural economic, and statistical analysts. Short-term technical assistance and on-the-job training will be provided to the core staff in order to reach project objectives. Some analysts (4 to 6 at a cost of about $25,000) will receive training either locally or overseas, to ensure the number of critical professionals necessary for long-range development. Seminars and workshops will be conducted for policy makers as a means of improving their understanding of policy matters affecting the agricultural sector in the Dominican Republic. The issue of land use planning, especially with regard to sugar production, will be given special emphasis as a major policy area to be studied.

In addition, this project will provide technical assistance to the Secretariat of Industry and Commerce's Office of Price Control to assist them in their desire to liberalize current policies and programs. Also, the FY-1985 PL-480 Title I program of $23 million will be leveraged to seek private sector imports of certain grains in lieu of INESPRE, thus denying INESPRE a portion of the income it currently uses to subsidize its interventions in the market place. Use of PL-480 proceeds will also not be programmed to fund GODR activities that result in government activities which are more properly left to the private sector.

Finally, the ongoing Rural Development Management Project (No. 517-0125) will receive incremental funding in FY-1984 to complete the development of case studies designed to focus the attention of sector decision-makers on such key issues as land use, food price policy, and agricultural policy in general.

(2) In order to increase investments in agriculture and improve agricultural productivity, an effective program of agricultural research and extension is needed for crops of primary importance to the national economy. While the GODR has made significant investments to

develop its research and extension capability, the existing research data base and extension capability are inadequate to support the needed increases in agricultural production. The cause of this situation has been identified as the inability of the existing public sector system to effectively manage, coordinate, and carry out the required research programs. Accordingly, in FY-1985 AID will finance the Agriculture Research and Extension Project (No. 517-0180) with $5 million in loan and $1.5 million in grant funds. The project is aimed at developing an interdisciplinary private sector research capability in the Dominican Republic akin to the U.S. Land Grant University research/extension system.

(3) The possibility for increased rural savings and investment will be tested under the Rural Savings Mobilization Project (No. 517-0179) which comes on stream in 1984 and whose results will be evident in 1985. Three branches of the Agricultural Bank and three rural cooperatives will have tested the concept and established the feasibility of the concept. Given favorable results, and the willingness of the GODR to agree to the necessary policy changes, we expect to propose a major project in this area for start up in FY-1986.

(4) Natural resource protection is being assisted under a series of ongoing AID loans (NARMA No. 517-0126, and Water Management No. 517-0159), and a third loan scheduled for FY-1984 in Forestry (No. 517-0173). This third loan is designed to complete the watershed strategy recommended by the CEP, and leave in place operating programs involving upper (NARMA), lower (Water Management), and middle (Forestry) watershed management. The scale of the Forestry loan, however, is being reduced from $10 million to $6 million to allow for an FY-1984 start on an agri-business promotion loan, i.e., one year earlier than originally scheduled. This is to recognize that with the passage of the CBI, an earlier effort is called for; however, we believe the last piece in the watershed package should be done before moving on. This will strengthen the Directorate General of Forestry and provide AID with a policy instrument to affect those GODR policies which are impeding rational use and development of the country's declining forestry resources within an environmentally sound program.

3. HUMAN RESOURCES

a. Objectives

The major long-term goal of the USAID/DR in the area of education is to have an educated population which is functionally literate, equipped with the specialized skills necessary for the country to produce and compete competitively in foreign trade, and aware, involved and supportive of the democratic values which guide the country's development. The population must also be sufficiently informed so as to be able to support those necessary reforms and changes to the economy and society at large that the 1990's will require. At the least, this will require a complete restructuring of the public education sector, especially at the primary level.

b. Policy Dialogue Agenda

To achieve this goal, the USAID/DR adopts a strategy which aims at providing at least six years of primary school education to all children by the year 1990. Specifically, the policy changes and structural reform that will form the basis of our policy dialogue in the area of primary education reform are as follows:

(1) Administrative Structural Reform

The present Secretariat of State for Education, Fine Arts, and Worship (SEEBAC) structure is the result of almost 30 years of growth through laws, decrees, internal rules, resolutions, departmental orders and secretarial circulars, in response to diverse and sometimes contradictory national and international demands. SEEBAC has almost 30,000 teachers and 2,000 employees. Only within the last six months has a 4-year education plan been published for the 1982-1986 government. The issues for structural reform are:

(a) Duplication of Services: Over one-half of the national SEEBAC offices (78) maintain a direct relationship, through reports and supervision, of local schools, while 30 offices are responsible for teacher training.

(b) Over-Centralization: Only about 200 technicians are posted at 13 regional district offices.

(c) Too Broad A Scope of Work: SEEBAC is responsible for education, fine arts, and religion. The demands of these widely divergent sub-secretary activities not only place a tremendous administrative burden on senior staff, but also lack lateral salary relationships.

(2) Reordering of Internal SEEBAC Primary Expenditures:

For 1980-1981, SEEBAC direct expenditures per rural primary student were DR$46.17 while expenditures for an urban student were between DR$72.34 and DR$105.20. Further dichotomous urban/rural distribution patterns were present in repetition, promotion, and average class size. This rural inequity was butressed by a SEEBAC budget, which allocated only 50% of its total resources to primary education, although primary school accounted for 80% of the enrollment. USAID policy discussions will focus on a achieving 7% increase of primary school funding and a leveling of input and output per student costs.

(3) Reform of Teaching Methodology

The present curriculum allows the classroom teacher a great deal of latitude in unit planning. However, over half the teachers are not certified, and a disapproriate number of these are in rural schools. The USAID will focus activity on creating highly structured unit plans for the first four grades.

Equally important to the strengthening of the private sector is the provision of skills training to individuals at the several following levels of the educational structure:

-- Vocational/Technical Training. The ability of Dominican exports to compete in world markets is directly dependent upon the skills employed by the Dominican workers in transforming raw material and semi-processed goods into exportable surplus. The need for new skills will increase dramatically as new CBI-oriented foreign and domestic investment employs new technologies, methods, machinery, and materials. The policy reforms and structural adjustment requirements in this area are largely in place. The country has just recently established an Institute for Vocational Training financed by a payroll deduction plan and jointly owned by the workers, owners, and the State. IDB is financing a major physical expansion of public vocational schools and public college level technical course work. There is a well-established network of secondary level private vocational schools in agriculture and industry which, while suffering from a shortage of resources, offer a wide range of skills training to Dominican youth.

— Management Training. Today's Dominican private sector has its roots in a turn-of-the-century immigration from Europe. Family businesses were founded in some basic industries but the bulk of business enterprise was in the commercial import sector. In the 1960's, the business and industrial sector turned to import-substitution and that is the predominant activity of today's growing industrial sector. The management mode of many of the larger concerns, however, remains family-oriented. To compete, the Dominican private sector must depend upon a managerial cadre drawn from all sectors and levels of society and versed in modern management techniques. The structural reform required here has begun. The Catholic University (UCMM) has created a new graduate school of administration, and has signed an AID-funded long-term contract with the University of South Carolina School of Business. Classes began in September 1983. The school has a private sector consultation committee, and will have a research institute and a high-level management center to reach out to the private sector. Construction of a $3 million modern specialized facility with state of the art computer and library services will begin in January.

— Consensus for Reform. One of the most critical needs of Dominican society is to face imminent changes, inter alia, in industrial development, strategy, macro-economic policy and structural adjustments. The country faces these challenges with a nascent democratic system which, in the past, has worked in favor of a series of incentives and special privileges for special interest groups. The emergence of a functioning democracy, including an independent Congress, offers opportunity for a broader-based reform effort. However, there is the threat that unless these democratic institutions are strengthened to fulfill a responsible role, necessary change will be stymied or misdirected. The Congress is a critical element. Both chambers, the State and the House, are 90% filled by politicians who have no prior legislative experience. There are no staff resources, no constituency services, no offices, no reference services, etc. Yet, Congress is required to analyze the budget and ratify all legislation. Most legislators follow their particular party bloc line, but the Congress will become increasingly segmented as the left increases its influence and the two traditional parties suffer increasing factionalism. A program to educate and support public elected officials, in effect, is an effort to make them responsible partners of the Executive. Already, the Jorge Blanco administration is encountering opposition in Congress to any further reform efforts. If this trend continues, it is likely that the next two years of the administration (1984/1985) will see a growing and unfortunate confrontation between the Executive and Legislative branches sufficient to detail any major reform effort. The USAID believes it is appropriate and necessary that the bilateral assistance program include an activity which seeks to improve the human resource base of elected officials.

Structural adjustment and policy reform requirements are centered largely on the need to create a source of training and expertise to allow elected officials and their staff to draw upon before, during, and after their tenure in office. A private university (UCMM) has initiated such an effort, based upon an AID-financed 3-day legislative orientation session for 125 new Congressmen. The evaluation of that course reinforced the need for this activity. Ironically, the need for policy dialogue on many of the issues contained in this CDSS will be affected by the ability of Congress to act.

Related to this is the need to increase the level of economic sophistication within the government and the private sector to strengthen the ability of the country's planners and executives to comprehend the macro-economic forces at play and adjust domestic policies in the country's best interests. This is required in the short-term and will involve an immediate recruitment and selection of up to 40 Dominican professionals for graduate economic studies in the U.S. over the next three years.

c. Vehicles for Policy Dialogue

The policy dialogue vehicle in education will be the Secretariat of Education in the public sector, and the UCMM graduate school of business private sector consultation committee.

d. AID Interventions/Action Programs

The Mission's education program is directed basically at: (1) improvement in basic education through traditional and non-traditional (radio) methods, and (2) provision of skills and management training in areas of greatest need. An emphasis in basic education is still required in the Dominican Republic, where improvement in the literacy rate has lagged behind that of its neighbors. Unlike most AID education programs in Latin America, which have up to 20 years active involvement in primary education, the primary education program in the Dominican Republic, which began with an Education Loan (Project No. 517-0119) in 1979, is relatively young. In response to recommendations of the 1977 Education Sector Assessment, the loan supported activities in curriculum development, teacher training, and school construction, which have met with some initial degree of success, but constitute only the beginning of meeting the needs of this critical but neglected sector. A $8 million follow-on project (No. 517-0172) will begin in 1984, to continue the reform effort in administrative planning, institutionalization of teacher training and supervision, creation of local organizations to provide financial support to schools, and construction and use of low cost media.

Basic education is also being disseminated through a radio education program currently consisting of a program funded through FY-1984 for adult education in one region (Project No. 517-0163), and a centrally-funded primary education program in another region (Project No. 936-5807), which is scheduled to require funding through FY-1986. Through the innovative use of this technology, the cost of basic education per beneficiary is being reduced considerably; pointing to strong possibilities of replication within the Dominican Republic as well as in other countries.

Specialized skills training is being addressed through three ongoing programs: (1) vocational/technical training, (2) management training, and (3) participant training. Vocational training is being strengthened through support to an educational credit institution and vocational education institutions (Project No. 517-0127), and through the establishment of a center providing technical training for urban women (Project No. 517-0146). Both are scheduled for FY-1984 funding. For management training, a local university is now linked to a U.S. university for a long-term program, which will provide a local capability to train public and private sector leaders at the post-graduate level (Project No. 517-0157). This project will require funding through FY-1989.

Participant training is a major component of almost all AID programs in this country. For FY-1984 and FY-1985, USAID programs will finance a total of 109 short-term and 82 long-term trainees. This includes Dominicans directly involved in program execution as well as participants selected under three programs exclusively directed at training. The first is an FY-1983 $5 million Agricultural Training Loan (Project No. 517-0160) to train the next generation of agricultural scientists at the M.S. and Ph.D. levels. The second is a proposed FY-1984 program (Project No. 517-0180) to provide graduate level Policy Analysis Training, mostly in the area of macro-economics and public finance to strengthen the country's capacity to analyze and confront the serious economic problems facing the country for the foreseeable future. The third is the LAC regionally-funded training program (Project No. 598-0622) which provides U.S. training to Dominican professionals.

Finally, the USAID proposes to fund in FY-1984 an innovative program (Project No. 517-0189) directed at the legislation branch of the GODR. Working with the private Catholic University, the USAID will assist in creating a Center for Dominican Governmental Affairs.

D. AREAS OF CONTINUING CONCERN

As the AID program enters the mid-1980's, it is in a period of transition, wherein projects affecting the new private sector development strategy are being phased in, and older initiatives are being brought to an orderly conclusion. Several of these efforts have been "mortgaged" into FY-1984 and FY-1985 and beyond, and thus will require continuing AID assistance, albeit at a declining level. These include the areas of health (including population), energy, and rural roads.

1. Health

Health status of Dominicans has been a preocupation of the GODR and AID for the past 20 years, with the most recent efforts concentrated on establishing a rural health delivery system among rural communities below 5,000 population, and then integrating that system into the national health system of rural clinics, regional centers, and hospitals. The task is now almost complete. However, management of this system has shown extreme weaknesses, as evidenced by the difficulty of the necessary support services in getting through the service delivering infrastructure. In addition, it has been found that the Secretariat of State for Public Health and Social Assistance (SESPAS) has deficiencies in all the major management systems: finance, logistics, supervision, personnel, information systems, maintenance and planning. The major long-term goal of the USAID/DR in health has been, and remains, the provision of efficient and timely preventive health care to the rural population of the country. Two major sector loans have been made and a rural health delivery systems exists today, due largely to AID assistance efforts to the Dominicans. As we move beyond this phase of AID assistance to health, AID will pursue structural change and policy reform in the broad area of health services management. We view this as an effort to consolidate the gains made to date and insure lasting impact of the past investments.

The Health Systems Management program (Project No. 517-0153) was originally scheduled for FY-1983 obligation. Other Agency requirements forced postponement of this until FY-1984, which is when we now plan to obligate this 5-year program. Thus, FY-1984 will see us move our health program activities into a consolidation of benefits derived from earlier AID investments in health. AID will focus its activities through the Health Systems Management Project on increasing the effectiveness of central and regional management and support systems of the Secretariat of State for Public Health (SESPAS), and assist the GODR to increase the productivity and cost-effectiveness of its health service delivery infrastructure. Project activities will include: (1) improvement of management support systems such as finance, logistics, information, supervision, personnel, maintenance, and transport; (2) the development of a continuous in-house training capacity within SESPAS; and (3) a qualitative extension of basic health services and surveillance of dengue, yellow fever, and schistosomiasis control.

Moreover, AID will probe in the area of private sector involvement in health services, including the development of alternate financing mechanism schemes, joint private sector/GODR involvement in health care delivery, and in the possibility of developing rural water/sanitation organizations managed completely by the villages or by small geographic organizations.

In the nutrition sector, the Mission has approved an Applied Nutrition Education Program (ANEP) OPG, and is developing a Three-Year Plan for the utilization of PL-480 Title II food within the context of a nutrition program.

The experience gained through these approaches will be utilized in a future proposed multi-sector nutrition grant, which will assist the Dominican Republic in developing a capacity to plan, design, implement, and evaluate nutrition interventions.

2. Population

Although the population growth rate in the Dominican Republic dropped substantially from 3.4% in 1970 to 2.8% in 1981, it remains unacceptably high. This rate of growth not only consumes the benefits of growth, but also taxes the system to meet increased needs for employment and public services, particularly as the population growth adds much to the ever-increasing rural-urban migration. Although the need for family planning is apparent to both the GODR and USAID, recent conversations with the Jorge Blanco administration have indicated a continuing high level of political sensitivity to a bilateral program. Therefore, USAID has no choice for the foreseeable future but to use more subtle approaches to family planning, such as utilization of central funding and projects through PVOs. In fact, a large number of non-bilateral approaches are now being used. SESPAS, through assistance from USAID and other donors such as World Bank and the United Nations, is undertaking family planning activities in public health clinics. Private international donors, such as Church World Service (CWS), Family Planning International Assistance, International Planned Parenthood Federation, The Pathfinder Fund, Population Council, Development Associates International, and Westinghouse, carry on family planning activities--often through a local counterpart organization. Through centrally-funded mechanisms, AID can effectively increase family planning activities in the Dominican Republic without the need for a bilateral program. The Mission strongly encourages this approach. At the Mission level, small amounts of grant funding (PD&S and OPGs) can continue to be used to support studies, publications, conferences, and participant training.

3. Energy

The USAID has in place a major $15.7 million Energy Conservation and Resource Development program (Project No. 517-0144), which will be in execution through FY-1987 and which will require AID incremental funding through FY-1984. At this point, this program constitutes the major AID response proposed for the foreseeable future.

4. Rural Roads

The $15 million Rural Roads Maintenance program (Project No. 517-0177) is in its second phase, and will require substantial DA resources in FY-1984 and FY-1985 to complete the scheduled financing. This program will leave in place a completely new GODR institution of national scope in the year 1985. Future AID investments are not scheduled.

5. Urban Development

The Mission does not propose a separate urban development strategy as such.

The growth of the urban population in the Dominican Republic follows a similar pattern to that elsewhere in Latin America. The population growth rate in urban areas has been about 5.3% annually, compared with a national average of 2.8%. This trend towards urban growth is likely to continue for the rest of the century. Rapid urbanization has resulted in tremendous pressures on the provision of services and employment opportunities.

Current Dominican emphasis continues to be on rural development, particularly agriculture. Rural development/food production and the urbanization trend are intertwined in the confines of this island country.

The main AID focus, therefore, will continue to be on the rural areas. The Mission recognizes that demographic trends in Latin America do not auger well for successful efforts to staunch the flow of migration from the farm to the largest urban agglomerations. It is a matter of adjusting horizons to what is realistic. In the Dominican Republic, the potential for at least slowing the rate of migration to the principal urban centers suggests efforts to deflect as much as possible the inevitable flow off the farm towards the intermediate provincial cities. This comes down to questions of basic amenities: quality of life, employment, shelter, health, and education.

The GODR has assigned to the IDB and the World Bank primary donor responsibility for addressing the "intermediate cities" strategy. Several loans are being contemplated by the IDB for technical assistance, capital infrastructure, cadaster, and selected services needs, including a $150 million loan program for water supply in Santo Domingo. The IBRD has aq $15 million sites and services loan in the capital.

There are several AID programs, however, which will have a major impact upon urban population. These include:

— Establishment of a strong data base relating to urban poverty, employment, and migration.

— Programs in micro-industry and small/medium industry development.

— Energy conservation (industrial component).

— Vocational education and skills training.

— Primary education.

— Housing and service programs through HGs and low-cost housing technology.

— Agri-business investment support.

— Export expansion, including free zones.

AID recognizes that population growth and the stagnant performance of the agricultural and industrial sectors are the major causes of the unemployment problem in the Dominican Republic. Rural poverty and unhindered migration to the capital have been the results. The problems of unemployment and underemployment are very difficult, but they are not wholly intractable. The GODR, with the assistance of interested donors, has decided to try to address the problem. AID will play an important supporting role in that effort.

E. RESOURCES AND CONDITIONALITY

The USAID proposes the application of the entire range of resources available to AID to support our policy dialogue and subsequent project development for the planning period. This will involve the coordination of inputs from Development Assistance (DA) funds, Economic Support Funds (ESF), and PL-480 to be mutually reinforcing in their impact. The amounts involved are of a magnitude that AID influence can be not only useful but critical to the accomplishment of the structural adjustments and policy reforms we propose. Table I (see next page) shows the proposed assistance planning levels by functional amount for the fiscal periods 1984 through 1989.

1. ASSISTANCE PLANNING LEVELS (See Table I, Next Page)

2. ECONOMIC SUPPORT FUNDS

a. Uses. BOP problems of the Dominican Republic in the FY-1984 and FY-1985 periods will remain critical. Accordingly, the USAID proposes to apply the requested ESF resources to BOP assistance via the cash transfer mechanism. As before, the GODR will be requested to provide an equivalent amount of RD$ for programming towards mutually agreed upon purposes, as well as covenant to import an equivalent amount of US$ imports from the United States over a 12-month period. We intend to dedicate ESF peso resources towards a specific objective: export promotion. This permits development of a direct linkage between the immediate U.S. response to short-term problems and the longer-term development requirements.

b. Conditionality. No country in the Caribbean Basin is more sensitive about foreign-imposed conditionality than the Dominican Republic. As noted elsewhere, although our fundamental strategy is to support the IMF and IBRD initiatives, we intend to pursue our own policy dialogue in AID priority areas.

PROPOSED ASSISTANCE PLANNING LEVELS BY FUNCTIONAL ACCOUNT
USAID/DOMINICAN REPUBLIC
(THOUSAND OF U.S. DOLLARS)

		1984	1985	1986	1987	1988	1989
AGRICULTURE, RURAL DEVELOPMENT & NUTRITION	TOTAL	19433	20975	19450	20450	18500	24550
	GRANTS	4133	4625	4450	2450	4500	3550
	LOANS	15300	16350	15000	18000	14000	21000
POPULATION	TOTAL	50	200	125	175	225	225
	GRANTS	50	200	125	175	225	225
	LOANS	-	-	-	-	-	-
HEALTH	TOTAL	4924	2300	1875	1250	1150	900
	GRANTS	924	300	375	1250	1150	900
	LOANS	4000	2000	1500	-	-	-
EDUCATION	TOTAL	5371	7225	7450	7650	11700	8800
	GRANTS	2371	3225	2450	3150	2700	1300
	LOANS	3000	4000	5000	4500	9000	7500
SELECTED DEVELOPMENT ACTIVITIES	TOTAL	1222	1800	6400	8575	9325	8125
	GRANTS	1222	1800	1400	2375	2525	1125
	LOANS	-	-	5000	6200	6800	7000
DA	TOTAL	31000	32500	35300	38100	40900	42600
	GRANTS	8700	10150	8800	9400	11100	7100
	LOANS	22300	21850	26500	28700	29800	35500
ESF	TOTAL	40000	45000	50000	45000	40000	35000
	GRANTS	-	22500	5000	5000	5000	5000
	LOANS	40000	22500	45000	40000	35000	30000
DA & ESF	TOTAL	71000	77000	85300	83100	80900	77600
	GRANTS	8700	32650	13800	14400	16100	12100
	LOANS	62300	44350	71500	68700	64800	65500
PL-480 TITLE I		20000	22000	23000	25000	25000	26000
PL-480 TITLE II		2818	2600	3000	3500	3500	4000
HOUSING GUARANTIES		-	20000	-	20000	-	20000

Barring a political decision to the contrary reached at the policy level of the USG, compliance of the GODR with its IMF arrangement is the sine qua non for ESF assistance in FY-1984 and FY-1985. The rupture (unscheduled termination) of this 3-year arrangement would obviously signal lessened coherence of GODR economic policies. Partial compliance, as may arise from time to time, can be viewed mainly as technicality best left to IMF discretion to sort out. An IBRD structural adjustment program (SAL) has unknown probability of near term agreement, principally because of probable legislative action necessary prior to loan agreement. The key problem area rests in reduction of tax exonerations to import substituting industries. Other requirements for a SAL are increase prices for agricultural commodities sold within the country, relaxation of the interest rate control, and use of the parallel market for exports. Our strategy also seeks substantial progress in these areas, and we will work closely with the IBRD in the coming months to insure compatibility in our approaches.

In regard to the best use of AID resources in our own policy dialogue, our analysis indicates that the pressing foreign exchange problems suggests that <u>the major negotiating point for the FY-1984 ESF should be the successful conclusion of the IMF/GODR discussions concerning the second year of the IMF Agreement (this has been confirmed by the LAC/ARA review of the FY-1984 PAAD).</u>

<u>For the FY-1985 ESF, we propose a close working relationship with the IBRD to develop a common agenda of negotiating issues.</u> It is probable that the IBRD/GODR discussions currently underway will conclude that the conditions necessary for a SAL will not be possible. However, it is highly probable that the IBRD and the GODR will reach agreement on the terms and conditions necessary for an Export Sector Loan of substantial proportions. These issues relating to this loan coincide to a large degree with AID's. Accordingly, we intend to consult closely with the GODR to insure that those issues most important to AID are included in a common approach. We see advantage to approaching the GODR separately on the same general issues, and indeed foresee some confusion among AID, IBRD, and the GODR if we develop separate negotiating tactics. One area which we intend to press for GODR action jointly with the IBRD is with INESPRE. While

this is an issue we will pursue within our PL-480 negotiations (see later discussion in Section E.4.), it is related to IBRD and AID's concerns on agricultural pricing and its impact on export development.

3. DEVELOPMENT ASSISTANCE FUNDS

a. Uses

As noted, the FY-1984 DA program is one of transition, and while containing several new starts in private sector development, has significant resources devoted to continued funding of ongoing projects, or projects designed to terminate ongoing strategies in an orderly manner.

The FY-1985 program requested herein, at the $32.5 million level, will complete ongoing projects and emphasize export and investment promotion, agriculture research and extension, and improvement in the human resource base. The portfolio will consist of 14 funded projects with 4 new starts.

The agriculture sector, proposed at a $20.975 million level, represents 64.5% of the total program. Four projects are proposed for final incremental funding. Agricultural Policy Analysis (517-0156), Forestry Management grant (517-0178), Rural Roads Maintenance (517-0177), and Agri-Business Promotion (517-0186). One new start is the Agriculture Research and Extension project (517-0180).

Only PD&S and OPG funds are requested for population activities; and in health, the Health System Management grant (517-0153) is proposed for incremental funding. Health and Population, proposed at $2.5 million, account for 7.6% of the program.

The education sector is proposed at $7.225 million, representing 22% of the program. Two ongoing projects are proposed for incremental funding: the Graduate Management Training project (517-0157) and Rural Education (517-0172) proposed for final funding. Two new starts in FY-1985 are the Policy Analysis Training project (517-0188), which will provide highly qualified economic and business sector analysis; and the Center for Dominican Governmental Affairs project (517-0189), designed to strengthen and institutionalize the development of the nascent Dominican democratic process and enhances the soundness of public decision-making.

The Selected Development Activities sector consists of four funded projects at $1.8 million, representing 5.5% of the program. The one new start is the Export and Investment Promotion project (517-0190), whose purpose is to increase exports of non-traditional products. The Mineral Export Promotion project (517-0183) is proposed for incremental funding, and the Housing/Appropriate Technology OPG (517-0164) is proposed for final funding. Funds are also requested for the Special Development Activities project (517-0050), PD&S, and proposed OPGs.

b. Conditionality

There are inter-related issues with ESF and PL-480 in the areas of export promotion and pricing. As noted, when these exist, they will be part of the common agenda to be developed with the IBRD.

4. PL-480

Title I

a. Uses

Enhancing the developmental impact of PL-480 resources is a major objective of the USAID. AID participates fully in the programming of country-owned local currency generated by sale of PL-480 Title I commodities, and uses that involvement to seek achievement of mutually-agreed upon developed goals. To a large degree, PL-480 food aid resources are integrated with DA funds to help achieve specific program and policy objectives, and to enhance the developmental impact of all external resources. AID and the GODR agree in principle on the specific uses of the sales proceeds and other self-help measures before signature of the annual agreement. Sales proceeds are kept in a separate account, and disbursements are subject to AID approval.

Program direction of use of Title I proceeds has shifted significantly in the past two years. Previously, proceeds were used mainly to expand upon the small farmer services provided by the Secretariat of State for Agriculture (SEA) begun under AID sector loans in the 1970's. This program concentrated mainly on services and production inputs provided by the public sector. Starting two years ago, the Mission encouraged the GODR to shift the emphasis to more direct integration into ongoing AID and other donor programs and to provide more investment to productive infrastructure. That trend will continue to be reinforced in the future.

b. Conditionality

The Mission has undertaken a policy dialogue with the GODR focussing on the role and extent of the Price Stabilization Institute's (INESPRE) participation in the economy. The Mission's major instrument for this is the Title I negotiations, as all PL-480 imports must be authorized by INESPRE. In the past, INESPRE has purchased Title I products at the official exchange rate of US$1.00 = DR$1.00, and sold them at the going market rate. The resulting "differential" or profit was used to cover the costs of handling, transportation, etc. The current wide disparity between the official and parallel market rates (jumping 60 points the past year to about 1:1.80) has resulted in INESPRE realizing a wide margin of "profit" and has generated considerable liquidity which allows INESPRE rather wide margin of "profit" and has generated considerable liquidity which allows INESPRE rather wide discretion on market interventions in a variety of products. Starting with the FY-1984 agreement, the Mission has negotiated a change to require INESPRE to deposit all sales proceeds with the GODR, and devote these proceeds to agreed upon development activities. Such a step will result in INESPRE's scaling back significantly in its range of market interventions, and assist it to focus on its higher priority functions of avoiding wide variations in prices of agricultural products. We will also be investigating the role of INESPRE pricing per se through the Agricultural Policy Analysis project proposed for FY-1984.

INESPRE has proven to be a somewhat exclusive participant in any policy dialogue. AID has channeled almost all of its concerns through the Technical Secretariat of the Presidency (STP), who is the formal GODR representative in PL-480 negotiations, and who monitors GODR progress on self-help measures, programs use of peso proceeds, prepares reports, etc. The TSP has also been somewhat frustrated by some of INESPRE's actions and its apparent independence from GODR guidance. We intend to use the FY-1985 PL-480 negotiations as the forum for requesting a major policy shift in INESPRE's relationship with PL-480, i.e., a shift of the role of INESPRE from importor to licensee, with the PL-480 imports being managed directly by private sector importors.

Also, the Agriculture Policy Analysis project will have staffed out specific price policy issues which can be incorporated within the discussions. The IBRD has also identified INESPRE as a major policy issue within their discussions. Their recommendations relate to narrowing INESPRE's activities in rice marketing, divertiture of stocks of oil and other commodities, lifting of price controls on oil, and selling of physical assets such as tanks and cold rooms. These are issues which we intend to pursue within our common agenda with the IBRD.

The issue of price disincentives as a result of increased levels of PL-480 will be included in our discussions. Recent domestic price increases for domestically produced corn and sorghum have eliminated, by some degree, any problems in that commodity. As the country does not produce wheat, no problem exists there either. In edible oils, however, there is a domestic price control which is linked to the production of peanuts and is theoretically set to protect these local producers. The degree to which the local price may act as a disincentive is not clear, especially as there are several new large investments in palm oil and cotton production which have begun under the current price, and which would seem to indicate economic returns are sufficient to warrant further investment.

Title II

a. Uses

The Dominican Republic continues to face serious malnutrition in many of the poorest rural regions of the country. Surveys show that up to 75% of the population is estimated to be undernourished, with about 50% consuming an average of 1,424 calories and 28.26 grams of protein per day, against a recommended daily level of up to 3,000 calories and 62 grams of protein. Another 25% have a daily intake of 2,054 calories and 51.7 grams of protein.

The PL-480 Title II program is implemented by three U.S. Voluntary Agencies (VolAgs) with their Dominican counterparts,1/ and

---

1/ U.S. Voluntary Agencies:	D.R. Counterparts:
Catholic Relief Services (CRS)	CARITAS
Church World Service (CWS)	Servicio Social de Iglesias Dominicanas (SSID)
CARE	Secretariats of State for Education and Public Health.

entails basically four types of programs: Nutrition, including Maternal and Child Health (MCH), Other Child Health (OCH), and Pre-School Feeding (PS); and Rural Development Programs under Food for Work (FFW).

The objectives of the MCH programs are: (1) to provide supplementary food to reduce the incidence of malnutrition in pre-school children and women of child bearing age; (2) to educate mothers in nutrition, hygiene, and child care, and provide literacy training and nutrition surveillance. OCH programs provide supplemental foods to State hospitals, particularly pediatrics and obstetrics wards, orphanages and special schools. Only CARE is involved in a pre-school feeding program, implemented through the Secretariat of Education. In addition to providing food, the program proposes to reduce the high incidence of primary school dropouts by giving underprivileged children a "head start" in the learning process. FFW projects provide in-kind payment to unemployed or under-employed rural workers for their participation in infrastructure projects, such as feeder roads, irrigation canals, water and sanitation, reforestation, and development of community organizations.

b. Conditionality

In 1982, an in-depth evaluation and an audit of the Title II program highlighted a wide range of improvements and reforms necessary to strengthen the program. The major reform is the ellaboration of a Three-Year Plan by each VolAg, which shifts the program focus from a dole-type activity into a development resource, including an improved targetting of recipients. The VolAgs have already undertaken several steps to improve their management and operations, including the acquisition of a USAID-funded micro-computer, accompanied with staff training and training of area supervisors.

The VolAgs' Three-Year Plan is the major policy instrument of the USAID in reforming the program. These plans, one for each VolAg, are under development. They take as their basic tenet that food alone is not sufficient and additional resources, including technical assistance, is required to effect change in nutritional and other status. The USAID is working closely with the VolAgs to:

(1) Integrate Title II projects with other AID development projects. This has already begun with: (a) The animal trails component of the Rural Roads II project--Title II FFW will provide food to families as compensation for labor during the construction of the animal trails. The VolAgs will first discuss and promote the trails with the benefitted communities, then request assistance from the Directorate General of Rural Roads (DGCV) for engineering assistance. DGCV will also provide culverts and cement for the construction of the trails. (b) The Radio Community Program, under which Title II food is provided to out-of-school children in a 1-year research effort to determine, in a controlled environment, the impact of a nutritional component in a radio education project for 1,000 school age children. (c) The Health and Nutrition OPG, which will share nutrition education resources with the Title II program, and promote closer collaboration on nutrition between the VolAgs.

(2) Integrate with development projects of other organizations. The Secretariats of Public Health and of Education have had full participation in the designing of the plan. Other organizations have also participated, such as the Office of Community Development (ODC), the Directorate General of Forestry, the Center for the Improvement of the Small Farmer, and the Peace Corps. In the process, some ideas have arisen involving co-participation in projects.

(3) Partial monetization (under Section 206) of the food to generate cash for development activities. This has not met with early acceptance by the VolAgs, who are reluctant to give up a portion of their rations in view of the limited size of their program and the large number of beneficiaries. Monetization, however, may become a positive element in FFP projects, where a partial monetization would generate required local currency for the purchase of necessary hand tools.

Our objective is to conclude the Three-Year Plans, and thus move the Title II program towards becoming an effective development resource in the benefitting communities. Already, we understand the process of improving the program is being considered as a model which may be replicated in other countries.

5. HG

a. Uses

The HG resources requested will support a public sector low cost housing program involving single family detached units or row housing costing between 5-7,000 pesos. The beneficiaries would have a monthly income of up to RD$350 and monthly payments would not exceed RD$40 per month, with a down payment of RD$1,000.

b. Conditionality

Negotiations for a major HG program in the Dominican Republic have been underway since 1980. Originally scheduled for application through the private savings and loans (S&L) system, a $15 million was authorized in 1982 for a worker housing program, including the private sector. High U.S. interest rates resulted in a reluctance on the part of the Housing Bank and S&L system to sign a loan agreement. Subsequently, the National Housing Institute (INVI) launched a massive construction program of home building of units which competed directly with the authorized HG program, at subsidized interest rates. The S&L system continued to demur, reflecting their belief that INVI housing would capture the market share originally proposed for the HG. After continued delays, the GODR formally requested that the HG be transferred to the INVI to assist in meeting the costs of the INVI program already underway. After discussions with INVI, the USAID replied that it could not agree to such a shift and requested a high level GODR policy review of the housing program, its objectives, and future directions. This was done by a special housing commission, which reported to the President, and recommended major changes in INVI's programs and policies. Unfortunately, the advanced state of the ongoing program precludes it from being covered by a HG due to its price levels. Thus, the original authorization was cancelled in September 1983. The GODR has subsequently requested a HG for a new INVI program more in keeping with HG guidance. The GODR has informed us of their desire to pursue this HG within the context of major reorientation of the INVI organization, changing it into a low-cost housing bank with its own capital, and removing the current levels of subsidy now provided. AID will support the GODR within this context.

6. OTHER DONORS

IBRD. There has been considerable discussions in this CDSS of the role of the IBRD. Their current emphasis is on structural adjustment; however, the ongoing portfolio of 10 loans totalling $270.5 million has an undisbursed balance of $138.8 million (June 30, 1983) and represents a significant contribution to sectoral investments in irrigation, tourism, highways and coffee/cacao rehabilitation. The IBRD portfolio is of relatively recent vintage, reflecting the major expansion of activities in the 1978-1982 period. Future lending plans include new loans in education and power (Haina Coal Port Terminal). Counterpart financing continues to be a major obstacle to implementing ongoing projects, which has been alleviated somewhat through programming of CBI-generated pesos towards this purpose. Recent changes in IBRD staff have resulted in closer cooperation between IBRD and USAID staff, which is expected to continue and deepen as our common agenda is developed and discussed.

IDB. The Inter-American Development Bank maintains an active program of approximately $150 million of new funding per year, making it one of the most important donors. Its emphasis has been in power, secondary roads and highways, agriculture, education, and port development. Most recently, IDB has made major contributions to Santo Domingo water supply ($150 million loan--the country's largest ever from IDB) and adult education ($23 million). Its future plans include increased lending to the urban sector (both Santo Domingo and secondary cities) and higher education expansion. Relations with the IDB office in Santo Domingo are close and cooperative.

7. STAFFING

No special USAID staffing requirements are contemplated. The current level of 22 USDH and 34 FSN, however, is considered minimal. We have incorporated the strategy of building project administration costs into each project, in most cases, and specialized contract employees have been recruited. We would point out that the current personnel levels have remained constant while funding levels and numbers of projects have increased four-fold.

F. CROSS-SECTORAL STRATEGIES

The following section specifically address two of the four pillars of AID strategy. The other two--private sector and policy dialogue--are treated at some length above.

1. Institution Building

Efforts in this area are being realized through a number of our ongoing projects. Major accomplishments in this area have been efforts to strengthen existing Dominican institutions to carry out new roles in the country's overall developmental efforts. Under the Rural Management Training project with the Instituto Superior de Agricultura (ISA), the Mission has been instrumental in developing a university curriculum and specialized facilities focussed on developing the management skills of mid-level managers in both the public and private sector. Through case history methodology, ISA has developed the capability to focus the attention of sector decision-makers on key issues, such as land reform, food price policy, and agriculture development in general.

The Rural Roads Division of the Secretariat of Public Works enjoys a major upgraded status as well as an improved budget, and a decentralized and country-wide administrative and organizational structure with trained administrators due to the USAID-supported Rural Roads I project. This will continue to be reinforced over the CDSS period.

In health, the SBS program has been expanded to include 5,300 rural promoters and strengthened through AID support. As a result of this experience, the Secretariat of Public Health (SESPAS) and AID are now designing a follow-on project to plan, staff, and manage the delivery system which is in place. The FY-1984 Health Systems Management Program will be aimed at increasing the benefits derived from earlier AID investments in the training of rural promoters and the construction and equipping of rural clinics.

The creation of a new graduate school of administration within the Catholic University (UCMM), including the construction of specialized facilities employing the most modern equipment and new teaching methods, is a major example of institution building resulting directly from AID involvement. AID's major emphasis is on business administration and the school will no doubt become a focus of private sector research and application for the country.

Under micro- and small industry programs, three Technical Assistance Centers are being established around the country to provide needed training in accounting, production and marketing to micro- and small businessmen.

New projects within the export promotion area will be deeply involved in institution building. The Mineral Export Promotion project will establish an institutional bond between the Dirección General de Mineria and the United States Geological Survey. Exchange of professionals and information, large amounts of U.S. participant training, and policy analysis and recommendations on changes to GODR mining regulations will be major components of the project.

The establishment of trading companies under the CBI represents a major institutional innovation in the country and will be supported. This will also include strengthening of the free zone concept within a private sector framework.

The restructuring of the current public sector agriculture research and extension program into a system involving the country's private universities is an institutional task of major proportions, and offers important benefits to the country if it succeeds. AID intends to devote considerable attention and resources to this issue over the next several years. Finally, the proposed Center for Dominican Governmental Affairs will be a totally new organization sewing the needs of the Legislative branch. Hopefully, with this project we will be strengthening three institutions--the Center itself, the legislature, and Dominican democracy.

2. Technology Transfer

The Mission objective of increasing agricultural production in the Dominican Republic is presently based on the transfer of improved technology to farmers and decision-makers alike. Ongoing activities include the Natural Resources Management project, with its components for farming systems research and soil and water resource conservation; the Swine Repopulation program, which demonstrates improved swine production techniques; and the Inland Fisheries project, which teaches farmers to produce fish using modern methods and ideas. The On-Farm Water Management project, which will demonstrate modern technology for on-farm water management and institutionalize research and extension capabilities in that critical area; and the Agricultural Sector Training project, which will focus on graduate U.S. training for technical specialists who will be the future researchers of the Dominican Republic, are two major loans in the early stages of implementation which demonstrate the GODR's desire to invest in technology transfer.

Appropriate technology is being introduced in the housing improvement area; and a new technology for rural roads maintenance is being piloted in the Dominican Republic. The use of solar power is being introduced for bagasse drying and for refrigeration; and the use of radio as an education media has been established and is being expanded.

Of special note is our major expansion of participant training at all levels. In FY-1983, 103 participants are scheduled for U.S. training (as compared to 78 in FY-1982), and this number will increase for the next several years. We believe this is one of the most effective mechanism for technology transfer.

Proposed programs in agri-business and export promotion will create significant flows of technology to the country via the investment of capital and technology by investors seeking to produce for the U.S. market under the CBI.

G. PEACE CORPS ACTIVITIES

There are approximately 120 volunteers in the country. The program concentrates its resources on rural development (25 PCVs), forestry (24 PCVs), small business development (19 PCVs), health and nutrition (41 PCVs), and inland fisheries (8 PCVs). There is a high degree of cooperation by volunteers in program assisted by AID in the following areas:

1. Small Business: PCVs are working with the community based organizations providing technical assistance to micro and small entrepreneurs in Santo Domingo and secondary cities. These local organizations receive assistance from one of several AID-supported programs with the Central Bank Rediscount Fund, Dominican Development Foundation, and the Association of Micro-Industries.

2. <u>Forestry:</u> The Peace Corps is a member of the USAID project committee developing the FY-1984 Forestry Development Project. The PCVs will become an integral part of the program.

3. <u>Inland Fisheries:</u> PCVs work at the community level assisting an AID-funded PVO organizations. They are an integral part of the project.

4. <u>Health and Nutrition:</u> PCVs are working in public health facilities with GODR rural health workers supported under an AID loan.

5. <u>Rural Development:</u> PCVs are working with several local PVOs who receive AID assistance in swine repopulation and low-cost housing technology, as well as community groups who receive small grants under AID's Special Development Activity Fund. In addition, the Peace Corps is executing a $40,000 AID grant which will support PCV small scale projects around the country.

The USAID/DR and PC/DR staff have begun a series of regular meetings to become more familiar with our respective programs, and encourage closer staff cooperation.