40945

DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
Washington, D.C. 20523

UNCLASSIFIED

AID-DLC/P-745
June 20, 1968

MEMORANDUM FOR THE DEVELOPMENT LOAN COMMITTEE

SUBJECT: Costa Rica: CONFISA, Private Development Bank (Second Loan)

Attached for your review are the recommendations for authorization of a loan in an amount not to exceed $5,000,000 to the Corporacion Costarricense de Financiamiento Industrial, S.A. (COFISA) to assist in financing the dollar costs of subloans and equity participation by Borrower for the creation and expansion of industrial and agricultural enterprises in Costa Rica and Member Countries of the Central American Common Market.

This loan proposal is scheduled for consideration by the Development Loan Staff Committee at a meeting on Monday, June ~~21~~, 24, 1968.

Rachel C. Rogers
Assistant Secretary
Development Loan Committee

Attachments:
Summary and Recommendations
Project Analysis
ANNEXES I-VIII

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# COSTA RICA - SECOND COFISA LOAN

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COSTA RICA - COFISA, Private Development Bank
(Second Loan)

SUMMARY AND RECOMMENDATIONS

1. Borrower: Corporacion Costarricense de Financiamiento Industrial, S.A. (COFISA), a private development bank.

2. Amount: Not to exceed $5,000,000.

3. Other Financing: COFISA will be required to sell additional shares for at least $1,500,000 equivalent to be paid in at least pari passu with AID disbursements and in not more than two years from the first AID disbursement. Private U.S. and European banks are expected to make at least an additional $1,000,000 available in short-term credit lines.

4. Purposes: To provide financing for economic diversification. To establish an effective private lender for agricultural development in competition with the nationalized commercial banks. To insure the continued expansion of the successful private development bank. To increase support for the CACM by assisting industries dependent on the CACM market. To help finance rapid economic growth while Costa Rica is taking needed fiscal and omnetary measures. To help develop a domestic capital market and encourage the investment of Costa Rican capital at home. To expand U.S. exports by requiring all loan proceeds be used for U.S. procurement.

5. Procurement: The loan proceeds will be used only to procure goods and related services with U.S. source and origin (excluding marine insurance).

6. Project Description: Changing the role and emphases of the effective industrial development bank (COFISA) by providing it with both the funds and an incentive to finance the highest priority productive projects. Emphasis is on moving COFISA into agriculture; it was largely limited to industrial lending during its formation period while disbursing the first $5.0 million AID loan. Reduction of the ratio between loan funds and increases in COFISA's equity insures a greater mobilization of Costa Rican funds to provide the source of local costs financing which is essential in agriculture. COFISA is also being given an incentive to make more equity investments to overcome the typical undercapitalization of Costa Rican

firms and to begin the creation of a capital market. It is recommended that use of funds from the second AID loan be prohibited for industries in the "C" category of the CACM Industrial Incentives Treaty (primarily assembly or packaging operations).

7. EXIMBANK and Alternative Sources of Financing: In May, 1967, the Eximbank informed AID it was not prepared to consider this loan. ExIm interest rates would not provide the incentives for priority investment on which this project is now based. Present lending policies of the IDB and IBRD require acceptable third party or government guarantees. No government guaranty is desirable since COFISA as a private lender should be independent of government. IFC loan funds are too expensive ($7\frac{1}{2}$ - 9 per cent), and foreign bank lines of credit are inappropriate sources for medium and long-term loans.

8. Country Team Views: The Country Team gives this loan second priority, after the malaria loan, as an integral part of its overall strategy. The continuing fiscal and balance of payments problems can most readily be resolved during a period of rapid economic growth. The availability of these AID funds will help maintain the growth rate and also make it possible for the Central Bank to resist demands for an increase in domestic credit which would exacerbate the balance of payments problems. The subloan projects will help the balance of payments directly. Substantial self-help measures have been taken during the past year in the fiscal field as well as in improving incentives for non-traditional agriculture. With Government programs oriented toward education, health and other Alliance objectives (no military expenditures), these self-help measures justify an AID input of more than $4 million in FY68. The COFISA loan is more appropriate than any alternative because of its direct support for the private sector. The loan will also increase U. S. exports both now and through future years by creating demands for spares and replacements.

9. Statutory Criteria: All statutory requirements of the Foreign Assistance Act have been met (Annex One).

10. Major Issues and Conditions

a. Why a second COFISA loan?

Because COFISA has been successful both administratively and financially, one can argue a second loan is not needed to build the

institution. The second loan provides the incentive for a capital increase diluting share value and the resources for a dynamic expansion, but the primary reason for the second loan is to take advantage of the effective private institution already developed to direct both AID and Costa Rican funds to priority development objectives, especially to commercial agriculture (Sections II. A, B; III. C).

b. Why any funds except for highest priority purposes?

There is still an important role for COFISA in lending to industries which do not export outside the CACM or use 75 per cent CACM raw materials to: (1) increase support for the CACM, (2) keep Costa Rica competitive with other CACM countries receiving AID funds for similar purposes, (3) provide employment, (4) increase COFISA's equity holdings to help develop a capital market, (5) provide financing for U. S. equipment competing with that of other developed countries. The most marginal industries are not eligible, and the size of the interest rate subsidy is greatly reduced. Availability of AID funds for U. S. procurement will permit use of a higher proportion of COFISA's capital and secondary generation for local cost loans in the priority fields (Sections I. C; II. A, B; III. A, D).

c. Ownership and Profitability:

Although COFISA has more shareholders than any other lending institution in Costa Rica, over 65 per cent is owned by 20 family groups. We recommend the condition be continued that, without the prior written approval of AID, no natural or juridical person, or anyone related to the same within the second degree, shall own, directly or indirectly, more than 5 per cent of COFISA's voting stock. The seven man board of directors owns 22 per cent, but less than 7 per cent of loans have been to firms in which board members and their families control 33 per cent or more. Nevertheless, AID is criticized for giving substantial assistance to a small group, though it is dynamic, efficient and mindful of the national interest. We recommend COFISA be required to place at least $500,000 equivalent of the new share issue with persons or firms not shareholders on December 31, 1967 (Section I. B).

Some are also critical of the supposedly high earnings on COFISA shares. We recommend a limitation of 12 per cent on cash dividends be retained for the 20 years of the AID loan and that the 12 per cent cash dividend limit be reduced whenever stock dividends

are paid such that the maximum cash dividend will be 12 per cent on the amount of capital subscribed in cash plus the 6 per cent stock dividend already paid. Thus earnings above 12 per cent will be retained and invested in economic development. In the current period of exchange rate uncertainty and rising prices, a fixed return of 12 per cent is not competitive with other investments such as Government bonds yielding 11 per cent tax-free. Typical investment returns are 20 per cent. Projected earnings on paid-in capital after taxes (Annex V, Part 1(a)) show a maximum return before reserve allocations of 20.5% in 1973, which peak reflects AID's concessional rate for relending for priority projects, but which declines thereafter to about 17% in 1976 resulting from an increase in AID interest after five years.

d. Lending terms and equity participations:

COFISA has made more loans of less than two-years than is desirable and has taken fewer equity positions than we would wish. We recommend the minimum term for subloans with AID funds be increased from two to three years with the maximum 10 years. COFISA used part of the first AID loan to finance imports from the U. S. of raw materials and intermediaries; we recommend only machinery and equipment be eligible under the second loan except when COFISA finances priority projects or takes an equity interest at least equal to other financed imports. We do not discourage COFISA's short-term lending with its lines of credit from foreign commercial banks because COFISA offers the only alternative to the slow and collateral oriented nationalized commercial banks (Section I. C (6) (7); Annex 4).

e. Exchange system problems:

The present exchange system makes it advantageous for a company to borrow from COFISA to import machinery even though it does not need the funds. Although we have confidence the COFISA board will not authorize unneeded loans, we recommend a detailed review before commitments pass $1,750,000 to assure AID its funds are going only where there is a real need. A devaluation would increase the leverage of the AID loans and thus the profitability per colón invested in shares. We do not recommend an escalator clause because additional earnings will have to be retained for 20 years and any escalator provision would make the shares unattractive at this time of exchange rate uncertainty when we want a maximum mobilization of Costa Rican resources for investment in Costa Rica (Section VI).

11. Recommendations: **Authorization of a loan to COFISA in an amount not to exceed $5,000,000.**

a. Terms: Loan to be repaid within 20 years including a 5-year grace period.

b. Interest: Three percent per annum on drawings for priority projects for five years after which the rate will be raised to five percent. Five percent on other drawings, which may not exceed $2,500,000. Priority projects are defined as those directed primarily at increasing exports outside the CACM or exchange earnings from tourism, those increasing agriculture production directly or the processing of Costa Rican agricultural production, and other projects for which COFISA can show that 75 percent of the inputs are of CACM origin and the expected selling price of the output is within 25 percent of the normal landed cost of similar imports.

c. Repayment: In U.S. dollars unless the Government enters a two-step agreement for the use of colon repayments with terms to the Government 40 years including a 10-year grace period and interest of 2 percent during the grace period and 2½ percent thereafter with repayment in U.S. dollars.

d. Other conditions:

(1) Except as AID may otherwise agree, a professional economist and an agricultural specialist acceptable to AID must be added to the COFISA staff before commitments exceed $1,000.000.

(2) The maximum interest rate charged to sub-borrowers utilizing these funds will be 8.5% for priority projects and 10% for other projects.

(3) No loans or investments will be made with funds from any source, including subsequent rollovers, which will directly or indirectly increase the production of coffee, sugar or cotton except as AID may agree in writing.

(4) Agricultural loans must be based on a comprehensive project to be considered priority; equipment financing or crop financing, except as part of a larger project, are not priority projects.

(5) Outstanding loans for the banana industry, including companies whose principal business is servicing banana farms or providing transportation for bananas, may not exceed $500,000 from all sources of funds, except as AID may otherwise agree in writing.

(6) At no time may disbursements of AID loan funds for projects outside the priority category exceed by more than $350,000 the amount of disbursements of AID loan funds plus loans of more than one year from other COFISA funds for projects in the priority category financed after May 15, 1968.

(7) AID may require COFISA to obtain prior AID approval for every project in the priority category if review of COFISA's monthly reports indicates the definition of priority projects is not being followed completely.

(8) COFISA will make no loans from any source of funds to purchase existing shares and may not make loans for the purchase of new shares in expanding or new enterprises unless COFISA itself purchases equity equal at least to the equity financed.

(9) No discrimination shall be practiced with prospective clients with respect to their nationality or citizenship. Foreign equity participation shall not exceed 40 percent of COFISA's voting stock.

Other conditions, most of which are normal for development bank loans, are shown in Annex Five.

PROJECT COMMITTEE:

| | | |
|---|---|---|
| Project Coordinator | - | Robert Grey USAID/CR |
| Economist and Financial Analyst | - | John Bushnell USAID/CR |
| Loan Officers | - | Ernst Schlomann USAID/CR |
| | | Arnold Schwartz AID/W |
| Evaluation Officer | - | William Ludwig AID/W |
| Supervising Officer | - | Robert Hoffman USAID/CR |
| Drafting Officer | - | John Bushnell USAID/CR |

# I. Background

## A. History of Project

The idea of a private industrial development corporation in Costa Rica dates from about 1948 when the local commercial banks were nationalized. At that time Rodrigo Madrigal Nieto, a young attorney, wrote a brief paper discussing the possibility of such an institution. The rationale was the need to finance on a larger scale the development needs of the private industrial sector to diversify the national economy which was then dependent on the production of agricultural commodities, particularly coffee and bananas, the world prices for which were subject to severe fluctuations. Stimulation of the private industrial sector, it was reasoned, would assist materially in providing jobs for a rapidly growing population as well as contribute to the amelioration of trade deficits by encouragement of import substitution industries.

In 1957, Madrigal visited the U. S. under ICA auspices to study capital formation; this trip resulted in further conversations and study of the possibilities of a private development institution by Costa Rican businessmen. By that time it became clear that strong external economic support would be required to assist in the formation of the development corporation, and various possible sources for such support, among them the Banco Nacional de México and Crédito Bursátil, were approached without success. Growing interest was generated among local industrialists and entrepreneurs, especially after the approval of the Industrial Incentives Law in 1959. During the early 1960's, with the approval of the President of Costa Rica, serious conversations were initiated with AID for long-term financing. The Madrigal group noted that the nationalized banking system was insufficiently liquid to meet the medium and long term needs of the private sector, that the existing banking system responded at best only slowly to industrial credit applications, made loans primarily based on adequacy of collateral rather than on in-depth project evaluation, and, as government entities, were subject to political pressures. In April 1963 an organizing committee for the development bank, headed by Madrigal, formally submitted an application for an AID loan to complement permanent equity capital to be raised from local entrepreneurs for the creation of Corporación Costarricense de Financiamiento Industrial, S. A. (COFISA).

The Capital Assistance Paper of 1963 called for the creation of a completely private industrial development corporation to finance a portion of the capital requirements of the private industrial sector. In November 1963, an AID loan to COFISA was authorized which was signed in December 1963. This loan was for $5.0 million at 2 percent interest for 20 years with a 5 year grace period. Up to $1,250,000 was for local currency use while

$3,750,000 was limited to U. S. procurement. To qualify for initial disbursement, COFISA was required to have commitments for $1.0 million equivalent in capital to be paid in over the anticipated three-year AID disbursement period. This requirement was satisfied by initial payment of $200,000 equivalent in share capital and legally binding commitments for the remainder, all of which has now been paid.

An important feature of COFISA's equity issue was the prohibition against acquisition of more than 5 percent of COFISA's stock by any business entity, individual or immediate family group; the result has been that COFISA's original stockholders numbered 136, making COFISA, after the National Cement Company, the most widely held private corporation in Costa Rica. This ownership limitation remains in effect. Of the 136 original shareholders, eight subscribed for the full 5 percent limit ($50,000) of whom three became members of the Board of Directors. Approximately one half of the original stockholders subscribed under $3,000 each. Only 18 of the original shareholders subscribed to over $15,000 equivalent, although these 18 purchased more than half the shares.

A manager, industrial engineer, financial analyst and other administrative personnel were engaged; a Board of Directors and vigilance committee were elected, and COFISA made its first subloan in October 1964.

When it appeared in early 1966 that the first loan would soon be fully committed to sub-projects, COFISA began discussing the possibility of a second loan. The negotiation of this second loan has been long and difficult. COFISA could not show to the satisfaction of the USAID that it required a second concessionary loan to continue in business. The very success of COFISA handicapped it in getting a second AID loan in comparison with other Central American development banks. Moreover, the favorable terms of the first loan mean that a second loan and an increase in COFISA's capital will reduce the value of each COFISA share. COFISA shares which have been sold have not commanded a substantial premium; as recently as mid-1967 COFISA shares were sold at par. As most COFISA shareholders purchased their shares as an investment, not to enhance possibilities of financing for their companies, there was major pressure for payment of a dividend as soon as possible, thereby limiting the amount of resources reinvested.

In 1966 a second Costa Rican business group proposed to AID the establishment of a second development bank with an AID loan to provide competition for COFISA. This group maintained that COFISA's board of directors played favorites in making subloans. Moreover, the second group was prepared to accept for its first AID loan the terms which COFISA was not prepared

to accept at that time for its second loan, especially all U. S. procurement and a five per cent interest rate. It did not appear that the second group could develop a profitable operation for a few years on the basis of this assistance. In September of 1966 an IRR was presented proposing a second loan to COFISA and a loan to the new group of businessmen. The IRR was rejected by the CAEC. The Mission was urged to attempt to bring the new group into COFISA in connection with a second loan to benefit from the economies of scale inherent in a single larger organization.

Despite major Mission efforts, few members of the alternative group are prepared to purchase part of the new COFISA issue. Part of the problem is a clash of personalities among the leading figures in each group, but the major problem is that, even if the alternative group should purchase 10 or even 25 per cent of COFISA's shares, it would not be entitled to even one seat on the COFISA board. There is no Costa Rican law providing for minority representation.

Negotiations with COFISA thus made slow progress. An IRR was approved by the CAEC in May of 1967. It became increasingly apparent that the over-encouragement with fiscal incentives of industry in Central America was creating a weak assembly-oriented industrial structure and serious fiscal problems. Costa Rica did not ratify the Central American protocol mildly limiting industrial fiscal incentives until early 1968. The Mission did not believe that additional assistance to industry had a high priority for AID.

Finally in early 1968 COFISA developed more interest in a second AID loan as it began to develop a backlog of good projects for which it lacked funds as its lines with foreign banks were used to the extent believed wise. The Mission took advantage of this interest to explore with COFISA the possibilities of converting it into an institution to finance high priority investment in agriculture, the processing of agricultural production and industries which can export outside the CACM. Negotiations on these points have resulted in the proposal presented in this paper.

B. Borrower

1. Legal Status

The Corporación Costarricense de Financiamiento Industrial, S. A., COFISA (Costa Rican Industrial Financing Corporation, Inc.) was legally established in San José on August 29, 1963 as a private corporation.

2. Organization

The Board of Directors of COFISA is composed of the Chairman and six members. Each of the present members of the board or his family hold some shares although it is not required that they be shareholders. The

Board is elected to a four-year term by the General Assembly of stockholders with one vote for each share of stock held. The individual board members are eligible for reelection.

The staff of COFISA includes a manager, an assistant manager, an executive secretary, an accountant, a chief of operations, three loan officers, three secretaries, three office boys and one part-time lawyer. A Costa Rican consulting firm which has working arrangements with many Central American, U. S. and European firms performs feasibility studies for COFISA, usually assigning a specialized engineer to each study.

A Vigilance Committee with three members is elected every two years by the General Assembly. The function of this Committee is to audit the meetings of the Board of Directors; although members of the Vigilance Committee do not have a vote in Board of Directors decisions, they may participate in discussions. The present Vigilance Committee collectively controls a total of about two per cent of the total COFISA stock issue.

The Board of Directors meets at least once each week. Its main function, other than the handling of internal business, is that of a loan committee. The Manager, who is present at Board meetings but has no vote, presents credit requests on whose eligibility the Board passes. Criteria for project eligibility follow the general requirements for development projects. The criteria have been improved over time partly because of continual dialogue between COFISA and USAID. A project is first declared eligible; it may then be presented as is, if sufficiently detailed, or it may be sent back to the applicant or to COFISA's technical or financial staff for further study and/or development. When an eligible loan project is presented to the Board for final consideration, the Board fixes the interest rate and establishes the collateral and other details. Board decisions are made on the basis of a simple majority, and AID concurrence is sought only as required by the Loan Agreement, i.e., when a director, officer or principal stockholder of COFISA is the sub-borrower, if the subloan is in excess of $200,000, or if an equity position is to be undertaken.

As remuneration for their services, Board members receive ₡150.00 ($22.50) per meeting, and Vigilance Committee members receive ₡150.00.

3. Ownership

No individual shareholder or family may own more than 5 per cent of COFISA's stock. In March 1968, the number of individual owners had risen to 181. However, among the 181 shareholders, 20 now hold more than $15,000 equivalent worth of COFISA stock each - individual holdings larger than 1.4 per cent. At least 65 per cent of the shares are in the hands of not more

than 12 per cent of the total stockholders since some shares are held in an individual's own name and, at the same time, in that of one or more of his companies, even though the 5 per cent maximum limit is not violated. The Board of Directors owns in total approximately 22 per cent of the stock of COFISA. Thus, despite a numerically substantial ownership base for Costa Rica, effective control rests in relatively few hands.

This concentration of control has not been abused. Other Central American development banks as well as most Central American businesses have even more restricted ownership, and control in some other private CACM development banks rests with an even smaller group. Furthermore, the number and magnitude of COFISA loans made to all COFISA stockholders, not just those owning 5 per cent of the total issue, are not as large as had been expected at the time the 1963 Capital Assistance Paper was written when it was anticipated that individual members of the Board of Directors, composed of prominent, able and aggressive businessmen, would be borrowers of substantial magnitude. That this has not occurred as yet can be seen in Table One showing total lending of COFISA and AID funds to entities in which any COFISA shareholder, not only the largest owners, have financial interests.

In fact, the totals in Table One greatly exaggerate the amount of loans for which participation of the borrower in the ownership of COFISA might have affected the decision to make the loan. For example, loans to Industria Nacional de Arroz, S. A. are included only because the manager of COFISA (also a shareholder) holds 2 per cent of a company which holds 15 per cent of the borrowing company. The loan to CANCO, S. A. is included because CANCO holds 20 COFISA shares. Loans to Industria Nacional de Cemento, S. A. are included because many COFISA shareholders also hold stock in this widely held company. Although some COFISA directors are also directors of Cemento, less than 10 per cent of Cemento stock is held directly or indirectly by COFISA stockholders. The owners of Industrias Barzuna hold less than one per cent of COFISA's stock. Fábrica Saprissa is included only because a holder of a small interest in Saprissa holds 212 COFISA shares. A shareholder in Laboratorios Luz has 53 COFISA shares. Eliminating just the cases mentioned above reduces the total of loans from all sources to companies with a stockholder interest from $3.8 million to $2.3 million. Only $700,000 of the $5.0 million AID funds are included in the revised total.

A COFISA study indicates that only 7 per cent of its loans have been to companies in which members of the board or the manager and their families have an interest of 33 per cent or more. Even this percentage is exaggerated since the loans to Compañía Agrícola Santiago, S. A. were made before its owner became a member of the COFISA board (he and his family own only a small block of COFISA shares). Exclusion of these loans would reduce loans to companies of board members and the manager to 3 per cent. In short, COFISA has been managed as a development bank serving all Costa Rica, not as a stockholders club.

TABLE I

TOTAL COFISA LENDING TO FIRMS IN WHICH ANY COFISA SHAREHOLDER IS KNOWN TO HAVE ANY INTEREST
(In dollars)

| No. of Loans | Name | AID Funds | COFISA Funds | Repayment Funds | Lines of Credit Funds |
|---|---|---|---|---|---|
| | AGRICULTURE & LIVESTOCK | | | | |
| 1 | Ramón Aguilar Castro | | 7,518.80 | | |
| 1 | Hurtado, Ltda. | | 4,511.28 | | |
| 2 | Industria Nacional de Banano, S. A. | | 60,000.00 | | 3,759.40 |
| 1 | Frutera Atlántica, S. A. | | 3,579.40 | | |
| | FOOD PRODUCTS | | | | |
| 2 | Hacienda Santa Inés, Ltda. | | 51,127.82 | | |
| 3 | Central Agrícola de Cartago, S. A. | 7,518.80 | 7,518.80 | 15,105.75 | |
| 3 | Beef Products Co., Ltda. | | 23,007.52 | 22,556.40 | |
| 2 | Proyectos Industriales, S. A. | | 5,263.16 | | |
| 4 | Industria Nacional de Arroz | | 18,045.12 | 3,759.40 | 320,300.75 |
| 2 | Orange Crush de Costa Rica, S. A. | 35,000.00 | 15,037.60 | | |
| | TEXTILES & LEATHER | | | | |
| 5 | Fábrica Saprissa, Ltda. | 56,722.94 | 10,000.00 | 15,037.60 | |
| 4 | Fábrica de Tejidos Los Leones, S. A. | | 55,639.10 | 173,613.82 | |
| 8 | Industrias Barzuna, Ltda. | 140,000.00 | 248,120.30 | 103,975.19 | |
| 1 | Fábrica de Calzado El Progreso, S. A. | | 45,112.78 | | |
| 1 | Industrias Mil Colores, Ltda. | 8,495.30 | | | |
| 1 | Tenería Primenca, Ltda. | 30,075.19 | | | |
| | WOOD (Except Furniture) | | | | |
| 1 | Aserradero y Depósito de Maderas Barbará, Ltda. | 4,812.03 | | | |
| 1 | Donald R. Stewart, Ltda. | 19,548.87 | | | |
| 1 | Caribbean Veneer Co., S. A. | | 21,148.04 | | |

| No. of Loans | Name | AID Funds | COFISA Funds | Repayment Funds | Lines of Credit Funds |
|---|---|---|---|---|---|
| | PRINTING & PAPER PRODUCTS | | | | |
| 1 | Carlos Federspiel & Co., S. A. | 100,000.00 | | | |
| 2 | Industria Nacional de Papel, S. A. | 14,000.00 | | | 10,563.47 |
| 1 | La Nación, S. A. | 150,000.00 | | | |
| 10 | Editorial La Razón, S.A. | | | 49,939.86 | 79,447.11 |
| | CHEMICAL PRODUCTS | | | | |
| 5 | Laboratorios Luz, S. A. | 30,000.00 | 54,680.39 | | 18,045.11 |
| 1 | Productos Plásticos, S. A. | | | 3,920.19 | |
| 1 | Compañía de Plásticos y Aluminios, Ltda. | | | 15,037.59 | |
| | NON-METALLIC MINERAL PRODUCTS | | | | |
| 3 | Industria Nacional de Cemento, S. A. | 126,799.14 | 120,300.75 | 52,000.00 | |
| 2 | Sauri Continental, Ltda. | | 11,278.20 | | |
| 1 | Sociedad Arena y Grava | | 7,518.80 | | |
| 2 | Ricalit, S. A. | | 52,631.58 | | |
| | METAL & METAL PRODUCTS | | | | |
| 1 | Canco, S. A. | 150,000.00 | | | |
| 2 | Rosago, S. A. | 94,707.55 | | | |
| | NON-ELECTRIC MACHINERY CONSTRUCTION | | | | |
| 6 | Vulcan Engineering Works | 50,000.00 | 41,244.26 | 7,542.60 | 43,481.81 |
| | CONSTRUCTION OF ELECTRIC MACHINERY | | | | |
| 3 | Productos Electrónicos, S. A. | 30,000.00 | 49,624.06 | | |
| 1 | Panatra, Ltda. | 49,762.26 | | | |

| No. of Loans | Name | AID Funds | COFISA Funds | Repayment Funds | Lines of Credit Funds |
|---|---|---|---|---|---|
| | TRANSPORTATION | | | | |
| 1 | Compañía de Plásticos y Aluminios, Ltda. | 48,421.05 | | | |
| 1 | Quirós & Cía., Ltda. | 86,124.09 | | | |
| 1 | Lachner & Sáenz, S. A. | 10,024.65 | | | |
| | INDUSTRIAL CONSTRUCTION | | | | |
| 5 | Urbanizaciones y Carreteras, S. A. | 38,373.14 | 39,093.98 | 18,797.00 | |
| 1 | Barzuna & Vinocour, Ltda. | | 2,255.64 | | |
| 1 | Construcciones Urbina, Ltda. | | | | 13,758.75 |
| | ELECTRIC ENERGY | | | | |
| 3 | Compañía Agrícola Santiago, S. A. | | 37,593.98 | 347,368.42 | |
| | INDUSTRIAL SERVICES | | | | |
| 1 | Lavandería y Dry Cleaning La Margarita | 18,045.11 | | | |
| 2 | Servicios Marítimo-Aduaneros, Ltda. | 22,556.39 | 12,030.08 | | |
| 1 | Proyectos Industriales, S. A. | 2,631.58 | | | |
| 2 | Consultécnica, Ltda. | | 16,552.87 | | |
| 1 | Alberto L. Arce, S. A. | | | 3,383.46 | |
| 2 | Talleres Industriales Carrazo, Ltda. | | 18,045.11 | 22,556.39 | |
| 1 | Construcciones Urbina, Ltda. | | | | 30,000.00 |
| 1 | Daniel Ratton Thiery | | 3,007.52 | | |
| | INVESTMENT DEVELOPMENT | | | | |
| 1 | Omar Dengo Obregón | | | 7,788.00 | |
| 1 | Edmund Woodbridge Mangel | | | 4,984.89 | |
| | TOTAL IN DOLLARS | 1,241,036.51 | 1,174,238.38 | 817,426.70 | 519,356.40 |

4. Loan Policies

COFISA, upon being organized, advised AID that its main activity would consist of making loans or participating in the equity financing of private industrial enterprises which are financially sound and contribute to the economic development of Costa Rica. It was anticipated, however, that among other activities in which COFISA might participate would be the issuance of guarantees, underwriting stock issues, offering technical assistance to clients and trade in foreign exchange. The categories of industries to be financed included basic raw materials, i.e., forestry products, agricultural industries, sea food industries and mineral extraction; manufacturing industries including all production activities involving more or less extensive processing or requiring a large amount of equipment; and service industries.

Contrary to what is reputed to be characteristic of the granting of loans through the existing nationalized banking system or of "street" transactions through which short-term money is made available at high interest charges, COFISA proposed to make loans based in large measure on the appraisal of a project's economic and technical feasibility, rather than relying primarily on the adequacy of collateral.

Prior to the initial disbursement of AID funds, COFISA submitted a proposed operations program including an identification of the kind of loans it would make and general procedures. This proposed program noted that while COFISA would not finance agricultural activities directly, it expected to help develop the agricultural resources of the country by financing processing industries that use agricultural products for food or as raw materials for other industries. COFISA also agreed not to finance ventures which might result in the increase of production of any agricultural commodity in world surplus. COFISA contemplated playing a substantial promotional role in attempting to evaluate deposits of mineral resources. It emphasized the promotion of industries which would increase Costa Rican exports as well as substituting for imports.

COFISA also indicated it would not approve subloans for projects dependent on continuation of high protective tariffs. The stated basis of this policy was COFISA's aim of increasing the efficiency and competitive ability of Costa Rican industry. Although COFISA expected that equipment financed by subloans would normally be secured by chattel mortgages and, possibly, additional property mortgages, it expected to rely mainly on the feasibility of each project, its earnings prospects, the financial position and managerial/technical abilities as the main determinants in considering loan applications.

Beyond the colón and dollar funds made available under the AID loan, which were to be lent for not less than two nor more than twelve years for the importation or CACM acquisition of equipment, fixed assets (excluding land), long-term inventory needs, raw materials and industrial construction costs, COFISA planned to open lines of credit with private U. S. and other commercial banks for short-term lending to borrowers whose needs would meet the general development criteria established.

COFISA's program of operation also envisioned equity investments in new share issues, normally to be made in combination with loans. Such activity was not only consistent with COFISA's role as an industrial development institution but also conducive to the eventual formation of a stock market in Costa Rica.

COFISA began to make loans for agricultural production in 1967, and it is expected that COFISA will expand its role in agricultural lending. Otherwise, its basic policies have not changed.

C. Evaluation of Performance Under First Loan

1. Principal Purpose Accomplished

In November of 1963, AID authorized a loan of $5.0 million to COFISA "to facilitate the establishment of a private development corporation and enable it to make medium and long term (two years to twelve years) loans and take equity participation so as to promote the creation and expansion of private industrial enterprises in Costa Rica". The building of a new institution, which was the principal purpose of the first loan, has clearly been achieved. COFISA is established. It makes medium and long term subloans and takes some equity participations. By March 31, 1968, COFISA had made 449 loans for a total of $11.2 million; 55 of the loans for $2.6 million were made to cover fixed investment in new industrial establishments, and 61 operations for $1.7 million to provide working capital to new industries. A total of 132 loans for $2.8 million financed fixed investment in expanding firms and 201 operations for $4.1 million working capital in expanding firms.

2. Operating Methods Unusually Good

The project Committee is pleased with the results of COFISA's operations and its modus operandi. Its board has become a high-quality loan committee bringing together more diverse talent than any comparable organization in Costa Rica or most other developing countries. The board members have been willing to spend time and effort in studying loan applications far beyond what could normally be expected for the compensation received. Most board members consider their work in COFISA is important to help the development of Costa Rica. The attachment they have to COFISA is illustrated by the request of one board member who was recently appointed manager of the Central Bank to join

the Vigilance Committee and continue working with COFISA as he could not legally continue on the board while serving as Central Bank manager. This director has only a small financial interest in COFISA.

COFISA clients who were interviewed, including several who were turned down, were unanimous in complimenting COFISA for the dispatch with which it deals with applications. Those whose loans were for expansion indicated the expansion would not have occurred or would have been postponed were it not for COFISA. COFISA's major "competitor", the Bank of Costa Rica which administers several IDB credits, favors a second loan to COFISA although it complains that joint financing operations are difficult because COFISA wants the first mortgage which is the usual security for its loans.

Interviews with about 25 borrowers by members of the USAID and the project committee indicate a higher percentage of borrower satisfaction with COFISA than is normal in the banking business. No borrower complained that COFISA's lending rates or collateral requirements are unreasonable. It would appear logical that businessmen would prefer to borrow from the Bank of Costa Rica because the exchange risk is carried by the Bank and a greater proportion of local cost financing is generally available while the interest rate is about the same as COFISA's. However, the interviews indicate the opposite is the case. Several of the companies interviewed have had loans from both COFISA and the Bank of Costa Rica, and a couple noted that COFISA's interest rate is higher but they prefer dealing with COFISA. The main factor in this preference for COFISA appears to be that COFISA handles loan requests in a business-like way and acts rapidly, while borrowers have experienced long delays with the Bank of Costa Rica.

During the period in which the first AID loan was disbursed, industry was a leading sector in the Costa Rican economy with production increasing by 11 to 14 percent per year. COFISA's loans made an important, although unmeasurable, contribution to this rapid growth, not only because of the investment COFISA itself financed, but more important because of the domestic and foreign investment it drew into projects through the leverage available from its loans.

3. Lending Distributed by Industry as Expected

Table Two shows the breakdown of COFISA loans by industry. The general pattern conforms to what might be expected in a developing country. Essential consumer goods industries, capital goods for construction, and natural resources export industries generally develop first in an industrializing country. There is a temptation in 1968 to criticize COFISA for lending too heavily for assembly-type industries and not enough for the industrialization of Costa Rican raw materials. Given the national priorities of 1968 such criticism would be warranted, but COFISA loans made in 1964-66 tended to comply with the then current national (and AID) priority of emphasizing industries which could export to the CACM even if raw materials had to be imported.

The data in Table Two indicate that much of COFISA's lending went to areas now considered priority. The largest single field of activity has been foodstuffs with over 20 percent of the AID funds. The manufacture of shoes and clothing is second; the garment industry is increasingly based on CACM raw material and is highly competitive within the area. In general, prices are below those in the United States although not yet as low as some areas in the Far East. Shoes are made from local raw materials, and one factory to which COFISA has made loans began exporting outside the CACM recently. The textile industry is in third place. Much of this industry processes local cotton for the growing garment industry. Other industries based on local raw materials are electrical energy (all loans were for hydroelectric plants), wood products, and agriculture. Over 55 percent of AID funds were used in the above-mentioned six industry groups.

4. COFISA Loans Have Encouraged Imports But Not Monopoly

None of the industries assisted by COFISA enjoys monopoly status within the CACM, the so-called integration industries, although some have high tariff protection and/or duty free import and other tax concessions. Costa Rica has now taken the lead in the CACM in pressing for limitations on the tax and other incentives offered to industry to control competition for new plants among the member countries. The original Fiscal Incentives Treaty was executed and ratified but subsequently revised to accommodate Honduras. The revised protocol awaits ratification in Guatemala and Salvador. In the

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## TABLE II

### COFISA. DISBURSEMENTS BY ACTIVITY FROM INCEPTION TO MARCH 31, 1968

(Thousands of dollars)

| | Total Disbursements | COFISA Capital & Reserves | AID | Repayments | Lines of Credit |
|---|---|---|---|---|---|
| Foodstuffs | 2,380 | 231 | 1,474 | 377 | 298 |
| Manufacture of Shoes & Clothing | 1,716 | 427 | 854 | 391 | 44 |
| Textile Industry | 869 | 246 | 201 | 414 | 8 |
| Industrial Construction | 747 | 238 | 335 | 103 | 71 |
| Electrical Energy | 716 | 353 | - | 363 | - |
| Printing & Paper Products | 601 | 192 | 298 | 42 | 69 |
| Manufacture & Extraction of Non Ferrous Mineral Products | 537 | 200 | 263 | 74 | - |
| Chemical Products | 507 | 102 | 267 | 97 | 41 |
| Manufacture of Electrical Machinery, Accessories & Electrical Products | 506 | 234 | 122 | - | 150 |
| Wood Products | 446 | 69 | 277 | 94 | 6 |
| Industrial Services | 410 | 137 | 198 | 33 | 42 |
| Transportation | 391 | 33 | 351 | 7 | = |
| Metallurgical Industry | 285 | 5 | 245 | 35 | - |
| Machinery Manufacture | 172 | 55 | 66 | 8 | 43 |
| Agriculture & Livestock | 162 | 114 | 15 | 29 | 4 |
| Miscellaneous | 156 | 88 | 22 | 39 | 7 |
| TOTALS | 10,601 | 2,724 | 4,988 | 2,106 | 783 |

view of the AID Central American Industrial Policy Committee, the World Bank and others this protocol does not go far enough. Costa Rica has proposed eliminating most duty free import privileges altogether as a means of encouraging industrialization. Thus, it appears Costa Rica and its fellow members of the CACM are aware that inefficient industrialization must be paid for in reduced public revenues and/or higher consumer prices and that inefficient industry is a result of an indiscriminate granting of incentives. The priorities for investment in Costa Rica have changed.

The common CACM tariff on many items remains quite high. Many of the protected industries have received financial assistance from COFISA and the project committee visited several. The manufacturer of Manhattan shirts complains of the competition from Van Heusen (manufactured in Honduras); a relatively small canner of meat described the problems and advantages in competing with large foreign-affiliated canneries in El Salvador and Nicaragua. In short, it appears that because of competition within the CACM consumers have not been required to bear an unduly high share of the costs of industrialization in the majority of industries financed by COFISA. On the contrary the propensity to import may have been increased by an actual reduction of prices to consumers leading to greater consumption of goods with a high import component. Much of the loss of public revenues at the customshouse may eventually be offset by gains in corporate income tax receipts☆/ and other taxes.

It has not been possible to make meaningful estimates of the amount of product value added by the Costa Rican industries assisted by COFISA that import most of their raw materials. Some of the plants visited by the project committee; e.g., a radio and television assembly shop, appear to add little except labor to the imported components; nonetheless, inexpensive skilled labor is an important competitive advantage enjoyed by Costa Rica. It was the major

☆/ In Costa Rica corporate income taxes like individual income taxes have a progressive rate schedule. The World Bank study of Central American industry points out that this acts as a disincentive to the establishment of large firms and a reform to create a separate fixed rate corporate tax has been prepared by a technical committee with CIAP assistance and will probably be submitted to the Costa Rican Assembly in 1968.

reason given by a Japanese textile firm for locating in Costa Rica rather than elsewhere in the CACM. These industries have the possibility of encouraging subsequent growth through vertical linkages, e.g., the production of cabinets for the radios and TV sets.

Nevertheless the low value-added industries with tariff exemptions are a serious national problem. It can be shown that COFISA has financed few of the most glaring examples of tax evasion such as in the cosmetic industry. Both its loans to automobile assemblers were made after the industry was established to finance additional operations increasing the local value added. Thus COFISA has not contributed substantially to the most undesirable aspects of the industrial structure developing in Costa Rica and the CACM. The Costa Rican authorities are now taking measures to redirect the industrialization pattern, including a freeze on incentive contracts for industries new to the CACM which do not have substantial local inputs.

5. Profits Larger Than Expected

COFISA has earned substantially larger profits in its first years than projected in the first loan paper, partly because the projections were based on a four instead of a five million dollar AID loan. The projected income statement forecast a loss of $57,500 in the first year followed by a profit of $66,791 in the second year. In the first year (ended September 30, 1965) COFISA had a deficit of approximately $32,000 after provision of $35,700 to bad debt reserve. In the year ending September 30, 1966, COFISA earned $116,000 after deducting taxes and reserves, or 11.6 percent on share capital. The extra $1.0 million in AID funds plus higher re-lending interest rates provided the higher earnings. The estimates of administrative expenses were good ($100,000 projected as against $102,000 actual in the second year). In the year ending September 30, 1967, COFISA showed a net profit after taxes of $153,860 after provision of $48,450 to reserves; administration expenses were $125,654. The balance sheets and income statements for COFISA's first three years of operation are shown in Annex Two.

COFISA has not yet been able to pay the 12 percent maximum cash dividend to which it is limited by the conditions on the first loan. For the

1965-66 year AID permitted a smaller allocation to reserves than called for in the loan agreement and COFISA paid a 6 percent cash dividend plus a 6 percent stock dividend. Thus none of the 1965 loss was covered in 1966 and the loss was carried forward into 1967. In 1967 COFISA earned 14.5 percent on its increased capital after taxes and reserves. However, USAID did not give permission to tap reserves for the payment of cash dividends as requested. It was possible to pay only 11.1 percent on the capital increased by the previous year's stock dividend because the 1965 loss had to be covered. This payment was equivalent to a dividend of 11.8 percent on the original capital investment.

COFISA believes it is important to pay as close to the maximum dividend as possible in order to keep up the value of its shares and attract new stockholders for the new issue. It will be able to pay 12 percent in cash for its 1967-68 year when earnings are expected to be 17.3 percent after taxes and reserves. It should be noted, however, that 12 percent is not a high return in Costa Rica; government bonds are available paying 8 percent on face value tax-free, and such bonds can often be purchased at a discount to yield about 11 percent to maturity. Bonds in leading industrial companies pay 12 percent tax free. Commercial banks charge 12 percent on some loans and the street lending rate is often 2 percent a month even for borrowers with the best security.

It would of course be desirable for COFISA to retain more of its earnings to build up the capital it has available for investment. As earnings advance beyond 12 percent the conditions of the AID loans will require such retention. The lack of a functioning capital market discourages such retention in COFISA as well as in other Costa Rican companies. The value of the shares simply does not appreciate to reflect the value of the retained earnings or of a good management record. Despite its excellent record, which would have moved its shares to a substantial premium in most areas with an organized capital market, there have not yet been sales of COFISA stock at a substantial premium. COFISA has tried twice to organize a curb exchange for common stocks as well as bonds under provisions of the commercial code. However, there has thus far been too little activity to support such an operation.

6. Few Equity Positions Taken

A disappointing aspect of COFISA's performance has been its slowness in taking equity positions. To date COFISA has acquired equity in three companies for a total equity investment of $98,000 or roughly 10 percent of its equity. One such equity investment resulted from a work out situation. A rice processor who had borrowed from COFISA was in default. Rather than foreclose on the machinery, COFISA and the other creditors reorganized the company and added some new capital for which COFISA received $33,000 in shares. COFISA also made two loans totalling $75,188 which carry conversion rights; i.e., the debt securities can be exchanged for stock at an agreed price at the option of COFISA. The problem is basically that solid closely-held firms or family businesses simply do not want to bring in new partners even when a major expansion of equity is needed. Generally, those borrowers willing to sell shares have such poor earnings prospects that COFISA is not interested in acquiring equity. The legal structure in Costa Rica gives no protection to minority stockholders and COFISA is understandably reluctant to take small equity positions, in firms where it does not have Board representation. Many firms furnish no financial information to the public.

The failure of COFISA to take more equity positions has been unfortunate not only because equity positions would begin to lay the base for a capital market but also because many, perhaps most, Costa Rican enterprises are undercapitalized and chronically short of working capital because of this undercapitalization. In many cases COFISA has made short-term loans when a purchase of new equity would have been a much better long-term solution to the financing of the enterprise. COFISA is being given an incentive to take equity positions in such cases under the second loan by permitting the use of AID funds for the import of raw materials or intermediary products even for non-priority projects when COFISA takes an equity participation.

In mid-1967 COFISA requested USAID authorization to make loans to individuals to purchase shares in new or expanding companies. COFISA argued that through such loans it could support more risky ventures since its funds would be secured by the total assets of the borrower not just by the stock in the new or expanding company. At first USAID authorized such loans with the limitation that COFISA itself must purchase equity in the company of the same amount as its loan to an individual permits him to purchase. In making

this concession the USAID took into account COFISA's problem of taking small equity positions without Board representation. By making a loan to purchase stock to a businessman known and trusted by COFISA, the Board could feel reasonably sure COFISA's interests as an equity holder would be protected; it could in fact make arrangements with the borrower to represent its shares.

Later, COFISA argued that many companies and families are unwilling to make shares available both to COFISA and an investor and the USAID removed the limitation that COFISA itself must purchase shares when loans for share purchase are made. The project committee believes the limitation that COFISA take equity equal to any equity purchases it finances should be reinstated in connection with the second AID loan. Failure to reinstate such a provision would work against the AID objective of encouraging COFISA to take as many equity positions as possible as there would be a temptation for board members or their friends to arrange COFISA loans to take attractive equity offers. Only because of our interest in encouraging COFISA to take equity positions do we even recommend continuing this limited authority to make personal loans for share purchases.

The investment in equity securities is the most important thing COFISA can do toward developing a capital market. A company that wishes to issue shares to the public finds it quite difficult at the present time, largely because investors lack knowledge of or confidence in the firm. If COFISA's name and participation were present, securities would be easier to place. This role is in fact what the old line investment houses did in Europe and the United States during the period of rapid industrialization before the enactment of investor protection laws.

7. Terms Shorter than Expected

COFISA has made shorter term loans than expected and has even used its own funds heavily for loans of less than one year. Table III and Annex Four show COFISA's portfolio according to maturity.

TABLE III

ORIGINAL MATURITY OF COFISA'S SUBLOANS
(in millions of colones)

| Amounts Outstanding September 30 | Total Amount | Less Than One Year | | One To Five Years | | Over Five Years | |
|---|---|---|---|---|---|---|---|
| | | Amount | Percent | Amount | Percent | Amount | Percent |
| 1965 | 14.5 | 3.0 | 21 | 8.1 | 56 | 3.4 | 23 |
| 1966 | 30.5 | 5.4 | 17 | 17.1 | 56 | 8.1 | 27 |
| 1967 | 39.7 | 6.1 | 16 | 22.8 | 57 | 10.8 | 27 |

As COFISA began operations, 26 percent of the amount subloaned was for less than two years (Annex Four). Once there was more time to process and study long-term loans, this proportion dropped to 19 percent in the year to April, 1966. However, as the flow of secondary generation, especially from short-term loans, increased, COFISA has moved substantially into short-term lending, 30 percent of the amount loaned in the year ending March 31, 1967, and 38 percent in the year ending March 31, 1968. However, as Table 3 shows, the percentage of funds loaned short-term may be misleading because these funds roll over so fast. In terms of debt outstanding the proportion with long original maturities has increased. On September 30, 1965, 21 percent of all funds outstanding had originally been loaned for less than one year; by September 30, 1967, this percentage was reduced to 16 percent despite the use of substantial funds from foreign bank credit lines for short-term loans. Offsetting the falling proportion of loans with short original maturities is the fact that medium and long-term loans become shorter term as time passes. The outstanding balance on a three-year loan made in 1965 is in effect a short-term loan in 1967. COFISA has had a tendency to do more short-term business than would be expected of a development bank. There are several reasons for this tendency toward short terms, some unique to Costa Rica and some common in most developing countries.

The most unique factor is the operation of the nationalized commercial banks. Although the commercial banks make loans largely with resources from sight deposits, they tend to make long-term loans. It is

reported that, until recently, two-thirds of commercial bank loans had an initial term of 5 years or more. As the commercial banks do not fulfill the usual function of providing working capital financing, the greatest limitation on industrial or agricultural expansion is often the lack of working capital to operate close to capacity the machinery purchased with long-term loans from the commercial banks. This situation is compounded by the undercapitalization of most Costa Rican firms. In may cases COFISA's short-term loans have a large payoff in increased production. Nevertheless, the purpose of a development bank is to make medium and long term loans and the USAID has discouraged COFISA from becoming overly active as a short-term lender. Use of COFISA's short-term credit lines from foreign banks for such short-term lending is appropriate and we are pleased that the increase in capital associated with the second AID loan will permit COFISA to increase the availability of short-term financing from its credit lines.

A second relatively unique factor is that the commercial banks are extremely slow in processing most loan applications. Such slow processing is usually less important for long-term loans than for short-term loans to cover immediate needs. As COFISA has established a record for extremely rapid processing of loan applications, especially in comparison with the commercial banks, companies with a desperate need for funds often come to COFISA. COFISA is often able to make low-risk loans at relatively high interest rates. Some of these loans are for as little as two or three months. In some cases these loans merely provide COFISA with an interim use of funds pending disbursements for other commitments. Although such lending is not the role of a development bank, because of the unusual Costa Rican situation we do not recommend restricting COFISA's short-term operations with its own funds. We are suggesting an increase in the minimum term of loans with AID funds.

COFISA has made few loans for more than six years, even for new industries and even where grace periods of up to two years were provided. The reason for the limitation to what might be called medium-term lending is that there are few competitive projects in developing countries on which the return is not sufficient to repay a loan within six years. COFISA would prefer to have the enterprise return for a second or third loan for subsequent expansion instead of giving it initial loan terms such that its expansion can be financed out of current cash flow. The USAID supports this COFISA policy as it

is both financially more sound and also gives COFISA a useful occasional review of its clients' operations. COFISA has in fact made several loans to many firms.

Another factor leading to a shortage of working capital and a high demand for short-term loans in developing countries is that new and inexperienced companies tend to underestimate their total capital requirements. When the plant and equipment are paid for, what is left over is working capital. Frequently this is not enough to carry adequate accounts receivable and inventories or to provide sufficient cash to meet payroll and other recurring costs. Construction cost overruns reduce the amount of funds available for working capital. While commercial banks commonly provide this financing to going businesses in developed countries, new firms have difficulty borrowing from banks until they have demonstrated their ability to earn a profit.

The World Bank indicates that a tendency toward short-term lending in the formative years of private development banks is usual. In its report on the conomic development of Central American dated June 1967, the IBRD states: "...the newly organized private financieras can play and have played a major role in developing capital markets. In the early stages of their operations these institutions tended to have a very high ratio of working capital or commercial loans in their portfolios, with very small amounts in equity and long-term investments. This tendency was to some extent to be expected since there has been great demand for short-term funds in the region while the development and processing of long-term loans or equity investments requires more time. It was obviously important to accumulate earning assets as quickly as possible to meet expenses and to give shareholders a quick return. Nevertheless, if these institutions are to serve their objectives which have qualified them for foreign public assistance, longer-term assets of a development type must become a more important element in their portfolios, in particular equity investments in industry." COFISA is representative. Table Three indicates how COFISA's average subloan maturity has lengthened while it was disbursing the AID loans. In 1967-68 when it had much less long-term funds to commit this tendency was reversed (Annex Four).

8. Wider Variety of Staff Skills Needed

COFISA is presently reconsidering its staffing requirements. The contract of a relatively expensive American industrial engineer was not

renewed upon expiration and a Costa Rican consulting firm was hired to provide these services. AID agreed to this change. It is the view of the project committee that COFISA and its clients would profit by the addition of an economist to the staff. COFISA should sharpen the economic analysis going into projects. For example, the degree of effective tariff protection, the pricing policies, the number of jobs created, and the public revenues lost should be weighed against one another. There is no question that the staff and Board of Directors of COFISA are capable of running an effective lending institution. However, they are lawyers, bankers and businessmen. Several of COFISA's clients who were interviewed appear to be in need of some economic and general business advice in solving marketing and expansion planning problems. COFISA cannot and should not attempt to manage its clients' affairs. Nonetheless, development banking consists of technical as well as financial assistance and it is largely on this basis that large interest rate spreads are justified. In addition, an agricultural specialist will be needed to review and promote agricultural production and agro-industrial projects stemming from the new thrust under the second loan. COFISA has indicated it is prepared to add these two staff members and will offer salaries on an unusually high scale for Costa Rica to attract qualified Costa Ricans now working in the U.S.

9. Legal Fees

A Costa Rican law establishes fixed fees for registering certain legal documents such as mortgages. For sizable transactions these fees are large in relation to the amount of legal work involved, for example two colones per thousand above one million. It is customary practice in the private sector for enterprises to give such work to their regular lawyers and for the lawyers to provide other legal services at relatively low cost. COFISA uses the legal services of its President's firm, and there have been accusations that the notarial fees on COFISA generated business provide a major benefit to the President and principal organizer of COFISA. The loan economist investigated the situation carefully.

COFISA pays only 500 colones ($75) a month to the firm for the part-time legal services of the three partners. This is an unreasonably low legal fee considering the substantial amount of legal services of various types required by COFISA. When COFISA takes a mortgage on a sub-borrower's

property, the registration is performed by the President's firm. However, much of COFISA's business is done on the basis of notes and other documents not requiring such registration. In fact COFISA requires considerably fewer notarial services and less mortgage security than the commercial banks, and the savings on such fees and commissions were mentioned by several borrowers as a reason for preferring to do business with COFISA. Notarial fees received by the President's firm as a result of COFISA's business do not appear to have exceeded 50,000 colones ($7,500) in any year. Since the AID loan was fully committed, such fees have been much less than 50,000 colones a year. These notarial fees are paid by the borrower, not by COFISA. In effect COFISA reduced the cost of its legal services by directing its business to this trusted firm. It does not appear that the total of the direct plus the indirect compensation received by this legal partnership because of its connection with COFISA is excessive in comparison with the legal and other services rendered. Also there does not appear to be any practical means of changing this relationship. Were COFISA required to spread its notarial services among many firms, the only result would be a substantial increase in legal fees which COFISA would have to pay itself to its regular legal advisors, thereby reducing its profits and the retained earnings it can invest in development.

## II. The Project

### A. Description of the Project

The project is the development of a major private lending institution to make loans quickly on the basis of project analysis to finance private sector projects contributing to the highest priority economic development objectives: increasing exports outside the CACM, increasing and diversifying agricultural production, and relatively efficient industrial import subsitutution based on CACM raw materials. The expansion and modification of the existing private development bank (COFISA) is proposed instead of the creation of a new institution because COFISA has an excellent performance record in complying with the objectives of a previous AID loan, has an established knowledgeable staff and loan committee, and is prepared to increase its own capital substantially in connection with a second AID loan. Thus use of COFISA offers the fastest development results, minimizes the requirement for local cost AID financing, and avoids straining the limited technical capacity of the country while taking advantage of economies of scale and the spread of risks available to a larger banking organization.

Except for farm development and agricultural production COFISA was authorized to make the priority type of sub-loans from the first AID loan. However, less than 35 percent of its funds were used in these categories. Incentives for COFISA to enter these priority fields must be increased if it is to meet the economic needs of the country. The percentage of COFISA loans in priority fields will also be increased by encouraging it to enter the agriculture financing field. The incentives proposed are a concessional rate of interest, 3 percent, for drawings on the second AID loan to finance sub-loans in the priority fields while COFISA will pay 5 percent on subloans not in the priority field. The spread permitted in the priority field will be 5½ points which will be reduced after 5 years when the AID interest for priority as well as other projects will be unified at 5%. The ultimate spread of 5 points after interest rate unification will be generally consistent with the spread to other development banks which have received a second AID loan. COFISA will also be permitted to finance working capital through use of the AID loan to pay for imports of raw materials and intermediaries in the priority fields if the overall loan term is at least three years. Otherwise use of the AID funds is generally limited to equipment. At least $2.5 million of the loan must be used in the priority fields or it will be deobligated, thereby reducing the leverage through AID funds for each COFISA share.

Moreover, disbursements for the priority projects must be approximately as rapid as disbursements against the more expensive but more easily used AID funds. Should a substantial part of the funds earmarked for priority projects not be used, it will also be necessary to deobligate a part of the AID funds not restricted to priority projects. The loan agreement will provide that at no time may disbursements of AID loan funds for projects outside the priority category exceed by more than $350,000 the amount of disbursements of AID loan funds plus loans of more than one year from other COFISA funds for projects in the priority category financed after May 15, 1968. Discussions with the COFISA board and management indicate COFISA wishes to concentrate its lending in the priority fields and it will be able to commit at least $2.5 million of AID funds in the priority fields within two years.

A major factor contributing to COFISA's much increased interest in the AID priority fields is a general change in national priorities. When the first AID loan was made, Costa Rica was just joining the CACM and there was great emphasis on import substitution industrialization to take advantage of the greatly expanded market. AID encouraged such industrialization at that time both through the COFISA loan and the provision of technical assistance to prepare import substitution projects. Both AID and the Costa Ricans have now realized that import substitution, especially that encouraged by fiscal incentives, has gone too far. The critical problem now is increasing exports outside the CACM. The management and directors of COFISA have good business reasons to be skeptical of projects which require fiscal incentives since there is considerable discussion of reducing these privileges. In addition COFISA's borrowers of AID funds carry the exchange rate risk; such risk is minimal for export oriented projects or efficient import substitution, but a substantial devaluation could cause a large loss for a firm dependent on imported inputs and the local market.

One of the most difficult problems in providing AID support for agricultural development is that many agricultural projects do not require a substantial import component. Local currency financing is essential for agricultural development as well as some other areas of foreign exchange earnings such as tourism. The strategy of this loan is to encourage COFISA to use most of its $1.5 million equivalent from its new share issue plus much of the secondary generation under the first AID loan to finance the colon costs of proj-

ects in the priority area. Therefore, the formula above permits COFISA to move faster with AID funds in the lower priority areas to the extent it puts its own funds into the priority areas.

A secondary purpose of the loan is to solidify COFISA as a dynamic and growing development bank covering the entire productive sector. Although the USAID does not believe financing of the textile, chemical, container and some other industries is as important as the priority areas identified above. increases in production in these other areas are needed to maintain an economic balance. Many of the non-priority industries export to the CACM and financing growth of such industries contributes to the objective of strengthening support for the CACM in Costa Rica and encouraging both competition and efficiency in the region. Eventually many industries which do not now qualify for the priority category may improve their efficiency such that they would qualify by exporting, particularly if the Latin American Common Market develops.

AID funds are being made available for these lower priority industries in other CACM countries through both private and public development banks. Moreover, suppliers' credits from most developed countries except the U.S. are now available for such industries from CABEI. Failure to permit COFISA to continue with its financing role outside the priority fields would probably result partly in slower economic growth and partly in a substitution of equipment from other countries (often higher cost) with CABEI funding.

Nevertheless, we propose to prohibit the use of AID funds for low priority industry projects. The Central American Agreement on Fiscal Incentives for Industrial Development (signed in 1962 but not yet in effect) divides industries into three categories:

Group A includes industries producing:

a) Industrial raw materials or capital goods; or

b) Consumer goods, containers or semi-manufactured products, provided at least fifty percent of the total value of raw mate-

rials, containers and semi-manufactured products utilized therein is of Central American origin.

Group B industries must meet the following three requirements:

a) Produce consumer goods, containers or semi-manufactured products;

b) Produce important net benefits in the balance of payments and a high aggregate value in the industrial process; and

c) Utilize, in their entirety or in large proportions, in terms of value, non-Central American raw materials, containers and semi-manufactured products.

Group C includes industries which:

a) Do not meet the requirements set forth for Groups A and B; or

b) Merely assemble, pack, bottle, cut or dilute products; or

c) Pertain to industries expressly listed in Annex I.

The industries excluded in the annex are those producing drinks, alcoholic or not, tobacco products, perfumes, cosmetics and related products except soaps. No loan may be made with AID funds for industries in the C category. The Mission is encouraging COFISA to consult with the Secretariat of the Central American Common Market, SIECA, to define the categories more precisely.

The second loan differs from the first in a number of ways. As is the case with the other second AID loans to development banks, the interest rate is higher and the full amount of the loan is tied to US procurement.

The first Loan Agreement contains a requirement that loans to or investments in firms in which " members of the Board of Directors, Officers,

or principal stockholders of the Borrower or their immediate families, have any financial interest" be approved in advance by AID. The CAEC has decided to substitute majority Board of Directors approval with the interested parties not voting for AID approval in these cases and this requirement will be modified.

AID presently requires subloans of more than $250,000 instead of $200,000 to be submitted for prior approval. Since we wish COFISA to make more equity investments, we are recommending that equity investment be treated the same as loans as has been the policy adopted in all recent development bank loans. The present reserves (legal and bad debts) seem adequate. They differ only slightly from the reserves maintained by the other AID-assisted development banks, and we are recommending continuing the present system of reserves.

COFISA will find it easier to make disbursement for the procurement of US raw materials than for US equipment. We propose to restrict the use of AID funds for raw materials and intermediaries procurement to the highest priority projects and projects in which COFISA takes an equity participation equal at least to the financed imports other than machinery and equipment.

Although COFISA is one of the most widely held companies in Costa Rica, AID is already subject to considerable criticism for giving such substantial assistance to a relatively small group. In order to broaden its ownership and to reduce criticism suggesting that COFISA is a closed club, we shall require that at least $500,000 equivalent of the new shares be sold to persons not shareholders of COFISA on December 31, 1967.

For the first time COFISA will not only be permitted but encouraged to use AID funds to finance agricultural production, equipment and farm improvement. This change is responsive to the needs of the Costa Rican economy, the priorities of the AID program as well as the request of COFISA and the recommendations of the AID Central American Industrial Policy Committee. We believe COFISA's Board of Directors together with the proposed agricultural specialist to be added to the staff contain enough agricultural expertise to permit effective appraisal of agricultural projects. A maximum relending interest rate of 8½% to sub-borrowers will also provide a meaningful incentive to applications for priority projects.

B. Justification of the Project

The USAID does not believe consolidation of a viable private industrial development bank and the provision of more funds for industry are sufficient justification for a second AID loan to COFISA. Because COFISA has performed so well, making sound loans to outsiders and keeping its administrative costs low, it does not have the same requirement for additional concessional AID support as did the private development banks in other Central American countries. Some may argue that the lack of a private commercial banking system makes the need for a dynamic and growing private development bank greater in Costa Rica than in other Central American countries where there are aggressive private commercial banks, including branches of U.S. banks. However, Costa Rica has chosen to keep deposit banking in state hands, and it is not an AID role to attempt to offset the results of this national decision, which was fully debated as recently as 1967. It should also be noted that Costa Rica has the highest interest rate structure in Central America, giving COFISA advantages in borrowing from higher interest rate sources. Costa Rica also has the most unstable exchange rate, making dollar loans more risky, however.

The justification for this loan is not to strengthen COFISA but to use it. The USAID believes the highest priority requirement for foreign financing in the productive sector is credit for agricultural diversification. Such diversification is needed to make the economy and particularly foreign exchange earnings less dependent on coffee and to help resources move out of coffee production. The resources which may move are more apt to be capital, management, technical skills and labor than land, although some diversification may even prove profitable enough to encourage diversification of land use.

Many of these diversification projects require integral lending for agricultural production, processing and marketing. Moreover, they require lending based on project analysis more than collateral requirements. The nationalized banks do not appear to have the flexibility to handle such lending and the expansion of commercial bank credit is being limited severely in connection with efforts to avoid devaluation. The Government has suggested the establishment of a new public sector institution, perhaps with private sector participation, to promote and finance diversification projects, and a group of

private agriculturalists had suggested the formation of a new private development bank along the lines of COFISA to concentrate on agricultural production and processing. USAID believes there are many self-evident advantages to using the existing, established institution over creation of a new institution along either of the above lines, particularly as many of the advantages of the above institutions can be incorporated. The Government has already established an autonomous center to promote exports and investment. COFISA has indicated it is prepared to work closely with the center. Once the center interests investors in a diversification project, COFISA would consider financing it. Some of the potential investors in a new agricultural development bank have indicated they will purchase part of the new share issue of COFISA and negotiations for loans to some members of this group are already in the preliminary stage. Moreover, AID would have to provide local currency for subloans to a new institution while COFISA can finance local currency needs partly from repayments on earlier industrial loans. Thus we conclude that making additional funds available to COFISA is theoretically the best means of financing the needed diversification.

The principal reservation is that COFISA may prove too conservative to play an active role in the more difficult and uncertain diversification field. As the risks are greater in this field, COFISA will have to take more equity participations to participate in the large profits of the successful ventures and cover the losses in the unsuccessful. The loan is being structured such that the funds can be deobligated and used in an alternative way if COFISA does not move vigorously into the priority fields.

Although USAID believes agriculture offers the best field for expansion of exports outside the CACM, there is no reason to prejudice purely industrial projects which can export to world markets. Such projects provide similar opportunities for diversification in the use of capital and labor. Thus these industrial projects are included in the priority category. COFISA urged that efficient import substitution projects be included as they have a similar effect on the balance of payments. Moreover, such efficient import substitution projects are often the initial stage of export industries. The principal problem is defining the efficient import substitution industries. The USAID has established a formula, but only experience will show its workability.

Since priority projects will generally have to compete on world markets, a concessional rate of interest to the lending institution is justified to support competitive entry into a difficult market. COFISA will be partly compensated for the greater risks through this low AID interest rate. Perhaps the projects with the greatest risk will be those financed from COFISA's own funds to cover local costs. Since AID funds can be used only for imports, there is an element of protection against loss in the goods imported. Thus, although the concession rate of 3 percent may not seem justified for some of the projects actually financed, such as milk processing equipment for the large cooperative, it must be kept in mind that we expect the earnings on these projects to be risked in other projects which may require few imports.

The above discussion fully justifies the funds to be used for priority projects, but why should COFISA be authorized any additional funds for industrial lending in such fields as the textile and printing industries? The USAID is divided on this issue. Some believe no funds should be authorized for use outside the priority fields. Some believe COFISA plays a useful role in financing industrial development and such additional funds can be justified on the basis of creating support for the CACM and contributing to the growth of the economy and employment, especially since low-value added industries are ineligible. Others take a middle ground supporting COFISA's position that there is not yet enough business in diversification and export industry lending to support the development bank and that it needs to continue with the business for which it was originally established to carry its overhead, to justify such a large loan and increase in capital (which provides more local currency for the priority fields), and to press forward the development of such industries as wood products, chemicals and textiles which may not yet qualify for the priority category but must grow as the economy grows if the demand for imports in these fields (largely from other CACM countries no more efficient than Costa Rica) is not to increase rapidly and complicate the balance of payments problem.

There are also technical reasons for supporting additional funds for domestic industry. A smaller loan would mean a smaller increase in capital as only the leverage of the loan makes the shares an attractive investment, and a smaller issue would result in much less broadening of COFISA's ownership. Failure to make dollars available for domestic industries would force COFISA to use much of its secondary generation to continue its lending relationships with its best industrial clients. Thus, in part making these dollars available

liberates colones for the priority projects. Of course, these problems would be overcome through strict conditions on the AID loan, but COFISA has indicated that its shareholders will not accept the dilution of their original equity if such strict conditions are imposed. Continuing making AID funds available for some domestic industries is the price of taking advantage of the strong established development bank to move funds into the priority field.

There is another strong argument for a private organization in the diversification field. The establishment of new productive activities is difficult and complicated. Government institutions in many countries have suffered large losses because projects were not sufficiently studied. The profit motive is an important restraining factor in weeding out unworkable projects, even if it means a good project is occassionally rejected.

The Foreign Assistance Act, overall U.S. policy, and the AID Central American Industrial Policy Committee all recommend use of private institutions whenever possible. If the cost of using a good private institution is to make some AID funds available for a use somewhat below the highest priority, it may be a price well worth paying in terms of the efficiency with which the AID funds are used.

The World Bank family shares this preference for private institutions. The World Bank does not plan to continue financing capital equipment through the Central Bank as it did between 1955 and 1963. The IFC now deals only with privately owned institutions, and most of its potential projects in Costa Rica would be joint projects with COFISA if COFISA has funds available from the second loan. The same is true of ADELA.

C. The Effect of Higher World-Wide Interest Rates

When the first Central American development bank loans were made, AID believed the original seed capital supplied by AID would sufficiently strengthen the banks to permit them to finance future growth by borrowing from private sources or harder-term international lenders. When, in 1956, several development banks had committed their first loans and their shareholders capital, they found they were unable to contract long-term loans from other

sources. There were several reasons for this. First, money was generally tight and expensive in Europe and the United States; second, the moderate interest rate lenders (IBRD, IDB, and Exim) said they would require government guarantees of repayment or, in their absence, a substantial history of earnings and ability to service debt; third, higher risk private lenders (IFC and "Edge Act" companies) required a rate of return which makes it impossible for development banks to relend the funds profitably. Similarly, the level of local interest rates was sufficiently high to prohibit profitable operations with any funds that might be borrowed from that source. In Costa Rica first class industrial bonds pay 12 percent. The development banks were able to negotiate short-term credits from foreign commercial banks; however, these funds could not be used to finance their major development activities because they would risk an impossible liquidity squeeze by borrowing short term and lending long term.

The development banks were also limited by market forces as to the amount of new share capital they could raise. The Banking business is essentially borrowing money at one price and lending at another. If the stockholders were to increase their own equity contribution without acquiring any more debt capital, they would be lowering the average rate of return on invested capital since they would dilute whatever leverage the original shares enjoyed by dividing it with the new shares.

In view of these factors, AID decided to consider second loans to the development banks to continue their growth. Second loans in Honduras, Panama and Nicaragua were authorized in FY-67. The Costa Rican USAID did not recommend a second loan to COFISA in FY-67, although COFISA's funds were all committed, because other development areas had a higher priority as explained above.

There is reason to believe that these banks will be able to finance future growth from other sources. With a loan and investment portfolio of approximately $10 million they will be able to operate with a smaller spread between the interest they earn and the interest they pay and the second long-term AID loan will increase their borrowing base since private medium-term lenders tend to look at the long-term AID funds as close to equity capital.

D. The Place of the Project in the Country Program

The FY-69 Program Memorandum (August 1967) identified the improvement of public sector economic policies as AID's first priority goal. The three policies to which particular focus is directed are: (1) closing the fiscal gap, (2) agricultural diversification away from coffee, and (3) revised emphasis in industry to stress exports and efficient high value-added import substitution.

During the past year the dialogue between the USAID and the Government has resulted in substantial progress on all three priority goals. Action has been taken to reduce the fiscal gap by more than half. The first AID program loan in Central America was justified by this self-help. However, the fiscal problem continues and the prospects for 1969 are for a much larger deficit. Thus consideration of a second program loan, which was indicated as the highest priority AID loan in the program memorandum, has been postponed pending additional fiscal action. In the meantime, the Government will find it easier to resolve the fiscal problem if the economy continues growing rapidly. Performance continues good with an average 6 percent growth rate in real terms over the past three years. There are indications the growth rate is slipping below this rate in 1968, and early approval of the COFISA loan will provide another injection of investment funds to help maintain rapid economic growth in 1968 through 1970 and thus indirectly help the Government resolve the fiscal problem, both through a higher income base to tax and through a general atmosphere conducive to new tax action.

The economy of the country and exports are being diversified rapidly. In 1969 bananas are expected to surpass coffee in export earnings. Minor exports to markets outside the CACM have started in a substantial number of fields. Among products now being exported for the first time are yuca, tires, cut flowers, shoes, gloves, women's underware, dry-cell batteries. An export and investment promotion center has been created to develop additional diversification and export products; major work is already underway on pine trees, macademia nuts, and a pond fish for domestic consumption. The proposed loan provides direct financial support for such diversification projects. COFISA has already made loans to firms exporting all but two of the new ex-

port products mentioned above. Early approval of the loan is needed to reduce the bottleneck of financing for diversification projects.

The Costa Rican Government alone cannot revise industrial policy because Costa Rica is in a common market. Should Costa Rica refuse industrial incentives to a firm, it can go next door to Nicaragua, obtain the incentives, and then export the product to Costa Rica. Thus an incentives policy tighter than its neighbors merely results in the loss of both revenues and jobs instead of just revenues. However, Costa Rica has taken the lead in pressing for CACM changes in industrial policy. Meantime, it has modified its own incentivespolicy to make it one of the toughest in the area. The COFISA loan will provide financing for precisely those industries which should receive emphasis, and the preferencial interest rate to COFISA and to the borrowers for these industries will increase interest and investment in these fields even before there is a formal change in CACM policies.

The USAID believes self-help in Costa Rica has been impressive in FY-68 and justifies a substantial input of AID resources, even though the fiscal and balance of payments problems have not been fully resolved. Most Costa Rican economic policies are already among the best in Latin America. The fiscal deficit is not the result of heavy spending on the military, there is none, nor on prestige type projects. The deficit is because of large spending on education, health and development of infrastructure, the key objectives of the Alliance for Progress. Over half the employees of the Central Government are school-teachers, and taxes are already the highest as a percent of GNP in the CACM. Incentives for agriculture have been improved during the past year through an increase in the support prices for rice and beans and by permitting the domestic price of beef to rise somewhat closer to the export price. Plans have been made for a large expansion of agricultural research and extension services with the assistance of an IDB loan. Roads are being built in almost every part of the country.

In 1968 the Planning Office expects the rate of industrial expansion to slow from the 11 to 14 percent of recent years to about 8 percent, the same as the total increase in GNP in current prices. The rate of increase in agricultural production is expected to increase sharply. Thus the revised emphasis of the second loan to COFISA fits the revised national priorities.

The Country Team gives the highest priority to the second malaria loan because failure to continue funding that project will result in tremendous losses allowing malaria to spread to areas where it is now controlled. After that loan the Country Team gives the highest priority to the second COFISA loan and urges its rapid approval with the conditions proposed in this paper such that disbursements can begin promptly to assist in maintaining the rapid growth rate and to reduce the pressures on the monetary authorities to expand credit beyond the scope of the stabilization program .

## III. Economic Aspects

### A. Industry in the CACM and Costa Rica

The problems of industrial development in Central America were examined by both AID and the World Bank in 1967 (final report AID Ad Hoc Industrial Committee, San José A-434, June 1967 and volume IV of IBRD's Economic Development and Prospects of Central America, June 1967). The general thrust of these studies is that the CACM has proceeded too rapidly with fiscal incentives for industrialization, especially exemptions from import duties on raw materials and intermediaries, that insufficient attention has been given to basic industries and industries of scale, and that there is a tendency to provide virtually unlimited tariff protection to almost any industry establishing in the area. The reports recognize the high priority of additional investment in industry but suggest that consideration be given to basic changes in industrial policy to obtain more CACM value added and industries to process CACM raw materials and export outside the area and that more emphasis be placed on the agricultural sector. The details of these reports will not be repeated; however, the conditions on this loan conform both to many specific recommendations and to the general thrust of these basic studies.

Because of the problems of modifying CACM industrial policy, there is a tendency to forget that industrialization is what the CACM (and later the LACM) is all about. The CACM was formed because of the desire of the member countries to industrialize and the need for regional trade to support industrialization. While there is some inter-member trade in agriculture, it is the expanded trade in manufactured goods which has been the significant feature of the CACM. Intra-regional trade in the period 1962-67 grew from about $50 million to nearly $200 million with manufactured products accounting for some 85 per cent of the increase.

The CACM has about 15 million people, but the economy is only about the size of Nebraska or Arizona. Most of the trade has been in products with relatively simple production; however, nearly half the growth in trade occurred in non-traditional products (fertilizer, petroleum products, chemicals and metal products) all of which are produced by industries relatively new to the region and which are dependent to a great extent upon imported raw materials. Many of these are also dependent upon high tariff protection and liberal tax incentives because they are essentially mixing or assembly operations with low value added. On the other hand, some of these assembly industries produce a product with a high labor content; e.g., the metal fabricating industry, which tends to make the Central American product competitive. Some of these industries would be competitive without excessive protection because of the high cost of transport from other regions. Consequently, all assembly or mixing industries cannot be condemned out of hand.

We are limiting the use of AID funds to prevent use in projects with the most obvious abuses of incentives, but there is no doubt that some of the 5 per cent AID funds will be used for industries which Costa Rica and the CACM should not encourage at this time. It is the history of developing countries, including the United States in its time, to go too far in encouraging inefficient industry during the initial phases of industrial development. The cost of such inefficiency should be considered a part of the cost of development; moreover, in the case of the CACM, there is the major additional benefit of promoting regional integration.

The World Bank study attempts to apply the results of Professor Hollis Chenery's work for the United Nations relating industry's share of gross domestic product to population and per capita income. The results of this exercise are set forth in Annex III. Costa Rica, which has the highest per capita income in the CACM, has achieved a level of output somewhat below the expected values.

B. Relationship of Loan to Tight Domestic Credit

The Central Bank has embarked on a program of tight domestic credit to reduce pressure on the exchange rate and the balance of payments. At the same time the commercial banks are attempting to make their portfolios more liquid by concentrating new lending from domestic resources in short maturities. Thus there will probably be few commercial bank medium and long term loans for industry or agriculture during the next 12 to 18 months except for loans at least partly financed abroad.

Table Four shows the growth of commercial bank credit during the past four years. The amount of loans for both industry and cattle increased by over 15 per cent a year and for the rest of agriculture by over 8 per cent. These credit increases as well as the first AID loan to COFISA and other foreign financing have been extremely important in establishing the current growth rate of about 6 per cent in real terms. As domestic credit will grow only slowly, if at all, under the Central Bank's stabilization plan, there is a major need for additional foreign resources to maintain the growth rate.

The Table also illustrates the importance of COFISA entering the agricultural field. The rate of increase in credit for agriculture, excluding cattle raising, was only a little over half the rate of increase for industry although agriculture is the basis of Costa Rican exports. Credit for cattle did increase rapidly, partly because of the IDB loans in this field.

TABLE IV

COMMERCIAL BANKS LOANS
(Outstanding Balances in Millions of Colones)

End of February

| | 1964 | 1965 | 1966 | 1967 | 1968 | % Increase 1968 Over 1964 |
|---|---|---|---|---|---|---|
| Agriculture * | 257.2 | 339.8 | 323.7 | 346.4 | 356.8 | 38.7 |
| Cattle, Hunting & Fishing | 136.8 | 165.5 | 199.0 | 207.5 | 242.6 | 77.3 |
| Manufacturing & Extraction | 131.7 | 166.4 | 185.7 | 180.6 | 220.0 | 67.0 |
| Electricity | 2.7 | 3.3 | 6.3 | 6.8 | 7.4 | 174.1 |
| Commerce | 52.8 | 56.1 | 53.1 | 43.4 | 33.7 | -36.2 |
| Services, Transportation and Storage | 54.7 | 62.4 | 70.2 | 61.7 | 66.1 | 20.8 |
| Housing | 27.6 | 24.0 | 16.9 | 12.5 | 19.0 | -31.2 |
| Personal Credit | 48.9 | 57.5 | 56.7 | 54.6 | 59.1 | 20.9 |
| Other | 12.3 | 20.2 | 34.9 | 34.7 | 26.9 | 118.7 |
| TOTAL | 724.7 | 895.2 | 946.5 | 948.2 | 1,031.6 | 42.3 |

* Includes Rural Credit Department

The Table also shows the results of the major efforts which have been made by the banking system to concentrate credit in the directly productive fields. The absolute amounts of credit for commerce and housing were reduced.

The Table overstates the effective increase in credit for industry, however, because of what might be called the credit costs of integration; credits for the export of industrial goods are included in the industry classification. As industries trading in the CACM have developed, there has been a heavy demand on the national credit resources of each country to finance sales to the other countries. For example, the opening in 1967 of the large Firestone tire plant in Costa Rica creates a substantial demand on the Costa Rican banking system for credit to discount the export sales of tires; usually 80 per cent of the invoice is financed. From the point of view of the CACM, as a whole, the industrialization process greatly increases the need for credit. For example, before the formation of the CACM, tires were imported and there was little domestic bank credit to finance tires since little credit is extended to finance retail sales. The distributors took advantage of what foreign suppliers' credits might be available. When production starts in the CACM, the local manufacturers are pressed to provide at least the same terms as the previous foreign suppliers. The composition of imports switches from tires

to various raw materials, but suppliers' credits for raw materials are usually shorter than for finished products. There is a net reduction of working capital credit furnished from abroad which must be offset by domestic credit. Once competition among various manufacturers begins in the area, there is a tendency to increase credit terms, especially since the banks in each country tend to give export credits generously. Thus credit is provided indirectly to commerce and consumers.

In short the development of the CACM and increased trade among the member countries increases the requirement for domestic bank credit. The COFISA loan does not meet this need directly, but it will provide additional medium and long term financing in agriculture and industry while the commercial banks are shifting resources to these shorter term needs. Thus, in a sense, the COFISA loan does cover one of the most difficult and immediate costs of integration and supports the U. S. objective of assisting integration efforts.

C. Relationship to Other Foreign Lending

AID-DLC/P - 535 of April 1967, supporting a $5.0 million loan for relending to small farmers, argued that other foreign loans were covering the needs of the medium and large farmers. However, developments during the past year make additional credit for large farmers essential, especially for the diversification projects that have the highest national priority in order to reduce the dependence of the economy on coffee.

In early 1967, it was planned that the needs of large farmers would be met from a $5.0 million IBRD loan which would be the first stage of extensive IBRD lending for export agriculture, a $2.5 million loan for bananas from National City Bank, loans from Chase of $5.0 to $20.0 million and, to a lesser extent, use of the IDB $5.2 million loan directed primarily at medium-size farmers. The IBRD loan has not yet been made; the amount under consideration has been reduced to $3.0 million, and the credit is limited to production of bananas, cattle, pineapples and cotton. The loan will probably be authorized shortly, but there are already applications for more than twice the amount available for both bananas and cattle. There is no indication the IBRD plans to make a second loan soon. AID funding may not be used for cotton; thus the only area in which there will be a possible overlap with the proposed COFISA loan is pineapples. As the IBRD loan may not finance facilities to process pineapples, a role for COFISA lending with AID funds may develop even in this field.

The National City Bank increased its banana loan to $3.0 million, but it is already fully disbursed. A new loan of $6.5 million for bananas and other agriculture has just been arranged with Chase Manhattan Bank. Negotiations are underway for additional banana credits from foreign commercial banks. Meanwhile, considerable foreign capital is being invested in the banana business without passing through the banking system. The AID loan itself can have only a

limited role in the banana industry. Aside from the largest foreign companies which import their own heavy land clearing equipment, most of the foreign exchange investment is in service companies engaged in land clearing, aerial spraying and other production operations and in railway construction and rolling stock. Thus the banana farmers themselves have little requirement for AID funds although they may need COFISA's local currency. COFISA may also make some loans with AID funds to the service companies for the import of U. S. equipment. Because of the large amount of credit going into bananas and the uncertainties of the banana market, COFISA loans outstanding at any time to the banana industry including companies servicing banana farms or providing transportation for bananas will be limited to $500,000 from all sources of funds except as AID may otherwise agree.

The funding now proposed from other foreign bank credits to the banking system would essentially be a switch of seasonal financing of coffee and sugar from Costa Rican resources to foreign resources without an alternative use of the Costa Rican resources. This operation is primarily a means of improving the balance of payments, not of providing additional domestic financing.

The IDB loan to medium-size farmers has been committed only slowly until recently. There is still about $3.0 million uncommitted. Utilization is now accelerating; over $1.0 million was committed during the first four months of 1968. Commitments will be even faster once arrangements are made to use the funds through the Rural Credit Boards as well as the commercial department. Most of the loan will be committed by the end of 1968.

The National Bank pays a higher interest rate than COFISA, 4 per cent, but it does not pass on an exchange rate risk as the IDB loan is from the Fund for Special Operations and is repayable in colones. ~~Thus, although COFISA may offer loans at 7.5 per cent or less compared with the National Bank's 8.0, the exchange rate uncertainty would appear to make the National Bank's loans relatively more attractive.~~

In addition to filling gaps where funds for purely agricultural purposes are not available, COFISA will offer an important new type of integrated lending including financing for both the agricultural production and its processing. Such financing is especially important for most of the diversification crops. It is not enough just to grow strawberries. They must be frozen or canned for export. COFISA is uniquely qualified to provide such integral financing for agricultural production, processing and marketing because its operations are themselves integrated in a small staff. The commercial banks have different departments for agricultural, industrial and commercial credits. Moreover, as a private institution COFISA offers more security on the timely availability of funds. In many diversification projects the financing and construction of the processing (industrial)

facilities does not begin until well after there has been a major investment in the agricultural parts of the project. COFISA can guarantee the availability of such credit when it is needed. The commercial banks do not have the procedures to make such guarantees and experience has shown that even when guarantees on credit availability are made, the credit is often delayed by a year or more. Such delays have bankrupted more than one promising Costa Rican diversification project.

Entry of COFISA into the agricultural field may have multiplier effects by providing some competition for the nationalized commercial banks. The banks now rely almost exclusively on security for agricultural loans. COFISA will rely on project analysis. For example, some of the dynamic but undercapitalized firms which rely on renting land instead of buying it will be eligible for COFISA credits, although they experience great difficulty in borrowing from the collateral-oriented commercial banks.

The international lending agencies are providing three sources of funds for industrial lending in Costa Rica. The IDB has made two loan packages to the Bank of Costa Rica, a nationalized commercial bank. Suppliers' credit from most developed countries are available through the Central American Bank (CABEI), and AID has supported COFISA. All international lending for imports of machinery and equipment competes with private supplier credit financing.

The first IDB loan to the Bank of Costa Rica (BCR) was for $3.0 million in 1962. It is fully disbursed. Two loans were approved in 1965 and signed in 1966, one for $2.0 million from ordinary resources at 6 per cent and one for $2.2 million from the Fund for Special Operations at 3.25 per cent. Most of these funds have now been committed, and the Bank of Costa Rica expects to apply for additional IDB funds before the end of calendar year 1968 as soon as all funds are committed and disbursements advanced. At the end of February 1968 only $1.4 million of the $4.2 million had been disbursed. However, the current exchange system is accelerating use of this loan. The BCR offers one major advantage to the sub-borrower in comparison with COFISA; the BCR carries the exchange risk while COFISA denominates its subloans financed with AID funds in dollars. The interest rate from both institutions is the same, about 9 per cent. Despite this advantage, which can be offered only because the BCR is state-owned, many borrowers favor COFISA and COFISA has moved funds at approximately the same rate as the BCR. It should also be noted that the BCR has been able to finance procurement in most European countries and Japan from its ordinary capital resources while financing U. S. procurement from the Fund for Special Operations. COFISA was limited to U. S. procurement under the first AID loan, once the $1.25 million for CACM procurement was exhausted.

In most respects COFISA's record compares favorably with that of the BCR. It has made some loans turned down by the BCR because of insufficient collateral. COFISA's record on subloan repayments is excellent while the

BCR is only now improving its record with technical assistance from the IDB. The choice between two active industrial lenders has been useful in keeping both on their toes. The availability of funds from the BCR avoids the charge that AID is establishing a private monopoly in the industrial lending market and avoids the always present danger that COFISA will attempt to maximize its profits at the expense of national development.

During the first six months to one year that the proposed second loan to COFISA is available, the BCR will probably have only limited funds for commitment as its application to the IDB is processed. This slowing in its competitor's operations will help COFISA commit its loan rapidly, just as COFISA's relatively limited fund availability, since the second IDB loans to the BCR were signed in August 1966 , has helped the BCR move funds rapidly. The loan committee believes such staging is useful in assuring rapid commitment and disbursement of funds while maintaining the competition between the two organizations.

With the exchange rate situation increasingly uncertain, COFISA will find it much harder to move its funds passing on the exchange rate risk if the BCR does not pass it on also. It would seem no additional Fund for Special Operations loans should be made to the BCR until it agrees to pass on the exchange rate risk.

The reported philosophy of CABEI is to limit its industrial lending in the member countries to projects requiring loans of at least $0.5 million. As COFISA generally does not wish to concentrate as much as $0.5 million in a single loan, there is theoretically little competition. However, CABEI has loaned a total of $7.1 million since 1963 in Costa Rica, making 15 loans excluding increases in loan amounts. Of this 15, three were for $1,000,000 or more, three between $400,000 and $500,000, four between $200,000 and $300,000, two between $100,000 and $200,000, and three less than $100,000. Thus CABEI has in fact provided competition for COFISA. The two CABEI loans most recently approved in Costa Rica are for $60,000 and $100,000. CABEI subloans can only be made to "regional" projects, but this qualification does not really exclude anything since any plant that imports raw materials from or sells output to one of the other member countries qualifies as regional. Because of its eagerness to move some of its over $50 million in suppliers' credits from Mexico, the U. K., Switzerland, Holland, France, Italy and other countries, CABEI is encouraging applications for industrial credits of all sizes in Costa Rica. In general, CABEI's terms are about the same as COFISA's. However, COFISA will not face serious competition until CABEI's reputation for taking a year to process credit applications is changed.

COFISA has been prepared to engage in joint operations with either CABEI or the BCR. It is also encouraging a more active lending role by ADELA, a COFISA stockholder. One of the most interesting projects now being discussed between COFISA and CABEI is a major expansion of rice production for export. Initial studies indicate a loan of about $3.0 million is needed to generate annual experts on the order of $10.0 million. CABEI has approached COFISA on joint financing because much of the needed field equipment can be procured most economically in the U. S. and CABEI does not have funds for U. S. procurement. The project would be eligible for the lower interest rate under the AID loan and the lower interest rate might make it more economical to purchase some of the other equipment in the U. S. as well.

The project committee concludes that the proposed $5.0 million for COFISA do not increase the available foreign financing in either the agricultural or industrial field above the immediate needs of the economy and that provision of these funds through a private flexible institution is highly desirable not only to cover some needs not now being met by the public institutions but also to provide an element of choice for the borrower (competition).

D. The Amount of the Loan

There are several restrictions on the amount of the loan which it is prudent to make available to COFISA at this time: (1) the amount of funds it can commit for U. S. procurement in not more than 24 months for good projects in the priority areas; (2) the amount of new domestic capital which COFISA can raise with the 4 to 1 ratio of AID loan to equity (after the second loan) which has already been established in Central America; (3) the amount of supplementary resources available to COFISA from other lenders once the AID loan is made (which depends heavily on conditions in international capital market); (4) the amount of AID support justified by recent Costa Rican self-help; (5) the ability of its staff to handle increased volume; (6) the amount COFISA can commit for U. S. procurement in non-priority areas with the exclusions provided.

1. Needs for Priority Lending

Assuming Costa Rica should be developing a minimum of $5 million a year in additional exports outside the CACM in non-traditional products and a capital output ratio even as low as 2 to 1, a minimum of $10 million of investment a year is needed in the priority fields. This calculation makes no allowance for investment in efficient import substitution industry or non-export agriculture projects. Thus even $2.5 million of AID funds plus an equal amount of local currency from COFISA's capital issue and rollovers would meet no more than a quarter of this requirement during the next two years. However, it is not clear that the projects to use even this $5 million from COFISA will be

available or that the projects developed will require substantial amounts of U. S. procurement. COFISA now has relatively few such projects pending: establishment of a manufacturer or low quality colonial furniture to compete with Yugoslavia in the U. S. market, the growing and processing of strawberries, the growing and processing of tomatoes for export. The total value of probable loans of this nature now pending does not appear to exceed $0.5 million.

COFISA is considering two large milk processing loans, each about $0.5 million. One would assist Borden establish a plant to process condensed milk in remote Guanacaste to substitute for imports throughout the CACM; the other would finance a modern ice-cream manufacturing facility for the large and efficient milk cooperative to help promote the consumption of ice-cream and improve nutrition levels. If both of these projects develop satisfactorily and the new Export and Investment Promotion Center identifies several additional opportunities, more than $2.5 million of AID funds might be committed for the priority fields in less than 24 months. As subsequent studies may indicate problems in some of these projects, it appears the priority project area is being fully funded, if not over funded, at least for U. S. procurement for a 24-month period. We believe the priority of this area justifies liberal rather than conservative availability of funds.

2. Ability to Increase Local Capital

Given the uncertainty of the present financial situation in Costa Rica, COFISA is reluctant to undertake a share issue of more than 1.5 shares for every original share issued, even with the requirement to sell a substantial block of shares to new stockholders. To the extent the issue is too large it will either not be sold or will have to be sold to new stockholders at no premium at all, a substantial penalty for existing shareholders. Only after long negotiations has COFISA agreed to an issue as large as $1.5 million equivalent. Thus the ability to raise local capital in a 24-month period coupled with the 4 to 1 ratio accepted in Central America for AID leverage in private development banks limits the overall size of the AID loan to about $5 million. COFISA proposed extending the time period in which purchasers of the shares could make payment to three years. The USAID does not wish to enter such a long-term arrangement with COFISA because it is still an unproven lending institution in the priority project area.

3. Supplementary Resources

Additional lines of credit from foreign banks will undoubtedly be made available to COFISA once the second AID loan is approved. In May the COFISA manager had conversations with several important bankers during the IDB meeting in Bogotá, and approval of a second AID loan will lift a cloud which has formed on COFISA in the minds of some private bankers because AID has

not made a second loan as it has to other Central American development banks. However, conditions in the international capital markets are now tight. U. S. restrictions limit the expansion possibilities for many banks. Thus the amount of supplementary resources which will become available may be quite limited, perhaps no more than another $1.0 million. Failure to obtain more supplementary resources may mean the lack of sufficient accompanying local currency resources will limit the use of AID funds (available for U. S. procurement only), especially in the high priority fields where there are greater local currency needs.

4. Costa Rican Self-Help

Costa Rican self-help during the past year has been substantial and a loan somewhat larger than $5.0 million would be justified on this ground.

5. Staff Ability

Although a larger volume of lending will require some additional staff, the arrangement with the largest Costa Rican industrial consulting firm and the solid basic staff and loan committee indicate that COFISA's staff could handle a considerably larger loan than $5.0 million even with a sharply increased role in the priority fields.

6. Possible Commitments in Lower Priority Areas

As a new financing enterprise in a smaller economy COFISA was able to commit more than $2.5 million for industrial projects outside the priority areas in less than 24 months. Assuming the IDB does not make an unusually favorable loan to the Bank of Costa Rica, it appears virtually certain COFISA could exhaust its more expensive funds within the time period even with the limitation to machinery and equipment from the U. S. and a minimum term of three years. We hope the COFISA board will reserve some of these funds for additional projects in the priority areas if such projects become available. The availability to make non-priority loans is not a limiting factor. Commitments for lower priority projects will be limited by the rate funds are used for priority projects. As it is not the principal purpose of this loan to finance these lower priority projects, $2.5 million appears to be sufficient to make available.

Conclusion

Were the loan to be $4.0 million with only $1.5 million for the lower priority projects, the smaller sale of share capital and less supplementary resources from foreign banks would restrict the availability of local currency financing in the high priority field. Were the loan $4.0 million with half for

each priority, less resources would probably be available for the high priority field than needed and justified by the country's self-help. Were the loan $6.0 million, either the high priority field would tend to be overfunded at $3.0 or $3.5 million, especially in relation to local fund availability (secondary generation would be no greater), or additional funds would be made available for the lower priority projects which the USAID does not believe is justified at least until there is a full modification of CACM industrial policy. Thus a loan of $5.0 million is recommended.

E. Prospects for Repayment

COFISA is a well-managed development bank which has already proven its ability to earn substantial profits. Other sections of this paper, particularly IV. B, deal with the problem that COFISA may earn too much; thus there is no reason to believe its cash flow would ever be insufficient to service the AID loan. Cash dividends will be restricted to 12 per cent, and the reinvestment of profits as well as the establishment of a substantial bad debt reserve will ensure its financial solvency. The relatively short term of its loans insures a large cash flow.

However, it is possible that exchange restrictions might limit COFISA's ability to remit principal and interest to AID. Under the exchange restrictions the Central Bank imposed at the end of 1966, COFISA's position is ideal. It has not only been declared eligible for the official rate for servicing its registered debts, including the AID loan, but exchange has been made available promptly not only for payments to AID but also to service its lines of credit from foreign commercial banks. Such conditions may not always continue, however. Thus the loan is somewhat more risky for AID than a similar loan to the public sector.

It is proposed that the Government be offered a two-step arrangement to spread the debt service pressures on the Costa Rican balance of payments over the most concessional AID terms instead of the 20 years being made available to COFISA. A similar two-step agreement has been proposed to cover the first COFISA loan, and two versions have already been signed by the Government. The first agreement was turned down by the Finance Committee of the Assembly when neither COFISA officials nor the Finance Minister appeared to defend it. After signing the second agreement, the Government found it could not legally make the commitment because the Assembly had not authorized it to sign such an agreement. The Costa Rican Constitution is now being amended to remove the legislative authorization step, and the two-step agreement will again be submitted to the Assembly later in 1968. Should the Government find it convenient, one agreement might be submitted covering both the first and second COFISA loans. If the Assembly approves a two-step agreement, COFISA

will service the debt in colones and the Government, instead of COFISA, will have the problem of purchasing exchange for remittance to AID.

The Government has had little interest in the two-step on the first loan thus far because the grace period to COFISA has not yet expired and the difference between Government receipts and its payments to AID would be minimal. The grace period to COFISA expires in 1969 although the Government would still be within its grace period. Thus substantial amounts will be available from the first loan for mutually agreed economic and social development projects and it is expected the Government will increase its efforts to obtain approval of the two-step agreement.

A debt service projection for the public sector 1965-1990 is on page 162 of AID/DLC/P-535 and a complete analysis of the balance of payments is in AID/DLC/P-648, pages 19-21.

F. Effect of Loan on U. S. Economy

The loan will finance $5.0 million additional procurement of goods and services in the United States. Most of this procurement would not otherwise be made in the U. S., primarily because the borrowing firm would not have the funds for the purchases without the loan. In some cases the Costa Rican firm might eventually find the funds from another source, but the procurement might then be made outside the U. S., especially if the financing is from a non-U. S. source such as the CABEI supplier credits. Thus the loan will provide support for U. S. industry, especially industry producing the relatively simple industrial machinery and equipment needed in a developing country and the farm machinery industry. There will be no financing of local costs with dollars under this loan.

In the future, the sale of spare parts and compatible equipment will increase U. S. sales to Costa Rica not financed by AID. Also the strengthening of distributors and agents for U. S. products through this substantial volume of business will tend to increase the U. S. share of the Costa Rican market on a permanent basis.

Some of the projects financed under the priority section of the loan will produce for export to the United States. In most cases these firms will produce items which the U. S. is now importing from other sources at higher prices. The reduction in the price of imports to the U. S. may yield a balance of payments saving to the U. S. In other cases the products exported to the U. S. will make available desired food items during the seasons when U. S. production is not available. In only a few cases will Costa Rican production financed by this loan be directly competitive with U. S. production. Financing which would increase the production of cotton, sugar or coffee will be prohibited.

The increase in Costa Rican exports from projects financed under this loan will permit Costa Rica to import more goods and services. As the U. S. provides 50 per cent of all Costa Rican imports from outside the CACM, the principal beneficiary of increased Costa Rican imports will be the U. S.

Some of the projects financed by this loan will lead to import substitution and a change in the composition of imports. Import substitution tends to be in areas of relatively simple operations and high labor cost. The U. S. is generally not the principal supplier of these products. Thus import substitution tends to increase U. S. exports by switching the composition of Costa Rican imports to raw materials, intermediaries, and capital equipment in which the U. S. is more competitive.

## IV. Financial Analysis

### A. The Terms of the Loan

In Section III D a loan of $5.0 million is justified. The standard practice with AID loans to Central American development banks has been to provide a second loan such that the ratio of AID loan funds to share capital is 4 to 1 after the second loan is disbursed and the new share issue fully paid. In Mr. Diamond's basic text on development banks he recommends a ratio of long-term debt to equity of about 4 to 1, and this ratio seems appropriate for COFISA. By 1971, COFISA will have AID loan funds of about $9.5 (two $5.0 million loans less amortization) and $2.5 million of paid-in capital. The ratio will continue dropping as the AID loans are repaid.

The twenty-year maturity and five-year grace period are the terms AID has previously authorized for second loans to Central American development banks. These terms were selected because they provide for a strong capital base necessary to permit subsequent borrowings from other lenders and because they enable the banks to make equity investments and to extend grace periods to their sub-borrowers. Another advantage of the 20-year term is that it controls COFISA's cash dividends for a long period ensuring the reinvestment of funds in the business and in the development of the country.

### B. Profitability

COFISA has been a profitable enterprise as discussed in Section I. In its fiscal year ending September 30, 1968 it is expected to earn at least 17 percent on par value of its shares after taxes and provision to reserves. If there were no new share issue, earnings would continue increasing. Assuming there would be few loans which must be written off and an increased amount of short-term credits from foreign banks would be used as repayments on the AID loan, the profits per share would probably exceed 20 percent, perhaps even more if the staff and other expenses were reduced as the amount of new loans made was reduced. After several years, profits would begin to fall as repayments on the first AID loan reduced the leverage of the equity. However, profits per share in each of the next 10 years would be substantially higher than they will be with the new issue.

The requirement of a large capital increase in connection with the second loan means COFISA will not earn as much per share over the next

decade as it would have without the second loan. Projections have been prepared through 1976 (Annex V, Part 1(a)) which indicate that per share earnings after taxes but before reserve allocations will diminish from the 1968 level during the disbursement period 1969-70. These earnings rise to slightly above 20% during 1972 and 1973 principally as a result of the 3% AID interest rate on the component for priority uses but decline as the interest rate is unified at 5% after the 5 year concessional rate period. Yet these earnings are not excessive in the Costa Rica situation as is demonstrated below but will be adequate to assure a maximum return to equity holders of 12% leaving some funds for expanding COFISA's portfolio. The real possibility of further tax increases in Costa Rica will, of course, be reflected in an earnings decrease. Were AID to insist on charging higher interest for this loan the problem of attracting the requisite additional equity would be greatly intensified as the probability of a 12% return to shareholders became less certain.

Superficially it might seem AID should not assist a private enterprise owned largely by a score of families to earn profits at this level. However, AID wishes private Costa Rican investors to purchase COFISA shares as an investment, not for the purpose of obtaining loans. Thus the return on COFISA shares must be competitive with alternative investments available in Costa Rica. AID is also imposing a limit on cash dividends of 12 percent on capital paid in cash. Such a cash return, even if it is considered to be a certain return, is not competitive with other investments available in Costa Rica.

Bonds of the Government and various autonomous agencies, including the commercial banks, pay 8 percent tax-free. Such bonds are usually available with a clause providing for immediate repurchase. Government bonds without a repurchase guarantee are usually available at substantial discounts, making the yield to maturity as high as 11 percent. The large assembler and distributor of General Motors vehicles has been advertising regularly to sell an issue of 10-year bonds paying 12 percent tax-free. Interest on Government bonds is tax exempt; the borrower must pay tax at the rate of 15 percent on private bond issues to make the interest tax-free. At the moment corporate dividends are tax-free, but a tax reform which would make dividends taxable is now under discussion. A prudent investor would have to consider the strong possibility that his dividends from COFISA would be taxed within a few years. Other investments generally provide higher returns. Consumer finance companies are generally prepared to pay 1.5 percent per month or more for time deposits. Investors in most industrial projects expect to earn 20 to 30 percent per annum on their capital. In short, the investor in COFISA shares actually makes a financial sacrifice, at least in cash return.

Moreover, Costa Rican experience has been that shares in the few public companies have not appreciated to reflect retained earnings or good management. Thus the investor may not even be compensated with a capital gain should he sell his COFISA shares.

The assumptions on which the earnings projections were based appear reasonable and reflect close scrutiny of COFISA's operations to date. Interest receipts are estimated at 8% on the small transitory investment in bonds, 12% on short term loans and 10% on medium and long term loans utilizing COFISA's capital, lines of credit and funds from the first AID loan. The conditions of the second AID loan will require a maximum interest rate of 8½% as incentive to borrowers in the priority area and 10% for others through the initial disbursement period. If world-wide interest rates are reduced in the future from their present high levels, COFISA will have to reduce its rates, especially on dollar denominated loans which COFISA characteristically makes. Thus, interest earnings appear reasonable and may well be overstated for the later year projections of this long term loan.

COFISA assumes its equity investment will increase from 2 million colones at the end of fiscal 1968 to 6 million at the end of 1969, 9 million in 1970 and then stabilize at 10 million colones. Dividends received increase gradually on these investments to 8 percent in 1973. No capital gains on sale of stock are shown in the projection. These estimates appear reasonable for the next few years. Companies in which COFISA purchases equity will be new on expanding and it is reasonable to assume dividends will be restricted for a few years. In the longer run COFISA will perhaps receive greater returns from such equity investments including some substantial capital gains. Thus per share earnings may not taper off as rapidly as expected once the grace period on the second AID loan expires and the leverage on concessional funds falls rapidly. We believe COFISA should have a sufficient profit margin to encourage it to take equity positions, especially in new companies, without concern that its 12 percent dividend would be threatened.

The projections assume less use of credit lines from abroad than we would expect, a gradual increase to 7.3 million colones by September 1969 from about 5 million now. Because of the second AID loan and what we expect will be increased foreign bank purchases of COFISA shares, we believe more than twice as much funds will be available from foreign commercial banks. The margin on these funds is relatively small as it is not always possible to pass on the exchange risk and lend at 12 percent. Nevertheless, this under-estimation probably leads to a slight understatement of future profits.



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It appears the estimate for administration expense is slightly high. Expenses will certainly increase to handle the second AID loan and become more active in agriculture; the salaries and related expenditures of the two technicians which AID is requiring could be as much as 200,000 colones per year. Efficient organization may mean there will not be other personnel needs, but office expenses and travel will increase. However, amortization of organization expenses and of technical assistance (from a U.S. engineer) was 131,000 colones in 1967 and the remaining balance in this account is only about half a million. This operating cost, which was 15 percent of total administrative expenses in 1967, should fall substantially within a year or two. Administrative expenditures would have to be overestimated by 250,000 colones per year (20 percent) to increase the after-tax profits per share by one percent; clearly any overestimation is considerably less than 20 percent. Moreover, no increase in administration expenditures is projected in future years although wages and other costs will undoubtedly rise. After COFISA commits the second AID loan and its funds from its new issue, it might be able to reduce staff, but it is more likely to continue its active role in the economy. The projections do not take into account the future development of the organization.

In conclusion, the terms of the second AID loan, including the interest rates and the ratio to new capital have been designed to yield a proper and negotiable level of profitability. The profit level made available by the first AID loan was too high, and the existence of this extremely favorable situation for COFISA's shareholders greatly complicated our negotiations. Those who may feel the earnings after the second loan are high should keep in mind that profits will be about 20 percent beginning in 1969 if the second loan is not made. However, we do not believe the level negotiated is just the lowest COFISA will accept; we believe the level is fully justified given conditions in the Costa Rican capital market and the threat of devaluation. Moreover, a sufficient profit margin to encourage COFISA to take equity positions in new firms which will not provide a return for some years is necessary to serve both our developmental interest and our goal of helping create a capital market. Also AID is making its second loan when worldwide interest rates are the highest in over 30 years; most economists believe interest rates will fall within a couple of years; should interest rates fall, COFISA will have to reduce its rates for dollar lending and its profitability will be less than shown in the projections.

C. Taxation

COFISA pays income taxes under Costa Rican law which provides for a payment of 122,980 colones on the first 500,000 of profit and 30

percent on earnings above 500,000. In addition, there was a 25 percent surtax for the year ending in 1967. Should this surtax be extended to help reduce the Governments serious fiscal deficit, COFISA's after-tax profits would be nearly 2 percentage points less than shown in the profit projections.

COFISA is a substantial contributor to the Costa Rican treasury. In 1967 it paid 656,916 colones, about one-half of one percent of all income taxes paid in Costa Rica. The projections indicate that COFISA will pay over twice as much tax by 1972.

Its own tax payments are not COFISA's only contribution to the treasury. COFISA has found on more than one occasion that the financial reports submitted to it as the justification for a loan are not the same as used to compute tax liability. In such cases COFISA insists the borrower put his house in order to be eligible for a loan. Some borrowers complain bitterly about the unreasonable conditions of COFISA, especially as the commercial banks, although Government owned, do not exact such obnoxious conditions. We believe such conditions are precisely what is implied by the Alliance for Progress symbol on the back of COFISA's annual report and the title, Alianza para el Progreso en la Empresa Privada.

V. Implementation Procedures and Schedule

A. Increase in Capital

The COFISA board already has the authority to increase the share capital as required by this loan and has written the USAID that it fully supports the increase. However, Costa Rican law provides that the existing shareholders must be given the first opportunity to purchase new shares in relation to their current holdings. Thus, should each shareholder wish to purchase the approximately 1.4 new shares for each share now held (the proportion is less than 1.5 because of the 6 percent stock dividend), there would be no shares available to meet the AID requirement that at least $500,000 equivalent be sold to persons not shareholders of COFISA at the end of 1967. The AID requirement would then require COFISA to increase the amount of the share issue until sufficient shares are available to outsiders. Naturally the COFISA board does not wish to reduce the leverage provided by the AID loans more than necessary. Thus the board plans to call a meeting of shareholders to explain the situation and to work out arrangements for shareholders to turn over part of their entitlement of shares for sale to outsiders. By coordinating this operation COFISA hopes to place the shares at the maximum premium possible with the premium being used to cover part of the cost of the shares bought by existing stockholders. The total cash received from the new issue will be only $1.5 million. Because of the uncertain financial situation in Costa Rica and the size of the new issue, it does not appear that the premium will be large. Also the book value of the stock is less than 5 percent above par because of the relatively large dividends paid.

The basis for paying in the new capital will be the same as the first share issue. The downpayment will be 20 percent of the value with four subsequent equal payments at 6, 12, 18, and 24 months. The Costa Rican law provides that once an individual or company has made a commitment to purchase a share, the company has a legal claim against any assets of the individual or company for any part of the unpaid value of the share. Thus AID has full security that the full amount of the new issue will be paid in once the downpayments are made. The loan agreement will require COFISA's receipt of the 20 percent downpayment on new shares equivalent to at least $1.5 million and proof that at least $500,000 has been taken up by new shareholders as a condi-

tion precedent to the first disbursement.

The loan agreement will also provide that AID disbursements may not be more rapid than pari passu with the payment of the capital subscription. Because of the normal procurement delays, it is not likely that the receipt of funds from the share issue will delay disbursements on the loan at any time.

D. AID Disbursement System

The disbursement of the loan at two different interest rates is a minor complication. This situation will be handled by COFISA's opening letters of commitment with at least two different banks. Each letter of commitment will cover disbursements for either priority projects (3 percent) or non-priority projects (5 percent) but not both. Thus the AID Controller will be able to charge each disbursement against the outstanding capital at the appropriate interest rate by handling the two parts of the loan essentially as two loans initially. Once the loan is fully disbursed, within the grace period, the average rate of interest on the loan can be computed. Thereafter, the rate will be unified at 5%. In all other respects the procurement and disbursement system will be the same as for the first COFISA loan, and COFISA is already familiar with such AID requirements as small business notification and 50-50 shipping.

C. Hiring of Additional Professional Staff

Because it is desirable for COFISA to add highly qualified personnel in the new agriculturalist and economist positions required by the loan, it does not appear appropriate to require that both positions be filled as a condition precedent to loan disbursement. Such a condition would place extreme time pressure on COFISA to hire from a small market of professionals. It is worth waiting a few months for the right man. We recommend the loan agreement provide that COFISA will not firmly commit more than $1.0 million of the AID funds until AID has approved the personnel for these two positions. Such AID approval could be given on the basis of a contract which might not require the individual to begin work immediately.

D. USAID Monitoring of Loan

The most difficult monitoring aspects will be: (1) eligibility for the lower , priority project interest rate, (2) ineligibility of industries classified as Category C by SIECA, (3) assurance that commitments in the non-priority field do not advance substantially faster than commitments of AID and COFISA funds in the priority field, (4) assurance that only machinery and equipment are financed with the non-priority funds.

Both the USAID and COFISA wish to avoid prior approval of subloans by USAID because of the interference such a procedure would cause with COFISA's normal rapid processing and because of the peak demands on the limited USAID staff to handle such cases promptly. USAID investigation of proposed individual loans before they are made would result in client pressures on the USAID for approval and might even result in COFISA's passing USAID some difficult cases knowing that USAID (instead of COFISA) would turn them down. USAID also prefers to have the minimum problem of access to confidential business information. Instead, COFISA will send USAID a list of all new commitments each month including sufficient details to justify the lower interest rate when COFISA has determined it applies. Marginal cases will be discussed in the continual dialogue between COFISA and the USAID at any time. AID will reserve the right to require prior approval for eligibility for the lower interest rate, but this right will be exercised only if review of the monthly reports and subsequent discussion with COFISA indicate COFISA is not following the priorities established in the loan agreement as interpreted by the USAID. Since another provision requires that a loan increasing COFISA's outstandings to any firm to more than $250,000 must receive prior AID approval, there is little possibility COFISA will abuse this confidence during any month. The USAID will indicate the priority it believes a large project has at the time of giving approval.

Should the USAID review after the fact indicate COFISA has violated the loan agreement by financing a category C industry, financing raw materials or intermediaries outside the priority fields or equity participation, or any other loan condition, COFISA will be required to cancel any AID financed letter of credit opened and to refund any funds already disbursed from the AID loan for such subloans. Such refunds will reduce the principal of the loan; they will

not be reprogrammed. Presumably COFISA will then have to finance the sub-borrower from its own resources as it will have a binding commitment.

Past experience indicates a frank and informal relationship between COFISA and the USAID yields a mutual understanding of problems and priorities. The USAID director will play a major role in the COFISA dialogue personally, assisted by the loan officer, the agricultural economist and the Mission economist. It is expected this will be the largest loan being monitored by the USAID at least until the end of calendar 1969, and substantial staff resources will be used to insure compliance with both the above mentioned special conditions and the other conditions typical of all development bank loans. Quarterly and annual reports will be required on the same format as now being provided.

Because of the exchange rate problem discussed in section VI. the loan agreement will provide for a comprehensive detailed review of COFISA's lending operations from the new loan when commitments under the loan reach $1,750,000. Although this review will concentrate especially on the possible substitution of loan financing for other available financing because of the exchange rate system, it will provide an opportunity for a complete review of COFISA's performance. Because of the backlog of pending applications it is expected $1,750,000 of commitments will be reached quickly and this important review will be held in early 1969.

E. Implementation Schedule

1. June

AID loan authorized.
ROCAP regional lawyer prepares first draft of loan agreement.
USAID prepares first draft of implementation letter one.

2. July

Loan agreement negotiated with COFISA board and management.
COFISA shareholder assembly approves contract and makes arrangements for new stock issued.

(No legal steps are necessary to formalize agreement nor implemer project.)
Loan Agreement signed.

3. August and September

New COFISA share issue opened.
COFISA begins processing applications for potential financing under loan; small business and other conditions for procurement move forward although letters of credit not opened.
COFISA intensifies efforts to recruit new staff.

4. October

Final date for downpayments on COFISA shares.
Condititions precedent to disbursement met.
Letters of commitment opened.
First disbursement on loan.

## VI. OTHER ISSUES

### Effect of Devaluation on New Share Issue

Our recommendation requires COFISA to issue $1.5 million equivalent in new share capital. This new capital will be paid in over a 24 month period. The basis for determining the colon equivalent of the $1.5 million is the official exchange rate because it applies to all other COFISA transactions. However, once share purchasers make their downpayments, their obligation for additional payment is fixed in colon amount. Thus, should there be a formal devaluation which would increase the colon value of COFISA's subloans with AID funds and its debt to AID, the ratio of loan funds to equity would be increased even before the share capital is paid in.

Since purchasers of COFISA's new shares are placing their funds in shares with a fixed maximum cash return in colones for the next 20 years (12 percent) during a period of exchange rate uncertainty, we do not believe it is either practical or desirable to penalize COFISA share purchasers with an escalator clause. Such a clause would severely reduce the value of the new shares and would probably make it impossible to sell an issue as large as proposed. An escalator clause is a difficult obligation for most investors since a devaluation usually does not increase their liquidity in colones; thus they might not have the cash flow to handle the increased payments required by such a clause, especially since devaluation reduces the effective working capital of most businesses and therefore places substantial demands on most businessmen. Since they would have a legal obligation to make the payments on the shares under Costa Rican law, an escalator clause with both the amount and possible timing unknown would discourage those with limited liquidity from investing in COFISA. Nor do we believe it is possible to obtain agreement from COFISA's assembly of stockholders to a subsequent issue to maintain the 4 to 1 AID loan to equity ratio. Since the second AID loan substantially

reduces the per share profitability of COFISA and most shareholders are more interested in their return on COFISA shares than on possible loans from COFISA, there is a limit on the conditions which can be imposed.

Should a devaluation increase the effective leverage on COFISA's shares and thus COFISA's earnings, the 12 percent limit on dividends for the full 20 years of the second AID loan insures the continued use of such additional profits for relending and the development of Costa Rica.

# CHECKLIST OF STATUTORY CRITERIA
(Alliance for Progress)

| Criteria | Conclusion |
|---|---|
| **COUNTRY PERFORMANCE** | |
| **Progress Towards Country Goals** | |
| 1. FAA §.208; §.251(b)(1); §.251(b)(5); §.251(b)(6). Extent to which country is: | |
| a. Making appropriate efforts to increase food production and improve means for food storage and distribution. | Although agricultural production has increased faster than population, basic foods are still imported. The country is now intensifying efforts in order to increase rice production by at least 10 percent a year and corn production by over 5 percent. In 1966 corn production was stable and rice output increased only one percent, but in 1967 corn production was up 6 percent and rice 20 percent, and in 1968 both corn and rice output are expected to increase by over 10 percent. This loan will contribute to continuing these rates of increase in later years. The National Production Council purchases and stores the basic grains at support prices fixed before the planting season; in most cases these support prices are higher than U.S. prices. The Council also distributes basic foods at fixed prices through almost 100 of its own outlets in low income areas. |
| b. Creating a favorable climate for foreign and domestic private enterprise and investment. | Costa Rica is creating a favorable climate for foreign and domestic private enterprise and investment. Net private foreign investment is $10 to $15 million per year. The Constitution guarantees foreigners equal rights with Costa Ricans. Major tax benefits are given to encourage both domestic and foreign investment. |
| c. Increasing the public's role in the developmental process. | Creation of Export and Investment Promotion Center with significant public support, formation of rural electric and agricultural cooperatives and credit unions, universal primary education is really achieved and both secondary and university enrollments are growing by more than 10 percent a year. Over 350 land titles are being distributed each year. |

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| *d. Allocating expenditures to development rather than to unnecessary military purposes or intervention in other free countries' affairs.* | Costa Rica has no military forces has no army and is not intervening in other free countries affairs. A substantial part of the budget is devoted to development. |
| *e. Willing to contribute funds to the project or program.* | The Loan is to a private concern and the Government will not contribute but additional shares equivalent at least $1.5 million will be sold in Costa Rica. |
| *f. Making economic, social, and political reforms such as tax collection improvements and changes in land tenure arrangement, and making progress toward respect for the rule of law, freedom of expression and of the press, and recognizing the importance of individual freedom, initiative, and private enterprise.* | Tax measures taken by the Costa Rican Government increased tax collections by over 25% between 1966 and 1968. An AID financed cadastral project is designed to lead to land reform and increased revenues from property taxes. The Instituto de Tierras attacking land tenure problem, and expects to distribute over 5000 titles in the next 5 years. There exists historically in Costa Rica respect of rule of law, freedom of expression of the press and recognition of the importance of individual freedom, initiative and private enterprise. The independent court system is allocated 5% of the total national budget. |
| *g. Adhering to the principles of the Act of Bogota and Charter of Punta del Este.* | The Government of Costa Rica adheres to the principles of the Act of Bogota and the Charter of Punta del Este. Table I (pp. 8,9) of Program Assistance Paper AID-DLC/P-648 shows Costa Rica's, impressive performance on 11 of the 12 objectives in Title I of the Charter of Punta del Este. |
| *h. Responding to the vital economic, political, and social concerns of its people, and demonstrating a clear determination to take effective self-help measures.* | The Government of Costa Rica is showing a responsiveness to the vital economic, political and social concerns of its people. The Government has demonstrated a clear determination to take effective self-help measures, as demonstrated by its efforts in education and taxation. |
| 2. *FAA §.251(b). Information and conclusion on country's efforts to repatriate capital invested in other countries by its own citizens.* | The fiscal stabilization measures now being undertaken should encourage repatriation of capital invested in other countries by its own citizens and the opportunity to invest in this project will also encourage repatriation. |

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*Relations With U. S. and Other Nations*

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| 3. *FAA §.620(c). If assistance to a government, existence of indebtedness to a U. S. citizen for goods or services furnished or ordered where such citizen has exhausted available legal remedies, debt is not denied or contested by such government or indebtedness arises under an unconditional government guaranty.* | Not applicable. |
| 4. *FAA §.620(d). If assistance for any productive enterprise which will compete in the U. S. with U. S. enterprise, existence of agreement by the recipient country to prevent export to the U. S. of more than 20% of the enterprise's annual production during the life of the loan.* | Not applicable because this loan will be made under Title VI-Alliance for Progress (Sec. 251), not Sec. 201 to which Sec. 620(d) refers. |
| 5. *FAA §.620(e)(1). If assistance to a government, extent to which it (including government agencies or subdivisions) has taken any action which has the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property of U. S. citizens or entities beneficially owned by them without taking steps to discharge its obligations.* | Not applicable. |
| 6. *FAA §.620(j). Information whether the country permits, or fails to take adequate measures to prevent, the damage or destruction, by mob action, of U. S. property.* | There is no recent history in Costa Rica of mob action directed against U.S. property. The Government regularly provides adequate preventive police protection. |

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| 7. *FAA S.620(l). Consideration which has been given to denying assistance to a government which after December 31, 1966, has failed to institute the investment guaranty program for the specific risks of inconvertibility and expropriation or confiscation.* | The investment guarantee program for inconvertibility and expropriation or confiscation is in effect. |
| 8. *FAA S.620(o). If country has seized, or imposed any penalty or sanction against, any U. S. fishing vessel on account of its fishing activities in international waters, consideration which has been given to denying assistance.* | No such incident has occurred. |
| 9. *FAA S.620(q). Existence of default under any FAA loan to the country.* | No delinquencies of as much as three months exist on any FAA loan to Costa Rica. |
| 10. *FAA S.620(t). Prohibition on aid if country has severed diplomatic relations with U. S., unless agreements have been negotiated after resumption of relations.* | No such incident has occurred. |
| 11. *FAA S.620(u). Status of the country on delinquent U. N. obligations.* | Costa Rica is not delinquent in its U.N. obligations for the purposes of Article 19 U.N. Charter. |
| 12. *FAA S.209. Information about multilateral assistance being furnished to the country.* | CIAP has reviewed the Costa Rican development program in consultation with other international agencies and supports this loan. |

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| 13. *FAA §.620(a); App. § 107(a) and (b). Compliance with prohibitions against assistance to Cuba and any country (a) which furnishes assistance to Cuba or failed to take appropriate steps to prevent ships or aircraft under its registry from carrying equipment, materials, or supplies from or to Cuba; or (b) which sells, furnishes, or permits any ships under its registry to carry items of primary strategic significance, or items of economic assistance, to Cuba.* | Costa Rica does not (a) furnish assistance to Cuba nor are ships or aircraft under its registry permitted to carry equipment, materials or supplies from or to Cuba nor (b) does Costa Rica sell, furnish or permit any ships under its registry to carry items of primary strategic significance or items of economic assistance to Cuba. |
| 14. *FAA §.620(b). If assistance to a government, existence of determination it is not controlled by the international Communist movement.* | Not applicable. |
| 15. *FAA §.620(i). Information on representation of the country at any international conference when that representation includes the planning of activities involving insurrection or subversion against the U. S. or countries receiving U. S. assistance.* | The Costa Rican Government has not been either officially or unofficially represented at any international conference involving the planning of activities involving insurrection or subversion against the U.S. or countries receiving U.S. assistance. |
| 16. *FAA §.620(n); App. 107(b) and 116. Compliance with prohibition against assistance to countries which traffic or permit trafficking with North Viet-Nam.* | Costa Rica does not traffic or permit trafficking with North Vietnam. |
| *Military Expenditures* | |
| 17. *FAA §.620(i). Existence of determination that the country is engaging in or preparing for agressive military efforts.* | The President has not determined that Costa Rica is engaging in or preparing for aggressive military efforts directed against the United States, or any country receiving assistance from the United States, or any country which sales are made under the Agricultural Trade Development and Assistance Act of 1954. |

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| 18. FAA G.620(a). *Information and conclusion whether country is devoting unnecessary percentage of budget for military purposes and using foreign exchange for military equipment.* | Costa Rica has no standing army, only an internal security force (Civil Police), and has no military expenditures. |
| 19. App. G.119. *Information on reduction in assistance by amounts spent by country for the purchase of sophisticated military equipment.* | No purchases of sophisticated military equipment have been made nor are any planned. |

*CONDITIONS OF THE LOAN*

*General Soundness*

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| 20. FAA G.201(d). *Information and conclusion on legality (under laws of country and U. S.) and reasonableness of lending and relending terms of the loan.* | Loan funds are not to be loaned or reloaned at rates of interest which are excessive or unreasonable for the Borrower and are not higher than the legal rate of interest in Costa Rica. |
| 21. FAA G.251(b)(2); G.251(e). *Information and conclusion on activity's economic and technical soundness, including information on availability of an application together with assurances to indicate that funds will be used in an economically and technically sound manner.* | The borrower has administered the loan funds provided under the first AID loan in an efficient and economically sound manner and contributed greatly to the strengthening and expansion of private enterprise in Costa Rica. The addition of a professional economist and an agriculture specialist to the Borrower's staff, required under the second loan will give added assurance that the loan funds will be used in an economically and technically sound manner. A loan application has been submitted by the Borrower. |
| 22. FAA G.251(b). *Information and conclusion on capacity of the country to repay the loan, including reasonableness of repayment prospects.* | The loan will finance an expansion of exports, and this improvement in the balance of payments situation will be more than sufficient to permit the payment of interest and repayment of the loan. The financial record of the borrower fully justifies confidence in its continued profitable operation such that it will be able to service the loan regularly. |

Best Available Document

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| 23. *FAA §.611(a)(1). Information and conclusion on availability of engineering, financial, and other plans necessary to carry out the assistance and of a reasonably firm estimate of the cost to the U. S. of the assistance.* | Necessary substantive financial planning for the loan has been completed and a firm estimate of the cost of the program to the U.S. has been obtained. |
| 24. *FAA §.611(a)(2). If legislative action is required within recipient country, basis for reasonable anticipation such action will be completed in time to permit orderly accomplishment of purposes of loan.* | No legislative action is required to implement the project. |
| 25. *FAA §.611(e). Compliance with requirement that Mission Director certify, with respect to projects estimated to cost over $1 million, as to the country's capability effectively to maintain and utilize the project.* | This requirement has been complied with ANNEX VII. |
| 26. *FAA §.251(b). Information and conclusion on availability of financing from other free-world sources, including private sources within the United States.* | No financing by other international lending agencies nor private sources within the United States, at interest rates permitting reasonable spread for medium and long term subloans are available to Borrower. |

*Loan's Relationship to Achievement of Country and Regional Goals*

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| 27. *FAA §.207; §.251(a). Extent to which assistance reflects appropriate emphasis on:*<br><br>*a. Encouraging development of democratic economic, political, and social institutions.* | This loan is to a private enterprise to make subloans to other private enterprises, thereby strengthening the private sector of the economy while providing new productive jobs. Morover, the Borrower will be required to sell at least $500,000 of shares (about 20 percent) to persons or firms not holding the company's stock on December 31, 1967. Subloans will be made to cooperatives. |

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| *b. Self-help in meeting the country's food needs.* | The project will assist in financing new agricultural projects or substantial expansion of existing ones, and thereby stimulate self-help in meeting country's food needs. |
| *c. Improving availability of trained manpower in the country.* | The project will provide indirectly, through sub-borrowers, new employment opportunities for professional personnel and skilled labor, but is not directed at providing skilled manpower. |
| *d. Programs designed to meet the country's health needs.* | The loan has no effect on the country's health program. |
| *e. Other important areas of economic, political, and social development, including industry; free labor unions, cooperatives, and voluntary agencies; transportation and communication; planning and public administration; urban development; and modernization of existing laws.* | This activity will contribute significantly to the establishment of new industries and the expansion of existing industries, including establishment of new high priority industries including agro-industrial enterprises increasing exports outside the CACM. |
| 28. *FAA §.251(b)(3). Information and conclusion on activity's relationship to and consistency with other development activities, and its contribution to realizable long-range objectives.* | This activity is consistent with and closely related to other development activities being undertaken or planned and will contribute to realizable long range objectives as explained in Section II D. |
| 29. *FAA §.251(b)(7). Information and conclusion on whether or not the activity to be financed will contribute to the achievement of self-sustaining growth.* | This activity will, by increasing investment in agriculture and high priority industrial projects, accelerate the rate of growth and thereby bring closer the time when Costa Rica will be able to support continued rapid growth from its own savings. |

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| 30. | *FAA §.281(a). Extent to which the loan will contribute to the objective of assuring maximum participation in the task of economic development on the part of the people of the country, through the encouragement of democratic private and local governmental institutions.* | Not directly applicable in view of the nature of this loan. |
| 31. | *FAA §.281(b). Extent to which program recognizes the particular needs, desires, and capacities of the people of the country; utilizes the country's intellectual resources to encourage institutional development; and supports civic education and training in governmental skills.* | The project will broaden the field of activities and considerably strengthen and broaden the participation of individuals, business and industry in, and the operational base of the only private development banking institution in Costa Rica, thereby contributing to the economic progress of the country. |
| 32. | *FAA §.601(a). Information and conclusions whether loan will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; (c) encourage development and use of cooperatives, credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture, and commerce; and (f) strengthen free labor unions.* | Loan is designed to increase the flow of international trade by encouraging the creation of export oriented industries; foster private initiative and competition by providing medium and long term credit at reasonable rates of interest to private firms through a completely private intermediary; and improve technical efficiency of industry, agriculture and commerce through project analysis and guidance provided to sub-borrowers by the COFISA staff. |
| 33. | *FAA §.619. Compliance with requirement that assistance to newly independent countries be furnished through multilateral organizations or plans to maximum extent appropriate.* | Costa Rica is not a newly independent country. |

34. *FAA §.251(h). Information and conclusion on whether the activity is consistent with the findings and recommendations of the Inter-American Committee for the Alliance for Progress in its review of national development activities.*

This activity is consistent with the findings and recommendations of the Inter-American Committee for the Alliance for Progress. In its 1967 review of national development activities CIAP urged the foreign assistance agencies to make available additional funding for diversification and export production.

35. *FAA §.251(g). Information and conclusion on use of loan to assist in promoting the cooperative movement in Latin America.*

Cooperatives will be eligible for subloans and it is expected that as much as 10 percent of the AID funds will be loaned to cooperatives.

36. *FAA §.209; §.251(b)(8). Information and conclusion whether assistance will encourage regional development programs, and contribute to the economic and political integration of Latin America.*

Many of the industries which have received subloans and will receive subloans export a substantial part of their output to other CACM countries. The assistance to these industries strengthens this sub-regional market and the growth of these industries prepares them to compete in the larger Latin American Common Market.

*Loan's Effect on U. S. and A.I.D. Program*

37. *FAA §.251(b)(4); §.102. Information and conclusion on possible effects on U. S. economy, with special reference to areas of substantial labor surplus, and extent to which U. S. commodities and assistance are furnished in a manner consistent with improving the U. S. balance of payments position.*

Entire proceeds of loan will be used for purchases in the U.S. under standard AID procedures, therefore the loan will have no adverse effect on the U.S. economy. As a result the U.S. proportion of Costa Rican imports will be improved and new permanent trading relationships established which will have a favorable impact on the U.S. economy.

38. *FAA §.601(b). Information and conclusion on how the loan will encourage U. S. private trade and investment abroad and how it will encourage private U. S. participation in foreign assistance programs (including use of private trade channels and the services of U. S. private enterprise).*

There are no restrictions against subloans to U.S. citizen or firms and U.S. investment, both in the Borrower and in sub-borrowers is actively encouraged by the Borrower. The loan will significantly increase U.S. commercial exports to Costa Rica. Thus U.S. private trade and investment in Costa Rica will be facilitated.

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| 39. | *FAA §.601(d). If a capital project, compliance with the Congressional policy that engineering and professional services of U. S. firms and their affiliates are to be used in connection with capital projects to the maximum extent consistent with the national interest.* | Professional and engineering services will not be eligible for loan financing. |
| 40. | *FAA §.602. Information and conclusion whether loan will permit U. S. small business to participate equitably in the furnishing of goods and services financed by it.* | Provision will be made for American small business to participate equitably in the furnishing of goods and services financed by this loan wherever possible. |
| 41. | *FAA §.620(h). Compliance with regulations and procedures adopted to ensure against use of assistance in a manner which, contrary to the best interests of the U. S., promotes or assists the foreign aid projects or activities of the Communist-Bloc countries.* | Assistance provided by this loan will not be used in a manner which promotes or assists foreign aid projects or activities of the Communist-Bloc countries. |
| 42. | *FAA §.621. Information and conclusion on how the loan in providing technical assistance will utilize to the fullest extent practicable goods and professional and other services from private enterprise on a contract basis. If the facilities of other Federal agencies will be utilized, information and conclusion on whether they are particularly suitable, are not competitive with private enterprise, and can be made available without undue interference with domestic programs.* | No technical assistance will be provided under the loan. |

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| 43. *FAA §.252(a). Total amount of money under loan which is going directly to private enterprise, is going to intermediate credit institutions or other borrowers for use by private enterprise, is being used to finance imports from private sources, or is otherwise being used to finance procurements from private sources.* | All loan funds ($5,000,000) will go to an intermediate credit institution. All loan funds will be subloaned to private enterprise for importation of goods and services from private sources in the United States. |
| *Loan's Compliance with Specific Requirements* | |
| 44. *FAA §.608(a). Information on measures to be taken to utilize U. S. Government excess personal property in lieu of the procurement of new items.* | Standard language will be included in the loan agreement. |
| 45. *FAA §.604(a); App. §.108. Compliance with restriction of commodity procurement to U. S. except as otherwise determined by the President and subject to statutory reporting requirements.* | All equipment and commodities under the loan shall be procured in the United States. |
| 46. *FAA §.604(b). Compliance with bulk commodity procurement restriction to prices no higher than the market price prevailing in the U. S. at time of purchase.* | All equipment and commodities under the loan shall be procured in the United States. |
| 47. *FAA §.604(d). Compliance with requirement that marine insurance be placed in the U. S. on commodities financed by the loan if the host country discriminates against U. S. companies.* | Loan funds shall be made available for Marine Insurance on commodities shipped under subloans when such insurance is placed on a competitive basis as specified in this section of the Act. In the event that Costa Rica discriminates against any U.S. marine insurance company, commodities purchased under this loan will be insured against marine risk in the U.S. as required by this section. |

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| 48. | *FAA §.604(a). Compliance with requirement that funds not be used for procurement of any agricultural commodity or product thereof outside the U. S. when the domestic price of such commodity is less than parity.* | The loan will not be used for procurement of any agricultural commodity or product thereof outside the United States. |
| 49. | *FAA §.611(b); App. §.101. If water or water-related land resource construction project or program, information and conclusion on benefit-cost computation.* | The loan does not involve water or related land resource construction. |
| 50. | *FAA §.611(c). Compliance with requirement that contracts for construction be let on competitive basis to maximum extent practicable.* | No construction contracts will be financed with funds from this loan. |
| 51. | *FAA §.620(f); App. §.109. Compliance with prohibitions against assistance to any Communist country.* | Assistance provided under this loan will not be furnished to any Communist country. |
| 52. | *FAA §.620(g). Compliance with prohibition against use of assistance to compensate owners for expropriated or nationalized property.* | The loan agreement will provide that loan funds will not be used to compensate for expropriated or nationalized property. |

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| 53. *FAA §.612(b); §.636(h). Steps that have been taken to assure that, to the maximum extent possible, the country is contributing local currencies to meet the cost of contractual and other services, and that foreign currencies owned by the U. S. are utilized to meet the cost of contractual and other services.* | No contractual or other services in Costa Rica will be financed by the loan funds. |
| 54. *App. §.102. Compliance with requirement that payments in excess of $25,000 for architectural and engineering services on any one project be reported to the Congress.* | No architectural or engineering services will be financed under the loan. |
| 55. *App. §.104. Compliance with bar against funds to pay pensions, etc., for military personnel.* | No loans funds will be used to pay pensions, etc. for military personnel. |
| 56. *App. §.106. If country attempts to create distinctions because of their race or religion among Americans in granting personal or commercial access or other rights otherwise available to U. S. citizens generally, application which will be made in negotiations of contrary principles as expressed by the Congress.* | Costa Rica creates no distinctions because of race or religion among Americans in granting personal or commercial access or other rights otherwise available to U.S. citizens generally. |
| 57. *App. §.111. Compliance with requirements for security clearance of personnel.* | No personnel requiring security clearance will be financed by the loan. |
| 58. *App. §.112. Compliance with requirement for approval of contractors and contract terms for capital projects.* | No contractors or contracts requiring approval will be financed under this loan. |

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| 59. *App. S.114. Compliance with bar against use of funds to pay U.N. assessments, etc.* | The loan agreement will provide that loan funds may not be used to make any payments to the U.N. |
| 60. *App. S.115. Compliance with regulations on employment of U. S. and local personnel for funds obligated after April 30, 1964 (Regulation 7).* | No construction projects will be financed under this loan. |
| 61. *FAA S.636(i). Prohibition on financing non-U. S.-manufactured motor vehicles.* | The loan agreement will provide that no non U.S. manufactured motor vehicles will be financed under this loan. |
| 62. *App. S.401. Compliance with bar against use of funds for publicity or propaganda purposes within U. S. not authorized by the Congress.* | Loan funds will not be used for publicity or propaganda purposes within the U.S. |
| 63. *FAA S.620(k). If construction of productive enterprise where aggregate value of assistance to be furnished by U. S. will exceed $100 million, identification of statutory authority.* | The aggregate value of assistance is less than $100 million. |

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# FINANCIAL STATEMENTS
## A. BALANCE SHEET
## AS OF SEPTEMBER 30TH
(Thousands of Colones)*

| ASSETS | 1965 | 1966 | 1967 |
|---|---|---|---|
| **Current** | | | |
| Petty Cash | 1.5 | 1.5 | 2.0 |
| Local Banks | 162.7 | 116.6 | 705.0 |
| Foreign Banks | 89.7 | 185.0 | 1,344.4 |
| Sub-Total | 253.9 | 303.1 | 2,051.4 |
| **Receivables** | | | |
| Accounts Receivable for Subscribed Stock | 1,930.2 | - | - |
| Miscellaneous Debtors | 12.2 | 5.6 | 22.7 |
| Legal Stamps | 2.8 | 3.6 | 3.6 |
| Inventory | .8 | .7 | .3 |
| Sub-Total | 1,946.0 | 9.9 | 26.6 |
| Total Current Assets & Receivables | 2,199.9 | 313.0 | 2,078.0 |
| **Investments** | | | |
| Stock | - | - | 220.0 |
| Debentures | 1,047.0 | 2,699.0 | 2,236.0 |
| Short Term Loans | 2,976.4 | 5,333.9 | 6,085.8 |
| Medium Term Loans | 8,107.2 | 17,106.5 | 22,804.3 |
| Long Term Loans | 3,376.5 | 8,123.7 | 10,817.6 |
| Total Investments | 15,507.1 | 33,265.1 | 42,163.7 |
| **Real Property** | | | |
| Fixed Assets | 135.1 | 209.6 | 234.5 |
| Less Accumulated Depreciation | (14.5) | (30.3) | (50.8) |
| Next Fixed Assets | 120.6 | 179.3 | 183.7 |
| **Other Assets** | | | |
| Organization Expenses | 347.8 | 309.2 | 270.6 |
| Capitalized Tech. Assistance | 136.7 | 209.6 | 274.6 |
| Telephone Rights | 1.2 | - | - |
| Accumulated Proceeds | 72.3 | 302.8 | 353.1 |
| Deferred Expenses | .2 | 5.0 | 15.2 |
| Total Other Assets | 558.2 | 826.6 | 913.5 |
| **Total Assets** | 18,385.8 | 34,584.0 | 45,338.9 |

* (6.65 colones = U.S. $1.00)

| LIABILITIES | 1965 | 1966 | 1967 | |
|---|---|---|---|---|
| **Short Term Liabilities** | | | | |
| Dividends Payable | - | - | 3.0 | |
| Short Term Documents Payable | 37.8 | 312.5 | 1,975.9 | |
| Differed Proceeds | 31.3 | 48.2 | 101.0 | |
| Interest Payable to AID | 17.2 | 22.9 | 36.6 | |
| Accumulated Expenses | 13.3 | 29.8 | 47.0 | |
| Miscellaneous Debts | - | 134.5 | 1,031.1 | |
| Letters of Credit Requested | 120.8 | 153.4 | 422.1 | |
| Payments Orders Issued | - | 15.9 | - | |
| Total Short Term Liabilities | 220.4 | 717.2 | 3,616.7 | |
| **Long Term Liabilities** | | | | |
| Letters of Credit Requested | 273.6 | 2,028.3 | 57.5 | |
| Payment Orders Issued | 624.8 | 486.5 | 5.3 | |
| Amounts Paid to Correspondents Reimbursable by AID | 79.8 | 64.7 | 21.6 | |
| Long Term Payable Documen | 10,511.8 | 23,687.9 | 33,092.0 | |
| Total Long Term Liabilities | 11,490.0 | 26,267.4 | 33,176.4 | |
| Total Liabilities | 11,710.4 | 26,984.6 | 36,793.1 | |
| **Net Worth** | | | | |
| Capital Stock | 4,719.8 | 6,650.0 | 7,049.0 | |
| Capital Stock Subscription | 1,930.1 | - | - | |
| **Earnings Not Distributed** | | | | |
| Legal Reserve | 1.3 | 60.5 | 160.6 | |
| Reserve for Contingencies | 237.7 | 331.5 | 553.6 | 1496.8 |
| Current | (213.5) | 557.4 | 782.6 | |
| | | 949.4 | | |
| Total Net Worth | 6,675.4 | 7,599.4 | 8,545.8 | |
| Total Liabilities and Net Worth | 18,385.8 | 34,584.0 | 45,338.9 | |

## B. VARIOUS FINANCIAL INFORMATION

As of September 30
(Thousands of Colones)

| | 1965 | 1966 | 1967 |
|---|---|---|---|
| Securities Received as Guarantees | 5,013.5 | 7,185.7 | 11,544.8 |
| Bonds and Guarantees Responsibilities | 331.3 | 2,660.0 | 2,854.5 |
| Commissions Collected | - | 122.4 | 439.0 |
| Stock in Custody | 100.0 | 9.2 | 414.7 |
| Loan Due from AID | 22,738.2 | 9,562.1 | 158.0 |
| Letter of Commitment Issued | 6,821.0 | 3,950.3 | 33.9 |
| AID Recuperations Received | 265.3 | 2,297.7 | 1,782.0 |
| Lines of Credit Received | 4,828.9 | 7,543.8 | 14,716.6 |

## C. INCOME STATEMENT
## YEAR ENDING SEPTEMBER 30
(Thousands of Colones)

| 1. INCOME | 1965 | 1966 | 1967 |
|---|---|---|---|
| Interest on Subloans | | | |
| Own Resources | 234.4 | 598.6 | 921.4 |
| AID Resources | 350.6 | 1,436.3 | 2,360.0 |
| Total Interest Earned | 585.0 | 2,034.9 | 3,281.4 |
| Interest on Bonds | | | |
| Own Resources | 46.5 | 125.4 | 106.2 |
| AID Resources | 50.5 | 46.8 | - |
| Total Interest on Bonds | 97.0 | 172.2 | 106.2 |
| Commissions | 1.7 | 1.2 | 4.2 |
| Exchange Differences | 1.4 | 7.4 | 17.5 |
| Technical Assistance | - | 19.2 | 65.3 |
| Commissions on Guarantees Placed | - | 9.4 | 29.6 |
| Supervision Commission | 2.6 | 7.5 | 2.5 |
| Commitment Commission | - | 10.9 | 12.0 |
| Miscellaneous | 1.7 | 3.1 | 4.1 |
| TOTAL INCOME | 689.4 | 2,265.8 | 3,522.8 |

| 2. EXPENSES | | | |
|---|---|---|---|
| Administrative and General Expenses | | | |
| Salaries & Directors Fees | 336.1 | 402.2 | 462.6 |
| Travel & Representation Expenses | 23.5 | 38.0 | 49.6 |
| Office Operations & Supplies | 35.1 | 47.4 | 70.1 |
| Rent | 37.3 | 36.3 | 36.6 |
| Scholarship | .7 | 2.6 | 6.6 |
| Professional Fees | 9.8 | 15.6 | 35.0 |
| Amortization of Organization Expenses | 72.8 | 99.6 | 131.1 |
| Depreciation | 10.9 | 16.0 | 20.5 |
| Miscellaneous | 26.4 | 21.4 | 29.5 |
| Total General and Admin. Expenses | 552.6 | 679.1 | 835.6 |
| Financial Expenses | 111.4 | 403.0 | 684.9 |
| TOTAL EXPENSES | 664.0 | 1,082.1 | 1,520.5 |
| PERIOD EARNINGS | 25.4 | 1,183.7 | 2,002.3 |

# THE LEVEL OF INDUSTRY IN CENTRAL AMERICA - ACTUAL AND THEORETICAL

| | Value added in Manufacturing (in million CA pesos) | | | | Percentage Share of Manufacturing in Gross Domestic Product | | | | Relative Level of Industrialization | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 1962 | 1965 | 1962 | 1965 | 1962 | 1965 | 1962 | 1965 | 1962 | 1965 |
| | Actual | | Theoretical 1/ | | Actual | | Theoretical 2/ | | | |
| | | | | | (A) | (B) | (C) | (D) | (A÷B) | (B÷D) |
| Costa Rica | 60.8 | 80.7 | 71.4 | 92.2 | 13.9 | 14.7 | 16.3 | 16.8 | 0.85 | 0.87 |
| El Salvador | 96.6 | 136.1 | 101.8 | 120.4 | 14.9 | 17.4 | 15.7 | 16.0 | 0.95 | 1.13 |
| Guatemala | 146.7 | 216.7 | 208.9 | 285.1 | 13.1 | 15.2 | 18.7 | 19.4 | 0.70 | 0.78 |
| Honduras | 49.5 | 67.5 | 56.9 | 70.9 | 12.6 | 14.3 | 14.4 | 15.0 | 0.87 | 0.95 |
| Nicaragua | 52.9 | 68.9 | 60.9 | 85.5 | 12.7 | 13.0 | 14.6 | 16.1 | 0.87 | 0.80 |
| Total of above | 406.5 | 566.4 | 499.9 | 649.0 | 13.5 | 15.1 | 16.6 | 17.3 | 0.81 | 0.87 |
| Central America 3/ | 406.5 | 566.4 | 591.8 | 777.6 | 13.5 | 15.1 | 19.7 | 20.8 | 0.69 | 0.73 |

1/ Based on the equation: $\log V = 1.637 + 1.369 \log y + \log 1.124 \log P$, where y = per capita national income and P = population. Taken from United Nations, A Study of Industrial Growth: to be precise all data should be deflated to 1953 prices.

2/ Using actual data on gross domestic product.

3/ Computed as a regional unit.

Note: National income data for 1965 are based on extrapolating 1962 data prepared by Joint Planning Mission which relate national income to gross domestic product.

Sources: World Bank calculations based on Data of Joint Planning Mission and national statistical services.

## ORIGINAL MATURITY COFISA LOANS
(Thousands of Dollars)
Year Ending March 31

### Part One - With AID Funds

| | 1965 | 1966 | 1967 | 1968 | TOTAL |
|---|---|---|---|---|---|
| Less Than Two Years | 0 | 0 | 0 | 0 | 0 |
| Two Years | 107 | 115 | 285 | 106 | 613 |
| From Two to Three Years | 221 | 626 | 249 | 6 | 1,102 |
| From Three to Five Years | 318 | 777 | 475 | 21 | 1,591 |
| Over Five Years | 288 | 874 | 519 | 0 | 1,681 |
| TOTALS | 934 | 2,392 | 1,528 | 133 | 4,987 |

### Part Two - COFISA and Rollover Funds

| | 1965 | 1966 | 1967 | 1968 | TOTAL |
|---|---|---|---|---|---|
| Less Than One Year | 138 | 354 | 685 | 293 | 1,470 |
| One Year | 206 | 229 | 227 | 337 | 999 |
| From One to Two Years | 0 | 0 | 54 | 42 | 96 |
| Two Years | 0 | 102 | 98 | 156 | 356 |
| From Two to Three Years | 22 | 7 | 44 | 323 | 396 |
| From Three to Five Years | 0 | 0 | 483 | 321 | 804 |
| Over Five Years | 1 | 0 | 114 | 178 | 293 |
| TOTALS | 367 | 692 | 1,705 | 1,650 | 4,414 |

### TOTAL
### Part Three - AID, COFISA and Rollover

| | 1965 | 1966 | 1967 | 1968 | TOTAL |
|---|---|---|---|---|---|
| Less Than One Year | 138 | 354 | 685 | 293 | 1,470 |
| One Year | 206 | 229 | 227 | 337 | 999 |
| From One to Two Years | 0 | 0 | 54 | 42 | 96 |
| Two Years | 107 | 217 | 383 | 262 | 969 |
| From Two to Three Years | 243 | 633 | 293 | 329 | 1,498 |
| From Three to Five Years | 318 | 777 | 958 | 342 | 2,395 |
| Over Five Years | 289 | 874 | 633 | 178 | 1,974 |
| TOTALS | 1,301 | 3,084 | 3,233 | 1,783 | 9,401 |

Part Four - Lines of Credit Funds

| | 1965 | 1966 | 1967 | 1968 | TOTAL |
|---|---|---|---|---|---|
| Less Than One Year | 0 | 27 | 79 | 465 | 571 |
| One Year | 0 | 30 | 0 | 131 | 161 |
| From One to Two Years | 0 | 0 | 22 | 0 | 22 |
| Two Years | 0 | 0 | 50 | 0 | 50 |
| From Two to Three Years | 0 | 0 | 0 | 57 | 57 |
| Over Three Years | 0 | 0 | 0 | 0 | 0 |
| TOTALS | 0 | 57 | 151 | 653 | 861 |

# COFISA

## Breakdown of Projected Income, Expense & Profit
(In thousands of Colones)

| | 1969 | 1970 | 1971 | 1972 | 1973 | 1974 | 1975 | 1976 |
|---|---|---|---|---|---|---|---|---|
| RECEIPTS | | | | | | | | |
| Interest from: | | | | | | | | |
| Transitory Investments | 80 | 80 | 80 | 80 | 80 | 80 | 80 | 80 |
| Short-Term Loans | 1756 | 2178 | 2411 | 2401 | 2350 | 2264 | 2179 | 2090 |
| Med/Long Term Loans | 4156 | 4986 | 5328 | 5439 | 5273 | 5260 | 5260 | 4715 |
| Other Products | 80 | 80 | 80 | 80 | 80 | 80 | 80 | 80 |
| Dividends Received | 120 | 270 | 500 | 600 | 800 | 800 | 800 | 800 |
| Total | 6189 | 7594 | 8399 | 8600 | 8583 | 8464 | 8399 | 7765 |
| EXPENSES | | | | | | | | |
| Administrative | 1250 | 1250 | 1250 | 1250 | 1250 | 1250 | 1250 | 1250 |
| Financial | 2064 | 2565 | 2461 | 2419 | 2377 | 2668 | 2576 | 2429 |
| Total | 3314 | 3815 | 3711 | 3669 | 3627 | 3918 | 3826 | 3679 |
| Gross Profit | 2875 | 3779 | 4688 | 4901 | 4956 | 4546 | 4573 | 4086 |
| Less: | | | | | | | | |
| Taxes | 835 | 1107 | 1379 | 1443 | 1460 | 1337 | 1345 | 1199 |
| NET PROFIT | 2040 | 2672 | 3309 | 3458 | 3496 | 3209 | 3228 | 2887 |
| Profit as Percent of Paid in Equity | 15.65% | 15.7% | 19.4% | 20.3% | 20.5% | 18.8% | 18.9% | 16.95% |

## COFISA PROJECTION OF ESTIMATED TRIAL BALANCE
(Thousand of colones, September 30)

| | 1968 | 1969 | 1970 | 1971 | 1972 | 1973 | 1974 | 1975 | 1976 |
|---|---|---|---|---|---|---|---|---|---|
| Liquid Assets | 11,639 | 10,867 | 11,229 | 2,006 | 1,654 | 1,635 | 1,648 | 1,597 | 1,477 |
| Loans & Investments | 44,349 | 64,740 | 80,507 | 88,607 | 87,899 | 85,809 | 82,467 | 79,053 | 75,568 |
| Transitory Investments | 1,000 | 1,000 | 1,000 | 1,000 | 1,000 | 1,000 | 1,000 | 1,000 | 1,000 |
| Short-Term Loans | 6,776 | 14,630 | 18,150 | 20,093 | 20,005 | 19,580 | 18,867 | 18,157 | 17,417 |
| Medium-Term Loans | 23,639 | 28,770 | 35,103 | 38,524 | 38,050 | 36,914 | 35,154 | 33,326 | 31,484 |
| Long-Term Loans | 10,934 | 14,340 | 17,254 | 18,990 | 18,844 | 18,315 | 17,446 | 16,570 | 15,667 |
| Investments in Equity | 2,000 | 6,000 | 9,000 | 10,000 | 10,000 | 10,000 | 10,000 | 10,000 | 10,000 |
| Net Permanent Assets | 256 | 275 | 248 | 223 | 201 | 181 | 163 | 147 | 132 |
| Other Assets | 976 | 928 | 916 | 864 | 846 | 775 | 722 | 603 | 623 |
| Total Assets | 57,220 | 76,810 | 92,900 | 91,700 | 90,600 | 88,400 | 85,000 | 81,400 | 77,800 |
| Short-Term Liabilities | 8,150 | 11,684 | 11,672 | 11,620 | 12,685 | 13,687 | 13,634 | 13,515 | 13,535 |
| Accounts Payable | 2,192 | 2,223 | 2,211 | 2,159 | 2,151 | 2,080 | 2,027 | 1,908 | 1,928 |
| Payments on AID Loans | 1,073 | 2,146 | 2,146 | 2,146 | 3,219 | 4,292 | 4,292 | 4,292 | 4,292 |
| Lines of Credit | 4,885 | 7,315 | 7,315 | 7,315 | 7,315 | 7,315 | 7,315 | 7,315 | 7,315 |
| Long-Term Liabilities | 38,827 | 49,981 | 61,135 | 58,989 | 55,770 | 51,478 | 47,186 | 42,894 | 38,602 |
| AID Loans | 38,827 | 49,981 | 61,135 | 58,989 | 55,770 | 51,478 | 47,186 | 42,894 | 38,602 |
| Total Liabilities | 46,977 | 61,665 | 72,807 | 70,609 | 68,455 | 65,165 | 60,820 | 56,409 | 52,137 |
| Patrimony | 10,243 | 15,145 | 20,093 | 21,091 | 22,145 | 23,235 | 24,180 | 24,991 | 25,663 |
| Capital Stock, 1st Issue | 7,049 | 7,049 | 7,049 | 7,049 | 7,049 | 7,049 | 7,049 | 7,049 | 7,049 |
| Capital Stock, 2nd Issue | 1,995 | 5,985 | 9,975 | 9,975 | 9,975 | 9,975 | 9,975 | 9,975 | 9,975 |
| Legal Reserve | 260 | 409 | 596 | 811 | 1,030 | 1,352 | 1,464 | 1,666 | 1,702 |
| Contingency Reserve | 575 | 767 | 975 | 1,091 | 1,077 | 1,040 | 981 | 920 | 858 |
| Short-Term Loan Reserve | 68 | 146 | 181 | 201 | 200 | 196 | 189 | 182 | 174 |
| Net Accrued Profits | 296 | 789 | 1,317 | 1,984 | 2,814 | 3,723 | 4,522 | 5,199 | 5,905 |
| Liabilities plus Patrimony | 57,220 | 76,810 | 92,900 | 91,700 | 90,600 | 88,400 | 85,000 | 81,400 | 77,800 |

Part 2

## PROJECTION COFISA RESOURCES AND APPLICATIONS

(Thousands of colones)

| | 1967 | 1968 | 1969 | 1970 | 1971 | 1972 | 1973 | 1974 | 1975 | 1976 |
|---|---|---|---|---|---|---|---|---|---|---|
| **ORIGEN OF RESOURCES:** | | | | | | | | | | |
| Balance forward | 303 | 2,051 | 11,639 | 10,867 | 11,229 | 2,006 | 1,654 | 1,635 | 1,648 | 1,597 |
| Net Profit | 782 | 1,222 | 1,698 | 2,212 | 2,690 | 2,893 | 2,952 | 2,842 | 2,720 | 2,749 |
| Capital Stock, 2nd issue | -- | 1,995 | 3,990 | 3,990 | -- | -- | -- | -- | -- | -- |
| Reserve for depreciation | 21 | 28 | 31 | 27 | 25 | 22 | 20 | 18 | 16 | 15 |
| Legal Reserve | 100 | 99 | 149 | 187 | 215 | 219 | 222 | 212 | 202 | 36 |
| Contingency Reserve | 463 | 21 | 192 | 208 | 116 | -4 | -37 | -59 | -61 | -62 |
| Reserve for Short-term loans | -- | 68 | 78 | 35 | 20 | -1 | -4 | -7 | -7 | -8 |
| Lines of Credit | 1,916 | 2,458 | 2,459 | -- | -- | -- | -- | -- | -- | -- |
| AID 1st. Loan | 9,404 | 158 | -- | -- | -- | -- | -- | -- | -- | -- |
| AID 2nd. Loan | -- | 6,650 | 13,300 | 13,300 | -- | -- | -- | -- | -- | -- |
| Repayments | 12,391 | 17,617 | 22,110 | 31,253 | 38,553 | 44,546 | 44,146 | 43,268 | 42,051 | 40,273 |
| Total | 25,380 | 32,367 | 55,646 | 62,079 | 52,848 | 49,681 | 48,953 | 47,909 | 46,569 | 44,600 |
| **APPLICATION OF RESOURCES** | | | | | | | | | | |
| Investments & Loans | 22,547 | 19,802 | 42,501 | 47,020 | 46,653 | 43,838 | 42,056 | 39,926 | 38,637 | 36,788 |
| Amortization to AID, 1st. Loan | -- | -- | 1,073 | 2,146 | 2,146 | 2,146 | 2,146 | 2,146 | 2,146 | 2,146 |
| Amortization to AID, 2nd. Loan | -- | -- | -- | -- | -- | -- | 1,073 | 2,146 | 2,146 | 2,146 |
| Dividends paid, 1st. issue | 782 | 846 | 846 | 846 | 846 | 846 | 846 | 846 | 846 | 846 |
| Dividends paid, 2nd issue | -- | 80 | 359 | 838 | 1,197 | 1,197 | 1,197 | 1,197 | 1,197 | 1,197 |
| Balance | 2,051 | 11,639 | 10,867 | 11,229 | 2,006 | 1,654 | 1,635 | 1,648 | 1,597 | 1,477 |
| Total | 25,380 | 32,367 | 55,646 | 62,079 | 52,848 | 49,681 | 48,953 | 47,909 | 46,569 | 44,600 |

Assumptions Underlying Financial Projections

The projections in the preceeding three Tables are based on the following assumptions in addition to those discussed in Section IV, B and C.

1. A second AID loan on the conditions recommended in this paper will be disbursed in five equal parts over 24 months with the first received in September 1968 and half the loan and each disbursement at 2.5 percent and half at 5.0 percent. (Such early or rapid disbursement is unlikely leading to an overstatement of profits in 1969 and 1970.)

2. A second share issue of $1.5 million equivalent paid in within 24 months in five equal installments beginning in September 1968. (The small allocation to dividends on the second issue in fiscal 1968 is an error.)

3. Use of lines of credit will increase by 2,458,000 colones in fiscal 1968 and 2,459,000 in fiscal 1969 and then remain stable. The effective interest on lines of credit will be 7.75 percent.

4. The allocations of 5 percent of operating profits to legal reserves will halt when legal reserves equal 10 percent of capital stock.

5. The reserve for short-term loansis constituted on the basis of one percent of short-term loans.

6. Loan repayments were calculated by assuming short-term loans, are repaid in one year; medium term in three years and long-term in six years.

7. Dividends are assumed to be 12 percent in cash with no additional stock dividends.

June 20, 1968

ADDITIONAL CONDITIONS TO BE INCLUDED
IN LOAN AGREEMENT

1. No AID funds will be used to finance industries whose economic feasibility depends on the establishment of additional tariff protection; except as AID may agree in writing no AID funds will be used to finance industries which seek or have sought CACM integration industry status.

2. No resources of COFISA will be used to purchase land, either in a raw or improved state, although COFISA's resources may be used to improve land.

3. Without the prior approval of AID, COFISA shall incur no obligation to any creditor in excess of $100,000 except that lines of credit from foreign banks for an amount equal to twice the paid-in capital of COFISA may be used without such approval.

4. A minimum addition of 0.5 percent of total COFISA loans and investments outstanding at the end of each fiscal year shall be made to a reserve for bad debts or extraordinary losses until such reserve shall be equal to 2 percent of the total loans and investments of COFISA.

5. Without prior approval of AID, COFISA shall not engage in accounts receivable financing, take assignment of receivables, perform underwriting services, or engage in factoring operations, regardless of source of funds.

6. During the life of the AID loan, COFISA shall not reduce its authorized and issued capital to less than $2.5 million.

7. Except as AID may agree in writing, COFISA will make no subloan or investment which results in an aggregate investment of more than $250,000 in any enterprise.

8. Except as AID may otherwise agree in writing, COFISA will not take an equity position in any enterprise which would result in COFISA's having more than 30 percent of the total equity in the enterprise; for the purpose of this calculation any equity purchased with a loan from COFISA will be included in computing COFISA's equity against the 30 percent limit as well as any shares in the enterprise pledged against any COFISA loan.

9. COFISA will make no subloan or investment to an enterprise in which a director(s) or a member of his immediate family (ascendants, descendants, spouse, or siblings) has an interest unless the subloan or investment has been approved by a majority of the Board of Directors with the interested director(s) not voting.

10. Members of the board of directors and the manager shall be subject to the approval of AID during the life of the AID loan as well as changes in the compensation rates for directors.

11. Loans may be made only to private enterprises, which are defined as those in which government ownership is less than 35 percent. Loans may be made to cooperatives.

12. For the purposes of the review before commitments exceed $1,750,000, AID officials will be given access to the minutes of the COFISA meetings and to the files containing financial information on sub-borrowers on a confidential basis.

13. COFISA will use its own funds and AID funds only for financing resulting in an expansion of production; refinancing is not permitted.

CERTIFICATION PURSUANT TO SECTION 611 (e) OF THE FOREIGN ASSISTANCE ACT AS AMENDED

I, Robert B. Black, the principal officer of the Agency for International Development in Costa Rica having taken into account among other things, the maintenance and utilization of projects in Costa Rica previously financed or assisted by the United States, do herewith certify that in my judgement, Costa Rica has both the financial capability and the human resources capability to effectively maintain and utilize the capital assistance project, SECOND COFISA LOAN.

This certification is based on a careful review of both the borrower's and sub-borrowers' performance in utilization and maintenance under a similar loan authorized in 1964. The Borrower's financial record and projections are excellent (Section I C 5, pages 15, 16; Section IV B; ANNEXES II, V). The Borrower's organizational structure, record and human resources which will be strengthened by additional professionals (Section I C 8, pages 21-22), are already sound (Section I B 2 pages 3-4) and performance under the first loan complied with the purposes of the assistance (Section I C 1 and 2 pages 10-11). No disbursement will be made under the loan until the borrower has firm commitments, including a 20 percent downpayment, to pay in the additional capital required by the loan project. The utilization and maintenance of equipment by sub-borrowers has been checked and found to be fully satisfactory as would be expected in the private sector of the economy among sub-borrowers who are servicing their loans promptly in almost all cases.

Robert B. Black
Director USAID/Costa Rica

DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
Washington, D. C. 20523

UNITED STATES COORDINATOR
ALLIANCE FOR PROGRESS

LOAN AUTHORIZATION

Provided From: Alliance for Progress Funds
COSTA RICA: Corporacion Costarricense de Financiamiento Industrial, S. A. (COFISA) -- Second Loan

Pursuant to the authority vested in the Deputy U. S. Coordinator, Alliance for Progress, Agency for International Development ("A.I.D."), by the Foreign Assistance Act of 1961, as amended, and the delegations of authority issued thereunder, I hereby authorize the establishment of a loan pursuant to Part I, Chapter 2, Title VI, Alliance for Progress, to the Corporacion Costarricense de Financiamiento Industrial, S. A. (COFISA) ("Borrower") of not to exceed five million United States dollars ($5,000,000) to assist in financing the dollar costs of subloans and equity participation by Borrower for the creation and expansion of industrial and agricultural enterprises in Costa Rica and Member Countries of the Central American Common Market, this loan to be subject to the following terms and conditions:

1. Interest and Terms of Repayment:

(a) Borrower shall repay the loan to A.I.D. in United States dollars within twenty (20) years from the first disbursement under the loan, including a grace period of not to exceed five (5) years. Borrower shall pay to A.I.D. in United States dollars interest at the rate of (i) three (3) percent per annum on the disbursed balance of the loan devoted to "Priority" projects by the Borrower for the first five years following disbursement; thereafter, the rate will be five (5) percent per annum; and (ii) five (5) percent per annum on the remainder of the disbursed balance of the loan.

(b) If prior to the first disbursement under the loan the Government of Costa Rica so elects, Borrower shall fulfill its United States dollar obligations under the loan by paying to the Government in the currency of Costa Rica, the equivalent, determined as of a time and in a manner satisfactory to A.I.D., of the United States dollar amounts payable to A.I.D. under (a) above, and, in such event, the Government shall pay to A.I.D.:

(i) the equivalent in United States dollars of all amounts, paid to the Government by the Borrower, as follows:

a. All interest immediately upon receipt subject to the Government's right to retain all payments in excess of two (2) percent per annum during a grace period of not to exceed ten (10) years from the first disbursement under the loan ("Government grace period").

b. Principal within forty (40) years including a grace period of not to exceed ten (10) years from the date of the first disbursement under the loan ("Government grace period");

(ii) Interest in United States dollars of two (2) percent per annum during the Government grace period, and two and one half ($2\frac{1}{2}$) percent per annum thereafter, on all amounts of outstanding principal paid by Borrower to the Government from the respective dates of such payments of principal.

2. Other Terms and Conditions:

(a) Equipment, materials and services (except shipping and marine insurance) financed under the loan shall have their origin in and be procured from the United States. Shipping financed under the loan shall be procured from the United States, and marine insurance financed under the loan shall be placed in the United States with a company authorized to do marine insurance business in any state of the United States.

(b) No loan funds in excess of $1,750,000 shall be committed by Borrower until A.I.D. shall have conducted a detailed review of the commitment and administration of loan funds, and shall have advised Borrower that further commitments may be made.

(c) Borrower shall not apply more than $2,500,000 to subloans for other than "Priority" projects. Priority projects are those directed primarily at increasing (i) exports outside the Central American Common Market ("CACM"), (ii) foreign exchange earnings from tourism, (iii) Costa Rican agricultural production directly, or (iv) the processing of Costa Rican agricultural production; and those for which 75 percent of the inputs are of CACM origin and the anticipated selling price of the output is within 25 percent of the normal landed cost of similar imports. Agricultural subloans must be based on a comprehensive project to be considered as applied to Priority projects. Equipment financing or crop financing, except as part of larger, comprehensive projects, will not be considered as Priority projects.

(d) Borrower shall not with A.I.D. loan funds make any subloans for terms less than three nor more than ten years, or charge interest thereon at rates in excess of 8 1/2 percent per annum (in the case of Priority projects), or ten percent per annum (in the case of other projects).

(e) Except as A.I.D. may otherwise agree in writing, no funds obtained from any source whatever shall be applied by Borrower (i) to subloans or investments which will directly or indirectly increase the production of coffee, sugar or cotton; or (ii) to subloans for the purchase of shares in expanding or new enterprises unless Borrower itself purchases equity at least equal to the equity financed by Borrower.

(f) Borrower shall not apply any of its funds, obtained from any source whatever, for the purpose of refinancing.

(g) Upon the execution of the loan agreement, Borrower shall sell additional shares in an amount not less than $1,500,000, to be paid in at least pari passu with disbursements under the loan, and not later than two years after the first disbursement thereunder. At least $500,000 equivalent of these shares based on the official exchange rate at time of subscription shall be placed prior to the first disbursement under the loan with persons or firms not shareholders on December 31, 1967.

(h) The loan shall be subject to such other terms and conditions as A.I.D. may deem advisable.

Deputy U. S. Coordinator

Date

# AGENCY FOR INTERNATIONAL DEVELOPMENT

## UNITED STATES A.I.D. MISSION TO COSTA RICA

San José, May 31, 1973

U.S.A.I.D.
UNITED STATES EMBASSY
SAN JOSE, COSTA RICA

MEMORANDUM

TO: The Files

FROM: Isabel Chacón Isabel Chacón
Project Evaluation Coordinator

SUBJECT: Annual Project Review: COFISA Project
AID Loan 515-L-019

PURPOSE: TO PROMOTE ECONOMIC DIVERSIFICATION IN THE AGRICULTURE AND EXPORT AREAS AND INSURE CONTINUED EXPANSION OF COFISA

The internal AID evaluation review of the subject project was held on May 14, with the following staff members present: Robert Pratt, Project Manager; Peter Kreis, AID Affairs Officer; Daniel Greene, Controller; Thomas McKee, Chief, Institutional Development Division and Isabel Chacón, Project Evaluation Coordinator.

I. DISCUSSION

Mr. Pratt described the current status, activity and accomplishments of the project. Concrete activities include the following (plus a general background on COFISA described in Attachment #1):

1. The fact that COFISA has established itself as a solid development bank in less than ten years with no further AID assistance required, is the major indicator of its success. The second AID Loan made to COFISA has been 95% disbursed with final subloans already approved and equipment in shipment. Thus, the Mission has extended the deadline for final disbursement to June 30.

2. Through good management and available foreign bank lines of credit now totalling more than $13 million (granted as a result of COFISA's sound financial status and good reputation), this development bank has maintained a growing diversified lending program in the industrial, agricultural, export, and, lately, housing areas, thus creating new sources of revenue and employment.

3. Through its multiplier effect, loans have not only contributed to the growth of the GNP but have also created jobs for approximately 8,000 to 9,000 people. Life-of-Project export increases are valued at approximately $16 million with 75 new business activities generated.

4. The Mission's Controller reports that COFISA's fiscal and accounting records are well maintained and that the staff's prompt service and cooperation have always been above reproach. An audit of COFISA was previously carried out by the AID Auditor General Office.

5. The creation of a stock exchange market indicated as one of the purposes of COFISA at the outset of the project, proved unrealistic.

## II. RECOMMENDATIONS

Since the COFISA project appears to be a prime example of AID's successful support to private sector development through capital investment, it is strongly recommended that AID/W consider undertaking a full evaluation of this project. Variables responsible for the success should be measured separately in both qualitative and quantitative terms. This will enable the formulation of hypotheses that may have applicability to AID strategy generally and for other LDC programming priorities specifically.

ICH/frs

cc: Ambassador Viron Vaky
Mr. Peter Kreis
Mr. Robert Pratt
Mr. Daniel Greene
Mr. Thomas McKee
Miss Ana Sayagués

Narrative Report on COFISA AID LOANS 515-L-010 & 515-L-019

A.I.D. has made two $5,000,000 loans to COFISA, a private development bank (financiera), since 1964. The first loan was made when COFISA was just being established and was to provide it with a source of low-cost, long term, seed capital. The second loan, signed in May 1969, was made essentially to help COFISA greatly expand its volume and scope of activities, increasing its financing of agricultural and agro-industrial enterprises. It is now 95% disbursed. The initial A.I.D. assistance was provided at a time when considerable demand existed in Costa Rica to establish manufacturing industries to take advantage of the Central American market stimulated by the creation of the Central American Common Market (CACM). It was felt that the cumbersome nationalized banking system could not meet the new demand in the private sector for investment and working capital for industrialization.

COFISA quickly established a reputation of a sound, efficient financial institution and has been a significant force in Costa Rica's industrial and agricultural development. In terms of loan volume, in 1972 COFISA surpassed the smallest of the four commercial banks in size of loan portfolio. Its average monthly lending volume has exceeded $1,000,000 per month since late 1972. As of September 30, 1972 its loan and investment portfolio had reached $14.5 million, capital and reserves totaled $3.6 million and it had financed a cumulative total of $38.5 million of projects since its inception in 1965.

As a means of attracting local capital for investment industrial and agricultural projects it has been quite successful in that its capital is entirely from private sources (almost exclusively Costa Rican) and for every dollar of COFISA funds invested in a project there are usually several additional dollars invested by the project sponsors or owners. Furthermore, COFISA has been extremely successful in attracting foreign resources by means of medium term bank lines of credit (5 years). As of January 31, 1973 COFISA had available to it $11 million in lines of credit from U.S. and other foreign banks, of which it had drawn approximately $5 million. The confidence on the part of the foreign banks in COFISA's management and credit worthiness is probably the best possible indicator of COFISA's success in establishing itself as a strong financial institution.

During 1972 COFISA entered a new field of activity - housing. On its own initiative it issued approximately $1.5 million of bonds to provide mortgage financing for large scale, low to medium cost housing projects. This endeavor will help to alleviate Costa Rica's pressing housing shortage in those categories.

AID 1020-28 (1-73)

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project: From FY 65 to FY 73
Total U. S. Funding $10,000,000
Date Prepared: 5/3/73

Project Title & Number: COFISA AID Loan 515-L-019 and 515-L-010

| NARRATIVE SUMMARY | OBJECTIVELY VERIFIABLE INDICATORS | MEANS OF VERIFICATION | IMPORTANT ASSUMPTIONS |
|---|---|---|---|
| Program or Sector Goal: The broader objective to which this project contributes: (A-1)<br><br>Improve the economic development of Costa Rica. | Measures of Goal Achievement: (A-2)<br><br>1. Rate of growth of GNP and per capital income. | (A-3)<br><br>1. Central Bank statistics.<br>2. Planning Office reports.<br>3. Ministry of Industry, Commerce and Economy resources. | Assumptions for achieving goal targets: (A-4)<br><br>Continued economic and political stability in Costa Rica. |
| Project Purpose: (B-1)<br><br>To promote economic diversification in the agriculture and export areas and insure continued expansion of COFISA. | Conditions that will indicate purpose has been achieved: End-of-Project status. (B-2)<br><br>1. COFISA has a continuous lending program focusing on agric. & export areas.<br>2. COFISA has emerged as a viable, growing institution.<br>3. Development bank with | (B-3)<br><br>1. COFISA's loan records.<br>2. COFISA's financial reports. | Assumptions for achieving purpose: (B-4)<br><br>1. Continued economic and politi- stability in Costa Rica.<br>2. Continuation of sound manage practices. |
| Project Outputs: (C-1)<br><br>1. Loans to industrial and agricultural enterprisers.<br>2. Operating efficiency of COFISA staff. | Magnitude of Outputs: (C-2)<br><br>1. No. of loans and amount of loans over a four-year period.<br>2. Efficiency of operation measured by default record and by maintaining low overhead. | (C-3)<br><br>1. COFISA records.<br><br>2. COFISA records. | Assumptions for achieving outputs: (C-4)<br><br>Continued demand for loans. |
| Project Inputs: (D-1)<br><br>1. AID Loan 515-L-019<br><br>2. COFISA capital shares. | Implementation Target (Type and Quantity) (D-2)<br><br>1. $5,000,000-fully disbursed by 5/72.<br>2. $1,500,000-fully paid in by 6/71. | (D-3)<br><br>1. AID disbursement records.<br><br>2. COFISA records. | Assumptions for provid- (D-4) |

AID 1020-26 (1-73)
SUPPLEMENT 8

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY 65 to FY 73
Total U.S. Funding $10,000,000
Date Prepared: 5/3/73

Project Title & Number: COFISA AID Loan 515-L-019 and 515-L-010



| NARRATIVE SUMMARY | OBJECTIVELY VERIFIABLE INDICATORS | MEANS OF VERIFICATION | IMPORTANT ASSUMPTIONS |
|---|---|---|---|
| Project Purpose: (B-1) | Conditions that will indicate purpose has been achieved: End-of-Project status. (B-2)<br><br>an active lending program and solid financial status. | (B-3) | Assumptions for achieving purpose: (B-4) |

AID 1020-28 (1-73)
SUPPLEMENT 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY _____ to FY _____
Total U.S. Funding _____
Date Prepared: _____

Project Title & Number: COFISA AID Loan 515-L-019

PAG

| NARRATIVE SUMMARY | OBJECTIVELY VERIFIABLE INDICATORS | MEANS OF VERIFICATION | IMPORTANT ASSUMPTIONS |
|---|---|---|---|
| Project Outputs: (C-1) | Magnitude of Outputs: (C-2)<br>3. Low rate of management and staff turnover. | (C-3) | Assumptions for achieving outputs: (C-4) |

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