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BOLIVIA

FINAL EVALUATION:
Rural Development Planning Project,
and Departmental Development
Corporations Project

MID-TERM EVALUATION:
Market Town Capital Formation Project

Prepared for:

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TABLE OF CONTENTS

ACRONYMS
and Other Terms

BID 213	An Inter-American Development Bank line of credit currently available for refinancing through the commercial banks
DDC	Departmental Development Corporation, the acronym refers to both the Corporations themselves and to the USAID/Bolivia Project under final evaluation in this paper.
GOB	Government of Bolivia
ICI	Intermediate Credit Institutions
MPC	Ministry of Planning and Coordination
MTCF	Market Town Capital Formation Project
PACD	Project Activity Completion Date
PIL	Project Implementation Letter
RDP	Rural Development Planning Project
SAMs	Sociedades Anonimas Mixtas
UCFs	Financial Credit Units, formed under the DDC project in eight of the nine departments as financial intermediaries and reoriented as investment promotion entities under MTCF
UCP	Project Coordination Unit, located in La Paz, which managed the DDC and manages the MTCF Projects.
USAID/Bolivia	United States Agency for International Development/Bolivia
Corporations	Refers here to the DDCs not to private corporations.

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DETAILED REPORT OUTLINE

I. Executive Summary and Recommendations

- A. Executive Summary
- B. Recommendations

II. Political and Economic Context, 1978-1988

III. Final Evaluation of RDP/DDC Projects

- A. Evaluation Methodology
- B. Background, Goals and Objectives
- C. Evaluation
    - 1. Rural Development Project
        - a. Implementation
        - b. Results
            - (1) 1978-1983
            - (2) 1983-1987
    - 2. Departmental Development Corporations
        - a. Implementation
        - b. Achievement of Objectives
            - (1) Socioeconomic Impact
            - (2) Institutional Impact
                - a) DDCs
                - b) UCFs
                - c) UCP
                - d) ICIs
            - (3) Financial Impact: Status of DDC Loan Portfolio
                - a) Background
                - b) Operating Procedures
                - c) Loan Portfolio Analysis
- D. Conclusions
- E. Recommendations

1) UPIs
2) UCP
3) ICIs
4) DDCs
5) Private Sector

f. Financing Investment Promotion
g. Technical Assistance

Tables and Charts

Appendices

/1/

I. EXECUTIVE SUMMARY AND RECOMMENDATIONS

A. EXECUTIVE SUMMARY

The Rural Development Planning Project (RDP), signed in 1978, and the Departmental Development Corporations Project (DDC), signed one year later, were a combined effort to improve the standard of living of the rural poor in Bolivia. The RDP Project used grant funds to provide technical assistance to the Departmental Corporations and to the Ministry of Planning and Coordination to improve the quality of regional plans and to facilitate their incorporation into the national planning system. The DDC Project, supported by a $10 million loan, provided financial resources for sub-projects, primarily in the rural areas.

The goal of both projects was the same: to improve the standard of living of the rural poor in Bolivia. The purposes were complementary; that of the RDP Project was to improve the technical competency and coordination of the planning systems in five Departmental Development Corporations (DDCs) and in the Ministry of Planning and Coordination (MPC). The purpose of the DDC Project was "to enhance the outreach capability of the DDCs to identify and implement sub-projects...of direct benefit to the target group."

Both projects suffered many problems because of the economic and political situation of the time. Both were suspended between July 1980 and September 1983, when relations broke down between the Bolivian and U.S. governments, and both resumed operations just as Bolivia headed into the most severe economic crisis in its history. Over the life of both the RDP and DDC projects, activities became increasingly related to private sector project activities. Authorization to work and cooperate with the private sector was given by Project Implementation Letter (PIL) No. 16, signed in September 1983, when both projects were reactivated.

The technical assistance provided under the RDP project succeeded in improving the in-house capabilities of the Corporations, especially in the areas of regional planning and the identification, promotion and evaluation of private sector projects.

Over time, the DDC project became the more active of the two and its institutional and financial impacts are most visible today as they form the foundations of the current Market Town Capital Formation project (MTCF). As a result of the DDC project, the Project Coordination Unit (UCP) was created to provide overall project coordination, and the Financial Credit Units (UCFs) were established in the various departments. Under the DDC project, the UCFs performed a financial intermediation role and were closely allied to the Corporations. One success of the DDC project was the to orient to the Corporations toward private sector activities. The project also succeeded in financing some very good projects at a time when there was little financing available for productive investment.

Overall, however, the DDC project suffered many problems and unfortunately, many of those problems are still felt today. Among the key findings of this report is the fact that the loan portfolio generated under the DDC project is in trouble. This fact is especially significant because the DDC portfolio is carried over to the Market Town project. A total of 95 loans to 135 projects were made over the life of the DDC project. Of them, 50% are delinquent on interest payment and 30% are past due on principal payment. These numbers may well grow since the grace period on many is yet to expire. Because of the above, and considering that some of the participating banks are bankrupt, this evaluation estimates that the value of the DDC loan portfolio should be written down by 30%.

The DDC project suffered these problems for a variety of reasons, but especially because sub-project selection was poor and the bureaucracy was slow and cumbersome. Sub-projects were selected and promoted with little assurance of their financial or productive viability. In many cases, investment promotion became project advocacy and inexperienced borrowers began businesses for which the market was nonexistent, saturated or inaccessible. Examples include the excessive number of chicken projects approves in Tarija vis-a-vis a small and shrinking market, and the large number of Cochabamba flower projects developed without sufficient knowledge of and access to appropriate marketing channels. The DDC project also lacked the capability to track sub-projects and help those in need of assistance.

In addition to problems with sub-projects, the DDC project also experienced constraints due to excessive bureaucracy. At one point the loan approval process required seven signatures in USAID/Bolivia alone; among them that of the Mission Director. Bureaucratic delays were compounded by implementation delays. Import procedures were such that equipment was often late in arrival; six to eighteen months was not unusual and one company waited over two years. In the meantime, sub-project borrowers were expected to pay interest, and if the grace period had expired, to begin repaying principal, even without the productive, hence financial, capacity to do so.

Many of the design problems of the DDC project were addressed and resolved in the Market Town Capital Formation project; others were inherited by it. The MTCF project is a follow-on project to the two it succeeded and aims to strengthen the UCFs, more fully utilize the participating ICIs, and concentrate on financing sub-projects in rural and semi-urban areas by further developing cooperation among the UCFs, ICIs and investors. The goal of the MTCF project is to achieve a higher standard of living, through increased employment and production, in Bolivia's rural and semi-urban areas. Its purpose is to increase the level of productive private sector investment in those areas.

The MTCF project is not quite at the midway point. As such, it is not possible to draw definitive conclusions about certain aspects, especially regarding the quality of loans and sub-projects. Nevertheless, this evaluation makes the following observations:

- The project is significantly behind its implementation schedule;
- The overall system is not a system, it lacks clear lines of authority and permanence;
- UCP management is weak and is not results oriented;
- There is excessive focus on the creation of Market Towns (pilot project) to the exclusion of operating imperatives;
- Geographic and subsectorial restrictions limit success;
- Red tape and bureaucracy are excessive; and
- Self-sufficiency by 1989 is not attainable.

Given these findings, this evaluation team makes the recommendations outlined in the following section.

B. RECOMMENDATIONS

1. Project Goal/Purpose. In light of current economic events and realities in Bolivia, the project purpose should be broadened and should aim to increase the level of productive investment throughout Bolivia. Priority should be given to projects which have forward and backward linkages to rural and semi-urban areas, but urban areas should not be excluded.

The elimination of current geographic restrictions and the inclusion of La Paz, Cochabamba and Santa Cruz for sub-project eligibility refocuses attention on the urgent need for Bolivia's economic development. It re-establishes a priority included in the project paper for generating positive impacts in rural areas, and recognizes that successful urban-based industries can do that. This broadened goal also restores the emphasis on Market Towns to an appropriate level of human and financial resources, until the concept is proven. Most importantly, by including the more economically active centers, the expanded focus offers a way to execute the project.

2. Project Operations. This evaluation recommends the following operational guidelines:

- Support lending to the private productive sector;
- Emphasize the small and medium investor, but do not exclude larger entrepreneurs;
- Eliminate geographic restrictions;
- Conduct "market town" activities at a reduced level, as a pilot project, as per the original project design; and
- Eliminate working capital restrictions.

3. Institutional Implications. The short-term institutional recommendation is to act quickly to streamline the current structure and procedures. Long-term recommendations include the possible creation of a new financial institution. They are outlined below.

Short-term recommendations:

The current project is managed and administered by a variety of institutions whose functions should change in order to increase effectiveness and efficiency. The following short-term recommendations are made regarding the responsibilities of the UCP, UCFs, ICIs and U.S. technical assistance.

UCP

- Limit loan review responsibility to project eligibility, except for loans over $500,000;
- Process loans over $500,000 through USAID/Bolivia;
- Channel technical assistance to the ICIs, sub-project borrowers, UCFs and Market Towns;
- Strike agreements with selected ICIs for blanket loan authority, staffing and training obligations; some of these may be financial intermediaries which are not active currently in the project, e.g., CACEN, FENACRE;
- Track DDC and MTCF portfolios and the rotating fund; and
- Limit "market town" activity to three current areas, as a pilot project.

UCFs

- Remove from credit approval and lending process;
- Convert to UPIs, Investment Promotion Units, to become the investment promotion instruments for their respective Departments;
- Help UCP channel technical assistance and coordinate with DDCs regarding the pilot market towns; and
- Maintain the current system of financial support until the end of the project.

ICIs

- Become totally responsible for credit judgement;
- Become primary recipients of technical assistance channeled through the UCP for project evaluation and follow-up;
- Develop and increase outreach capacity beyond urban areas, to be paid for by temporary increase in spread;
- (Selected ICIs) make agreements with the UCP regarding staffing, quality of analysis, follow-up, outreach capability, lessened bureaucratic restrictions for loan

approvals, and additional spread to cover operating costs of staff development.

<u>U.S. Technical Assistance</u>

Reorients its assistance toward specific results in four areas:

- o improving capabilities of ICI staffs;
- o training UPIs (UCFs) in investment promotion;
- o providing technical assistance to sub-project borrowers; and
- o working with "market towns" as pilot projects and not as the main focus of activity.

The evaluation team feels that given the above mentioned recommendations, by project completion date the following results are possible:

- o ICIs will have stronger internal and outreach capacities and will be able to manage a portfolio of 300-350 loans;
- o The rotating fund should equal $ 30-34 million;
- o UCP will be quasi government organizations supported by interest payments; and
- o UPIs (former UCFs) will be supported by combined DDC and private sector contributions.

Long-term recommendations

Over the longer term, other options are possible and are recommended. The following alternatives were identified by this evaluation team and are recommended for further study as possible long-term institutional directions.

- The UCP, as a quasi-public entity, continues to manage the fund;
- The project is transferred to the Central Bank;
- ICI intermediation is strengthened and UCF activities are reoriented; and/or
- a new private financial institution is created. The possibilities include:

    - a second story bank;
    - a financiera with dual functions (second story as well as retail);
    - regional financieras;
    - the purchase of an existing bank;
    - the establishment of a guaranty fund;
    - the establishment of a venture capital fund; and
    - the formation of a private trust fund managed by one or a group of private banks. (A model agreement for such a fund is located in Appendix I.)

II. POLITICAL AND ECONOMIC CONTEXT, 1978-1988

The current Market Town Capital Formation Project is the successor to two earlier projects, the Rural Development Planning (RDP) and the Departmental Development Corporations (DDC) Projects. The two earlier projects were designed and begun ten years ago when the economic and political climate of Bolivia was vastly different from what it is today, and when U.S. foreign economic assistance was guided by priorities that differ from those of the late 1980s. None of these three projects, which are the subjects of this evaluation, can be properly assessed without placing them in the political and economic context of the past ten years.

This context is especially significant because all three projects have been tied closely to Bolivia's political bureaucracy and its economic environment. In political terms, the projects initially were under the implementation authority of the Ministry of Planning and Coordination. Even though lines of authority changed over time, specifically with the creation of the Project Coordination Unit in 1983, the projects remained tied to the Ministry. It is significant to note that during the life of the projects, Bolivian governments have changed with such frequency that there have been 12 different Ministers of Planning to which the projects have reported. These numerous changes have represented not only frequent turnovers of personnel, but also successions of governments with very different political philosophies, policies and programs. Complicating the philosophical agenda were the two years of strained relations between the U.S. and Bolivia during the Garcia Meza government. During this time, the projects were in abeyance.

Following Garcia Meza's exit from office in 1982, political relations between the U.S. and Bolivia normalized, but soon thereafter Bolivia's economy began to unravel. Within two years Bolivia was in the throes of the most serious economic crisis in its history. The October 1984-September 1985 inflations rate peaked at 23,000% and was not brought under control until 1986/87 when the economic stabilization policies of the current government began to take effect. Inflation has been reduced to the mid-teens, but is climbing and will likely exceed 20% by the end of 1988. In the meantime, a serious recession has set in.

The economic situation has been especially devastating for the DDC and Market Town projects, which aim to finance sub-project loans through the commercial banks. With regard to the DDC project, for example, between 1978-1985 none of the $10 million loan fund was disbursed. It was not until 1986, when both the political and economic situations had begun to settle, that disbursements began. The Market Town project, on the other hand, approved its first sub-project loan in July 1987, in the midst of the current serious recession.

These data are presented to illustrate exogenous, yet very significant constraints faced by all three projects. The current Market Town project, for example, is endeavoring to place loans for productive investment in an economic climate that lacks the incentives needed for investment, (as illustrated by the unknown political and economic direction of the government to take power in 1989, and that suffers from a fragile banking system, a constricted internal market, and difficulties in penetrating the external market.

It is also important to note that the past ten years have been characterized also by evolving U.S. policy priorities. When the RDP and DDC projects were designed and began implementation, the strategy of both AID/Washington and USAID/Bolivia focussed on public sector activities to help the rural poor. Over time the strategy has moved away from government planning and public works to private sector support and investment promotion.

The following evaluations assess the progress made and problems experienced by three projects which were implemented during chaotic times. The significance of the political and economic context of the past ten years cannot be overemphasized, and its legacy is the hopeful uncertainty in which Bolivia finds itself today.

The evaluation took place during July and August 1988. A draft report was submitted to USAID/Bolivia in September. Following consideration of USAID, UCP and contractor comments, received in full in December 1988, this final report was prepared in March 1989.

III. FINAL EVALUATION OF RDP/DDC PROJECTS

A. EVALUATION METHODOLOGY

This evaluation of the Rural Development Planning (RDP) and Departmental Development Corporations (DDC) Projects was conducted on the basis of extensive document reviews and interviews throughout La Paz and four other Departments.

In the case of the Rural Development Project, the team reviewed prior project evaluations, including those prepared by Development Alternatives and ABT Associates, as well as a USAID/Bolivia internal progress evaluation. The team also interviewed USAID/Bolivia and Market Town personnel who had knowledge of and/or experience with the project. Because the Rural Development Planning Project terminated several years ago, extensive interviews were not possible; furthermore, because the DDC Project was the immediate predecessor to the Market Town Project, and because the financial status of the DDC portfolio is directly related to that of the Market Town portfolio, more time was allocated to evaluations of both the DDC and MTCF projects.

The methodology employed to evaluate the DDC project involved many more interviews and document reviews.. The team spoke with personnel in USAID/Bolivia, the Project Coordination Unit (UCP) and the Unidades Crediticias Financieras (UCFs), as well as bankers, private sector representatives and investors. The team also visited DDC sub-projects in five Departments. In addition, the team reviewed numerous financial and descriptive documents concerning the DDC project.

Because the technical assistance provided under the RDP Project, and the loan portfolio opened under the DDC Project formed the foundations of the current Market Town Project, this evaluation is forward looking and discusses lessons learned, and their implications for the operations of the Market Town Project.

B. BACKGROUND, GOALS AND OBJECTIVES

The Rural Development Planning Project (RDP), signed in 1978, and the Departmental Development Corporation Project (DDC), signed one year later, were a combined effort to improve the standard of living of the rural poor in Bolivia. The RDP Project used grant funds to provide technical assistance to improve the quality of regional plans and to incorporate them into the national planning system. The DDC Project, supported by a $10 million loan, was to provide financial resources for sub-projects, primarily in the rural areas.

The goal of both projects was the same: to improve the standard of living of the rural poor in Bolivia. The purposes were to be complementary; that of the RDP Project was to improve the technical consistency and coordination of the planning systems in five Departmental Development Corporations (DDCs) and in the Ministry of Planning and Coordination (MPC). The purpose of the DDC Project was "to enhance the outreach capability of the DDCs to identify and implement sub-projects...of direct benefit to the target group."

C. EVALUATION

1. Rural Development Project

a. Implementation

The RDP Project began as a three year, $1.2 million grant to provide technical assistance in development planning. Its objective, as stated in the project paper, was "to make systematic conceptual and technical improvements in plan preparation and project preparation and implementation at the departmental and national levels."

It called for 21 work years of long-term, and three work years of short-term technical assistance. In addition, one staff person of the National Institute of Public Administration (ISAP) was to receive long-term overseas training. The long-term technical assistance was to be carried out by seven advisors assigned to the Departmental Development Corporations and to the Ministry of Planning and Coordination. These advisors were to provide on-the-job training to personnel of the DDCs and the MPC in operations management, systems analysis, and project design and implementation. Their efforts were to be supplemented by expertise offered by short-term advisors. The training component also included formal short-term courses in development planning and integrated rural development, as well as the development of training materials. A central feature of the project was that technicians would be assigned to work directly with counterparts in the participating DDCs. The Government of Bolivia contribution was to be $1.1. million to finance salaries of counterpart personnel, operating expenses, short-term training and in-country travel and per diem.

According to the Project Paper, the planning effort was deemed necessary to "correct the imbalance between the modern and traditional sectors of the economy and to raise the income and welfare of the marginal rural population." It was felt that the project would not only benefit this target group, but also would facilitate its direct participation in the identification and implementation of projects that would address its specific needs. Because the strategy was to help the rural poor, the departments targeted to receive assistance under this project were to be the more remote areas of Pando, Beni, Tarija, Potosi and Chuquisaca. In addition to providing technical assistance to the Corporations, the team would also be responsible for assisting the Government of Bolivia (GOB) prepare training materials and establish uniform criteria for project identification and evaluation for inclusion in the national plans.

b. Results

From the time the RDP Project was signed, in August 1978, until the final monies were expended in March 1987, the project size, level of effort and focus changed. The $1.2 million, three year grant grew to $4.2 million, and was expended over nearly nine years. The original intent of the project, to improve the regional and national planning process, also changed. Following reprogramming of both the RDP and DDC projects in September 1983, the RDP focus changed from that of improved government planning for development projects, to that of development through private sector investment in productive activities.

(1) Phase I - August 1978 - September 1983

During this period the project suffered many problems: start-up was slow, the technical assistance team disagreed over priorities, and relations between the U.S. and Bolivia became critical.

The contracting process and the fielding of consultants experienced a variety of delays. It was a year before the long-term contract with Practical Concepts was signed, and nearly another before all 8 long-term advisors were on board. Moreover, once in place, the members of the technical assistance team disagreed over project priorities. According to the <u>Review of the Rural Development Planning Project</u> conducted by ABT Associates in November 1981, the contractor, Practical

Concepts Inc. (PCI), "developed an internal schism over whether the greatest resources should be expended to develop...methodologies or...whether to focus on project design and implementation." According to ABT, "...too much time and resources were invested in the methodologies." The ABT review does credit the methodologies, however, for providing a means of capacity building in the DDCs, in terms of project design.

Finally, in July 1980, U.S.-Bolivian relations were suspended. According to the ABT Review, "one victim of this period was the originally proposed development of a permanent public planning and management training component for the MPC and the DDCs via ISAP."

One of the most important of the ABT recommendations was that the entire project should become operational. This recommendation was put into place with the reprogramming of the project in 1983.

(2) Phase II - September 1983 - March 1987

During this three and a half year period, the emphasis of the RDP project changed. According to the Development Alternatives Evaluation, (August, 1985) the most significant was the provision of technical assistance through the contracting of Bolivian, rather than third country, personnel.

In late 1983, when the Project Coordination Unit was established to manage both the RDP and DDC Projects, the focus changed again. Regional planning was deemphasized in favor of private sector investment. It was decided that technical assistance in regional planning to the DDCs had achieved its goals and could be de-emphasized. The DAI evaluation concluded that the "training, seminars, and publications improved the institutional capacity of the DDCs to elaborate coherent departmental plans and private sector projects." According to DAI, by the end of 1984, the technical advisors to nine DDCs had completed the tasks of developing regional surveys and operational one- and five-year plans. Since this task had been completed and had been termed a success, but since very few sub-projects had been approved, both USAID and the UCP decided to drop further planning activities and concentrate instead on the identification, promotion, design and evaluation of private sector sub-projects.

Through extensive interviews with DDCs and the UCP, the DAI evaluation concluded that the results of the technical assistance provided under the RDP Project were mixed. The DDCs viewed the technical assistance in regional planning as successful, while that of advise in restructuring the DDCs and helping them with organization and administration was not. The technical assistance in sub-project promotion and design was said to be needed and worthy of continuation.

2. Departmental Development Corporations Project

a. Implementation

The Departmental Development Corporations Project (DDC) was signed in September 1979, to provide financial resources and technical assistance to the DDCs to improve their capabilities to plan, design, and implement sub-projects aimed at improving the standard of living of the poor. The stated goal of the project was "to improve the standard of living of the rural and urban poor (the target group)". The purpose of the project was "to enhance the outreach capability of the DDCs to identify and implement sub-projects ... of direct benefit to target group communities".

By providing financial resources to the DDCs for the purpose of strengthening their outreach capabilities to implement sub-projects, the project was expected to complement the technical assistance being provided to the Corporations under the Rural Development Planning Project (RDP).

The DDC project provided a loan of US$10 million to include $9.7 million for sub-project financing and $0.3 million for technical assistance. As with the RDP Project, implementation was suspended from July 1980 to September 1983.

In 1983, as political difficulties eased, it was determined that the two projects should be reprogrammed and that implementation should resume. Resumption was authorized by Project Implementation Letter (PIL) No. 16, dated September 15, 1983.

Although the stated goal of the DDC project "to improve the standard of living of the rural and urban poor" remained unchanged by PIL No. 16, the purpose of the project was restated "to improve the capability of the DDCs to promote, design, and implement productive rural development projects, especially in cooperation with the private sector, which will be of direct benefit to target group communities".

In addition to AID loans and grants, GOB counterpart funds under PL-480 were provided by PIL No.16 for local currency costs of "experimental or non-directly productive rural development and infrastructure projects." Counterpart funds ultimately reached a total of $6.1 million.

As a result of the technical assistance provided by the RDP project, the Project Coordination Unit (UCP) was created in late 1983 as a semi-autonomous project implementation unit for the DDC Project, under USAID guidance.

In 1985 the first Financial Credit Unit (UCF) was created within the DDC of Santa Cruz. Similar units were subsequently established within eight DDCs. The UCFs were and are responsible for the promotion, design, and monitoring of the DDC sub-projects.

Although the DDC project originally had a completion date of July 1983, PACD was extended to December 31, 1986, as authorized by PIL No. 16 and then to March 31, 1987 by PIL No. 148. This completion date also applied to the RDP project.

In August 1985, an interim evaluation of both projects was undertaken by Development Alternatives, Inc. That evaluation covered initial implementation of the projects through the early stages of reprogramming. In view of the change in project purpose as expressed in PIL No. 16, this final evaluation concentrates on the final three year of project activity. It looks at the socioeconomic, institutional and financial impacts of the project. Finally, it discusses lessons learned and their implications for the follow-on Market Town Capital Formation Project.

b. Achievement of Objectives

(1) Socioeconomic Impact

This analysis of the socioeconomic impact contains general conclusions and observations based on interviews and meetings with sub-project borrowers, bankers and personnel from the UCP and the UCFs. It provides an overview of the positive and negative socioeconomic effects of the DDC project; it does not offer an in-depth analysis since supportive research was not possible due to time limitations and the more important priority of providing recommendations for the future direction the current MTCF Project. Of the approximately 20 sub-projects the team visited, half pertained to the DDC project. Almost all of the 50 bankers interviewed had experience with the DDC project, as had all members of the UCP and UCF staffs. Nevertheless, the conclusions drawn here are based on conversations, not on the results of a rigorous survey of the beneficiaries.

In socioeconomic terms, the DDC project results are mixed. On the positive side, sub-projects financed by the DDC project created jobs. According to the Memoria prepared by the UCP, nearly 2,500 jobs directly related to the sub-projects were created and indirect employment generation topped 6,000, with the principal benefit accruing to the agricultural sector. Employment was created in agriculture, industry, agroindustry, artisanship and production.

On the negative side, many of the DDC sub-projects experienced serious difficulties which had profound adverse affects on the borrowers. Delays in the processing of loan applications as well as in the arrival of equipment impeded sub-project implementation and/or continuation. It was not uncommon for loan disbursements or equipment to take months to reach the client and some experienced two year delays. The causes were many, and included the unwillingness of foreign suppliers to recognize Bolivian letters of credit (due to the economic chaos of the time). The point is, however, that borrowers often found themselves in very serious predicaments. Some of those awaiting timely disbursements found themselves without capital at precisely the period of time in the production process when it was most needed. Others awaiting the arrival of imported equipment found themselves with completed, but empty, building shells and no productive capacity to generate the income needed to repay the loans. Some experienced such lengthy delays in the arrival of equipment that the two-year grace period expired and they were obligated to repay not only interest, but also principal on projects that had not yet started. This unfair situation left some sub-projects in desparate straights before they began.

Other sub-projects had and have experienced problems because of poor conception or design, or incomplete market analyses. In some cases, no market existed, in others the market was saturated, still others had problems accessing marketing channels.

These and other problems experienced by the sub-projects are cited here to point out that the socioeconomic impact on borrowers has been mixed. While on the one hand employment was generated, on the other, serious economic problems have characterized several projects, and have adversely affected both investors and employees.

(2) Institutional Impact

Institutionally, the RDP and DDC projects led to the creation of a project management system that continues to operate today, and both private and public entities played roles in DDC project implementation. At the national government level, USAID/Bolivia and the Ministry of Planning and Coordination oversaw the project. At the operational level, both existing and new institutions handled and implemented the project. The primary actors were the Departmental Development Corporations, the private commercial banks and the newly created Project Coordination Unit (UCP) and Unidades Crediticias Financieras (UCFs).

a) Departmental Development Corporations (DDCs)

When the DDC project was first conceived, the Corporations were to play central roles in project implementation. The original design called for the creation of new offices within each Corporation to plan, evaluate and supervise activities funded through the project. As of July 1980 when the project was suspended, however, no formal offices had yet been established. By the time the project resumed three years later, economic and political events led to new thinking; the project's orientation was changed and it became less focused on planning and more dedicated to investment promotion and financial intermediation. As a result, these new offices assumed very different responsibilities; in essence, they began to act as liaisons between private investors and the banks. It became evident that they could no longer exist as ad hoc units located within the Corporations; they would have to be formalized, given structure and be located outside the Corporations. In May 1984, AID Project Implementation Letter No. 23 was signed and approved the creation of these new entities, called Unidades Crediticias Financieras (UCFs).

b) Financial Credit Units (UCFs)

The UCFs were created to help channel the loan resources of the DDC Project. They were created as semi-autonomous units and established offices outside the premises of the parent Corporations. In fact, they invited private sector participation on their boards. Nevertheless, the DDCs continued to exert influence over UCF operations. Informally, there were, and continue to be, close personal relations between the DDCs and the UCFs. Almost all the personnel who staffed the UCFs -from the managers to the drivers - had been previously employed by the Corporations. On a more formal level, the Presidents of the Corporations, who are appointed by the President of Bolivia, were and are, the chairmen of the boards of the UCFs. As such, although the UCFs were formally separated from the DDCs, the Corporations have continued to wield significant influence over the direction and operations of the UCFs.

Corporation support toward the creation of the UCFs varied from Department to Department, and to a large extent, changed over time. During the first phase of the project, which coincided with the Siles Zuazo government, most Corporations opposed the creation of the UCFs for both political and ideological reasons. The exception during this period was CORDECRUZ, in Santa Cruz. During the second phase of the project, under the current Paz Estenssoro government, most Corporations welcomed and supported the creation of UCFs.

The UCFs were formed over a two and one half year period beginning with PIL No. 23, dated May 23, 1984. The first UCF to be created was in Santa Cruz and by the end of the DDC Project, UCFs had been established in eight of the nine Departments. Only Pando, which was considered too small and underdeveloped to justify the creation of a UCF, does not have an office. Prior to the inauguration of the Paz government, political and bureaucratic delays hampered UCF formation, in addition, limited pools of qualified personnel, especially in the more remote departments, also delayed the process. The following is a list of dates when each UCF was created.

Establishment of UCFs

	Extra Officially	Officially
Santa Cruz	1984	Sept 1985
Cochabamba	Mid 1985	April 1986
Tarija	Mid 1985	Aug 1986
La Paz	1985	July 1986
Chuquisaca	Mid 1985	July 1986
Beni	Mid 1985	June 1986
Oruro	Mid 1985	1986
Potosi	Late 1986	1987

The institutional growth and consolidation among the UCFs has been uneven and has depended on the priorities of the Corporations, the UCFs, the existence of qualified staff and the perceived demands for sub-project financing. Not surprisingly, UCFs located in the more economically active departments have developed faster and deeper.

Overall, the staff composition for most UCFs appears to have been adequate to handle the volume of projects and the investment promotion activities envisioned. With the exception of Santa Cruz and Chuquisaca, however, none evolved to the point of becoming more complex regional development finance institutions. For the most part, the basic UCF staffing structure has consisted of a manager, one to three project evaluators, an administrator/accountant and support staff.

c) Project Coordinating Unit (UCP)

The UCP was created in 1983 and its efforts were fundamental to the creation of the UCFs. The UCP worked with the Corporations to convince them to support a more private sector focus for the project and to create semi-autonomous units, the UCFs, to implement that focus.

The main role of the UCP was to provide overall coordination and supervision of the project. The UCP worked with the Corporations, the UCFs, banks, investors, USAID/Bolivia and the Ministry of Planning and Coordination. Its primary role, however, was as the GOB representative to the project; the head of the UCP was appointed by and reported to the Minister of Planning and Coordination.

While no direct authority existed between the UCP and the UCFs, the Project Coordinating Unit had direct participation in several areas of UCF activity including the following:

Organizational

- Providing operating manuals and procedures
- Selecting and hiring staff
- Training (e.g. sub-project design and evaluation seminars)

Supervisory

- Credit Approvals
- Reporting activities and results
- Controls

Financial

- Rediscount of loans
- Funding of operations

Support

- Investment promotion
- Institutional promotion (seminars for ICIs)
- Technical assistance (for sub-projects and ICIs)

From 1984 until the PACD in 1987, the UCF, UCP and PL-480 evaluated projects which USAID/Bolivia then reviewed for approval. These approval procedures were quite cumbersome and a 1985 midterm evaluation recommended simplification. These recommendations were implemented and the momentum of the project picked up.

d) Intermediate Credit Institutions (ICIs)

The original DDC project did not contemplate a role for the ICIs, but upon its revival in 1983, the redesigned project included their participation. In fact, a major achievement of the DDC project was the integration of the country's commercial banks into the project. After September 1985, the ICIs became major actors in the project. During the period of project execution, the UCP reached agreement with 12 major banks throughout Bolivia to participate in the project. The banks and the extent of their participation are shown in the following table:

Bank Participation in DDC Project

	Bank	Number of Projects Refinanced	Total Amount	Average per Project
1.	Crédito Oruro	42	3,247.9	77.3
2.	Cochabamba	32	4,428.9	138.4
3.	Santa Cruz	19	2,314.4	121.8
4.	Mercantil	14	742.8	53.1
5.	Nacional	10	467.2	46.7
6.	BIG Beni	7	1,898.2	271.2
7.	Hipotecario	4	859.0	214.7
8.	La Paz	2	238.7	119.4
9.	Unión	2	384.8	192.4
10.	BLADESA	1	73.1	73.1
11.	Inversión	1	148.7	148.7
12.	Potosí	1	249.8	249.8
TOTAL		135	15,053.5	111.5

Intermediate credit institutions played a fundamental role in the marketing of the DDC credit program, the analysis and evaluation of sub-projects, and the administration of loans. Most significantly, they were the final risk takers vis-a-vis USAID/Bolivia.

Both the banks and the UCFs marketed the DDC credit program. Project analysis and evaluation was performed by most of the major commercial banks who used their own technical departments and specialized staff to handle these tasks. Some of the smaller banks, however, relied on UCF or consultant evaluations and analyses.

Credit management and monitoring was probably the area where the banks were weakest. In large part, this was due to inadequate staffing and infrastructure as well as to the prevalent concept that the clients were responsible for the loans, since they were fully guaranteed. No evidence was found, except in a few selected cases, of banks doing actual follow up on projects.

Risk was assumed by the banks. Their role as guarantors of loans before USAID/Bolivia was crucial to the project. Because the banks assumed the risk, they determined, to a large degree, the accessibility of the credit to certain segments of the population, and their perception of risk determined the type and level of collateral required or even if the loans were granted or not.

(3) Financial Impact: Status of DDC Loan Portfolio

a) Background

The Project Loan Agreement for the Departmental Development Corporation (DDC) Project was signed on September 20, 1979 with USAID providing $10,000,000 in loan funds and the Government of Bolivia (GOB) providing $3,500,000 in counterpart funds, for a total of $13,500,000.

b) Project Operating Procedures

Under the project, $10,000,000 in loan funds were provided to the GOB as a 40 year loan at concessional rates of interest. Procedures called for the GOB to pass these funds on to the DDCs in the form of grants, which would ultimately be lent to Intermediary Financial Institutions (ICIs) for on-lending to sub-project borrowers.

Sub-project loans provided by the ICIs required that the latter assume all credit risk. Although early subloans did not call for dollar maintenance, later loans carried this restriction, thus passing the exchange risk on to the sub-borrower. Interest and loan amortization payments were made to the ICIs and passed on by the banks to the Financial Credit Units (UCFs).

Interest rates with dollar maintenance were set at 13% with the ICIs retaining 5% and the UCFs and the Project Coordinating Unit each receiving 2% (subsequently changed to 2.4% and 1.6% respectively). The balance was to be held by the participating UCF in a revolving fund for relending.

c) Loan portfolio analysis.

(i) Portfolio Breakdown

At project completion date, March 31, 1987, a total of 135 projects had been financed for a total investment of $15 million. A breakdown by department and source of funding is as follows:

DDC Portfolio Breakdown by Funding Source

DEPARTMENT	PROJECTS	SOURCE OF FUNDING USAID	PL-480	TOTAL
BENI	8	$720.3	$1,077.3	$1,797.6
COCHABAMBA	25	2,014.0	811.0	2,825.0
CHUQUISACA	14	1,362.2	656.2	2,018.4
LA PAZ	12	1,077.2	903.0	1,980.2
ORURO	6	120.3	19.2	139.5
POTOSI	3	22.5	28.5	51.0
SANTA CRUZ	24	2,664.4	1,068.5	3,732.9
TARIJA	43	1,171.0	1,337.9	2,508.9
TOTAL	135	9,151.9	5,901.6	15,053.5

Analysis of the loan portfolio provides the following information:

- o 65% of total funds disbursed (approximately $9.8 million) are concentrated in the rural areas of the country.

- o 102 of the 135 projects financed are located in the rural areas, with an average investment of $95,000. The average urban area investment was $160,000 at project completion date.

- o While 47.7% of available funds, approximately $6.4 million, was devoted to 39 agro-industrial projects 23% financed 54 projects in the agropecuario sector for a total of $3.4 million. $2.8 million funded 12 small industrial projects with the balance funding 30 projects in agriculture, industrial support, and handicrafts sectors.

- o As of March 31, 1987 81% of approved credits had been disbursed, the balance representing the importation of capital equipment in transit as well as working capital assistance to be made available when project implementation began.

(ii) Breakdown of portfolio by Intermediary Financial Institution as of March 31, 1988:

DDC Portfolio Breakdown by ICI

(000's)

Bco. de Cochabamba	$3.838
Bco. de Crédito Oruro	2.687
Bco. de Santa Cruz	1.899
BIG Beni	1.828
Bco. Hipotecario	.855
Bco. Mercantil	.672
Bco. Unión	.371
Bco. Nacional	.358
Bco. La Paz	.033
Bco. Potosí	.226
Bco. Inversión de Bolivia	.147
TOTAL	$13.022

(iii) Payment Status by Department as of March 31, 1988

It should be noted that the portfolio has not yet been turned over to the UCP, therefore the exact status of individual projects is unknown. Some loans are known to have been reprogrammed although the exact figures are also unknown. Past due payments of principal may have been avoided by reprogramming.

DDC Payment Status by Department

($000)

DEPARTMENT	TOTAL DISBURSED	REPAYMENT	PAST DUE
Santa Cruz	$3.118	$.116	0
Cochabamba	2.551	.108.7	0
Chuquisaca	1.714	.155.0	.062
Tarija	2.311	0	0
Beni	1.723	.068	0
La Paz	1.804	.006	.111
Oruro	.110	.006	.010
Potosi	.057	0	0
TOTAL	13.387	.459	.183

D. CONCLUSIONS

The DDC project was approved and began implementation shortly before a period of economic and political instability that lasted several years and which made success of the project extremely difficult. Originally designed to assist the Departmental Corporations in largely public sector development activities, the project was suspended for two years and reactivated with a greater orientation to the private sector. In fact, ninety percent of the DDC loans were approved after its reactiviation and during the last year and a half of the project, between August 1985 and March 1987. The purpose of the project, however, continued to be directed toward improving the standard of living of the rural and urban poor.

One of the major achievements of the DDC project was the establishment of a refinancing system in the midst of an adverse political climate and difficult financial conditions. The DDC project helped change thinking within the public sector that the most efficient and optimal use of development resources could be channeled through the private banking system, rather than through the public bureaucracy.

The DDC project achieved success as well in the area of institution building and in terms of the number of sub-projects it developed. It also experienced a number of operational and control problems, however, that overshadowed its successes. The following factors limited the project's success:

1. The highly uncertain economic environment during the life of the project was a major hindrance to achieving project goals. De-dollarization, unprecedented levels of inflation and recession produced an atmosphere that was negative for investment. Those investments which did occur, moreover, were designed and developed with financial and marketing projections that proved to be overly optimistic as economic conditions changed.

2. A cumbersome approval process which included the DDC, the PL-480 Secretariat, the UCP, USAID, and finally, the ICI. The number of institutions involved, and resultant bureaucracy, led to serious approval and implementation, delays.

3. Shortages of counterpart funds provided by PL-480 often halted sub-project implementation unless the

borrower had other sources of working capital. There were instances in which sub-projects had received all the necessary approvals, yet local currency funds were short, and disbursed after several months of delay.

4. Overly optimistic sub-project proposals did not properly anticipate the marketability of the product being produced. In at least one instance two projects were undertaken to produce the same product in a marketing area that could not possibly absorb the output of both producers. In another instance sub-projects created to meet the demand for chicken subsequently found that they could not readily meet the competition from imports from Argentina. Other sub-projects suffered similar competition from Chile, Argentina, and Brazil. Although ever-changing economic conditions within the region were a significant factor, it would appear that there was insufficient emphasis on market analysis. A significant number of sub-projects have found that projected production goals were met due to unanticipated competitive factors. The end result has been reduced sales and a consequent shortage of the working capital necessary to proceed with sub-project development and to meet loan repayment obligations.

5. Inappropriate importation procedures for machinery procured abroad. Due to the economic crisis during project implementation, the issuance of standard letters of credit from Bolivian banks was not possible. USAID/Bolivia utilized an alternative mechanism, a letter of commitment, to the supplier to guaranty payment. In a number of cases, however, suppliers of machinery from neighboring countries would not accept the Letters of Commitment and resultant importation delays ranged from 6 months to 2 years.

6. Insufficient follow-up to sub-projects in distress resulted in unattended problems becoming more severe. Technical assistance to sub-projects will be a continuing need given the kinds of borrowers the program supported and the difficult areas of the country in which the projects are located. In the end, the success of the DDC project will depend on the successes of the sub-projects. Sub-project success will be determined by each one's ability to pay off its loans and to continue to operate and grow as a successful business.

7. Inexperienced subborrowers undertook projects in which they had little expertise, often resulting in failed or delayed implementation.

8. Requirements that the borrower use either his own funds or working capital borrowed for the sub-project to meet operating needs until imported equipment was received and installed. This often resulted in illiquidity just as project implementation was to begin, causing further delays while new sources of working capital were identified and put in place.

E. RECOMMENDATION

Of immediate concern is the status of the DDC loan portfolio which, to date, has not been transferred to the UCP. Until the transfer takes place, the UCP has no effective control over the capital reflows and the distribution of interest. Therefore, it is recommended that the DDC loan portfolio reconciliation be completed as soon as possible so that the portfolio can be transferred to the UCP.

IV. MID-TERM EVALUATION OF THE MTCF PROJECT

A. EVALUATION METHODOLOGY

Much like the evaluation of the RDP and DDC projects, the methodology employed to evaluate the MTCF Project consisted of extensive interviews and document reviews. Interviews were conducted in Cochabamba, La Paz, Oruro, Santa Cruz and Sucre with over eighty five people including representatives from nearly 20 banks, 7 private sector chambers as well as personnel in the UCFs and DDCs of the respective Departments. Site visits were conducted to approximately 20 sub-projects about evenly distributed among DDC and MTCF projects. The team reviewed project documents provided by USAID/Bolivia, the UCP and Development Associates as well as other relevant materials.

B. PROJECT BACKGROUND

1. General

The MTCF project, authorized in July of 1986, is a follow-on assistance program to two previous AID funded projects, the Rural Development Planning project (RDP) and the Departmental Development Corporations(DDC) project. An evaluation of the RDP/DDC projects concluded that a future project should strengthen the UCFs, more fully utilize the capacity of participating ICIs, and concentrate on financing and implementing sub-projects in rural areas by further developing cooperation among the UCFs, ICIs and investors. The MTCF project is the outgrowth of those recommendations.

This mid-term evaluation of the Market Town Capital Formation (MTCF) project is being conducted somewhat earlier than originally projected due to the Mission's concern for the project's ability to become self-sustaining by project completion date of July 1991. Although the Project Paper was signed in July of 1986, there was considerable delay in project implementation and the first sub-project loan was not disbursed until July of 1987. Under the circumstances, this mid-term evaluation has little loan history with which to analyze the loan portfolio, especially with regard to its quality and conformity with Project Paper guidelines. Nevertheless the financial analysis will assess the potential for project self-sustainability and institutional considerations.

2. Goal and Purpose

The goal of the project is to achieve a higher standard of living through increased employment and production in Bolivia's rural and semi-urban areas. The purpose of the project is to increase the level of productive private sector investment in Bolivia's rural and semi-urban areas.

By project completion date it is expected that the following conditions will exist:

- o Private sector investments in productive rural enterprises, notably in 5 to 10 priority market towns, will have increased significantly.
- o ICIs will be performing more effectively and their development loan portfolios will have increased substantially.
- o The UCFs will be working effectively as investment promotion entities.
- o A UCF Credit Fund will be created and operating.

3. Implementation Plan

This section discusses the implementation plan of the Market Town project. It reviews plans for institutional development, investment promotion and financial development.

a. Institutional Development

The institution-building focus of the project was to develop the role of the UCFs as investment promotion entities and intermediaries between potential investors and ICIs interested in expanding their rural investment loan portfolios. In addition, the project aimed to strengthen the UCP, and secondarily, the participating ICIs. Both the UCFs and the UCP were to receive technical assistance and training in technical as well as in administrative areas.

The UCFs, which were created under the DDC project to respond to the investment needs at the departmental level, were to have expanded roles in the Market Town project. They were to continue performing those tasks which they had begun under the DDC project, such as identifying investment opportunities, encouraging investors to submit sub-project proposals and inviting local banks to use the MTCF refinancing line. In addition, they were to prepare annual investment plans, assist investors and ICIs develop sub-projects, and also approve, monitor and assist sub-projects where needed.

Each UCF was to have a minimum staff of four professionals who would cooperate closely with the respective DDC planning departments and work closely with the development lending departments of the ICIs operating in their regions.

The second level of institutional strengthening was to be focussed on the UCP, located in La Paz. Created under the DDC project due to lack of institutional support for the project from the Ministry of Planning and Coordination, the UCP handled the loan component of the DDC Project and helped create the UCFs. Under the Market Town Project its responsibilities were increased. Its expanded functions were to include:

- provision of technical assistance and training to the UCFs;
- establishment of a UCF Credit Fund;
- approval of UCF annual investment plans;
- approval of sub-project loans; and
- liaison with the Ministry of Planning and Coordination, USAID/Bolivia and the PL-480 Secretariat.

The UCP was to be staffed by a Director, three project development officers, a financial analyst, an accountant, a banking expert, a regional planner and two secretaries. In addition, a long-term technical assistance team was to be contracted to provide support in the areas of investment promotion, small enterprise development and marketing. One of the principal responsibilities of the long-term technical assistance team was to be the selection and promotion of investment in priority market towns.

Another important institutional strengthening objective was to stimulate the private banking sector to become more actively involved in economic development, especially the financing of investment activities in rural areas. It was hoped that the banks would reorient their policies and begin lending to new clients and new types of activities.

Under the MTCF project, the ICIs were to be encouraged to work more closely with their clients and the UCFs, and to improve their monitoring of sub-projects.

As a means to strengthen the institutional capacity of the UCFs, UCP and the ICIs, the MTCF project was to provide technical assistance and training. Both long- and short-term technical assistance, as well as training through workshops, trips and on-the-job instruction would address these needs.

b. Investment Promotion

Investment promotion was the second major area to be addressed by MTCF project and was to be primarily the responsibility of the UCFs, although all other entities were encouraged to promote investment. The UCFs were to prepare annual investment plans that would identify the strengths of their respective regions and conform to the development priorities of their respective Corporations. The promotion of priority market towns was clearly to be the primary focus and the process involved the selection, analysis and support of towns. These efforts would support one of the main aims of the MTCF project: the promotion of investment in secondary areas.

c. Financial Development

The objective of this component was to improve the UCF-based investment financing system already created under the DDC Project. The MTCF project aims to strengthen the investment financing system by: 1) increasing the refinancing resources available; 2) ensuring strict compliance to sub-project selection criteria, especially with regard to socioeconomic impacts; 3) facilitating a decentralized credit approval process; and 4) establishing a UCF Credit Fund.

Sub-project approval would depend on its meeting eligibility criteria and financial viability. In order to qualify, loans refinanced under the MTCF project were to develop or expand productive, privately owned enterprises located either in priority market towns, or in other areas outside of Bolivia's three major urban centers (La Paz, Cochabamba and Santa Cruz). Other criteria called for forward and backward linkages to local economies and employment creation. In addition, some activities were specifically excluded from financing.

Financial viability was to be the responsibility of the ICIs, especially since they would bear full responsibility for repayment risk. For the initial period of the project, however, a Credit Committee and USAID/Bolivia would approve all loans. A decentralized approval process would begin once the project's guidelines were well understood.

C. <u>PROJECT EVALUATION</u>

1. <u>Introduction</u>

The MTCF project is not quite at the midway point. As such, it is not possible to draw definitive conclusions about certain aspects, especially regarding the quality of loans and sub-projects. Nevertheless, this evaluation makes the following observations:

- o The project is significantly behind its implementation schedule;
- o The overall system is not a system; it lacks clear lines of authority and permanence;
- o UCP management is weak and is not results oriented;
- o There is excessive focus on the creation of Market Towns (pilot project) to the exclusion of operating imperatives;
- o Geographic and subsectorial restrictions limit success;
- o Red tape and bureaucracy are excessive; and
- o Self-sufficiency by 1989 is not attainable.

The section will discuss the achievements of the project purpose as measured by its institutional, technical assistance and investment impacts.

In all fairness, it must be noted that the project faced a variety of constraints. They included:

- understandable resistance on the part of the UCFs regarding the reorintation, if not change, in their mission;

- slow acceptance on the part of the banking system for the FOCAS line. Their resistance was due, in part, to the geographic and sectoral restrictions placed on the projects, and to the changes and difficulties experienced in the financial system itself.

- conflicting goals within the project's design which called simultaneously for the promotion of investment (to a target group with limited resources and that is usually outside the formal banking system) as well as project self-sufficiency (which requires numerous loans of sufficient magnitude to generate the necessary reflows).

2. <u>Achievement of Project Purpose</u>

a. Institutional Impact

1) Performance of the Overall System

The overall system, judged in terms of administration, management and implementation, is cumbersome and bureaucratic. This is due, in part, to the complex array of entities involved in the project and to the changes it has undergone. The various entities include the Bolivian Ministry of Planning, the Departmental Development Corporations, USAID/Bolivia, the PL 480 Secretariat, the Project Coordinating Unit, the UCFs and, finally, the commercial banks. The relationship among these entities, and the levels of authority each has had, has changed over time. For example, in April 1988, the UCP approved a new set of operating guidelines. These guidelines aim to streamline and simplify the loan approval process, a needed development. They are mentioned here not only to illustrate that positive steps have been taken, but also to show that the Market Town project is still in a developmental stage and procedures remain rather fluid.

One of the most serious institutional issues is the lack of lines of authority among the various entities involved in the project. The UCP, for example, has no authority over the UCFs, which could be considered, in theory, its branch offices. The primary role of the UCFs, on the other hand, is to promote investment, yet they remain financial dependents of the Bolivian government's Departmental Development Corporations. The lack of lines of authority implies lack of responsibility and accountability; in sum, the structure does not combine financial and human resources in a productive way.

The following sections discuss the roles of the major entities involved in project implementation.

2) UCP

The UCP is the central coordinating unit of the MTCF project. It has two major departments: financial and project. The financial and accounting department tracks the sources and uses of MTCF funds as well as the reflows of principal and interest to the revolving fund. The project department, on the other hand, reviews sub-project proposals sent to the UCP for approval. The UCP is also the locus of the external technical assistance provided by Development Associates, Inc.

This evaluation found the UCP to be in a very early stage of development and without a strong command of its functions. It has spent far too much time concerned with internal issues and with activities that have not yielded concrete results. The inward focus on administrative issues has meant that sub-projects in the field have not been tracked. As a result, some subprojects are in serious trouble and their problems belatedly have been identified and addressed. The UCP's concentration on administrative over operational issues has also led to lengthy delays in sub-project review and approval.

The most recent operating guidelines, approved in July 1988, suggest that the UCP recognizes these weaknesses and is overcoming them. This evaluation team strongly recommends that the UCP's greatest attention be focussed on assisting sub-projects in need, developing strong future sub-projects and working with the ICIs to strengthen their analytical and tracking capacities.

3) UCFs

In their original conception, the UCFs were to be the project generating agencies. They would locate, analyze, and prepare projects for the ICIs. In turn, the ICIs would rely on the judgements of the UCFs about project viability. In the later stages, the banks were supposed to rely on the UCFs to supervise loans and render assistance when needed.

In practice this has not necessarily been the case. In some cases, the UCFs became interested promoters for investment schemes which have since faced severe difficulties. Another problem has been the multiple levels of review which retard and impede a businesses-like process. Since in practice, the banks will accept only their own project evaluations as the final basis on which to make the credit judgement, the evaluations of the UCF and the UCP have been often redundant. Finally, for the most part, neither the banks nor the UCFs have performed adequate on-going supervision of the loans.

This is not to suggest that the problems cited above were entirely the faults of the UCFs. To a large degree, they were the result of the project's design which placed investment promotion and approval roles within the same entity and which added bureaucratic layers to the approval process.

The investment promotion role assigned to the UCFs under the Market Town project is somewhat changed from the role they had under the DDC project, which was more financial in nature. This evolution has caused problems among some UCFs, most notably in Santa Cruz. Overall, the effectiveness of the UCFs in the current system is mixed. The most dynamic UCFs are located in the cities of Cochabamba, Sucre and Potosí.

The UCF in Cochabamba appears strong and is very favorably viewed by the local banks as well as the private sector. It was cited for having helped the banks with both investors and with the loan approval process. All parties are in frequent communication, and the banks and private sector feel that the Cochabamba UCF should be strengthened. The UCF views its role as promoting private investment. It should be noted that the private sector is very active and controls a majority on the UCF board.

In contrast to Cochabamba, the original UCF in Santa Cruz is non-existent. It has been completely subsumed under the authority of FINDESA, the newly created development bank. The Santa Cruz UCF feels its purpose is to facilitate regional and rural development in coordination with the DDC. Relations between the UCF and the private sector are strained in Santa Cruz. The private sector criticized the unit for not promoting a program for which there were many potential investors and suggested that the UCF should be entirely separated from the DDC. In part, this is underway and a new UCF will be formed in Santa Cruz.

4) DDCs

The DDCs have both financial and political ties to the UCFs. Financially, the DDCs support UCF salaries and other operating costs. Politically, Presidents of the Corporations are the Chairmen of the Boards of Directors of the UCFs. This structure presents the potential for the conflicts of goals and ideologies inherent between private and public entities. The DDCs are mainly focused on government development projects, such as infrastructure, road building, and irrigation, for example. The UCFs, on the other hand, are striving to find private investors to undertake productive activities. While the current government is receptive to and supportive of private initiative, a change in political ideology at the national level could and would affect the DDCs and hence, the UCFs.

5) ICIs

At the present time, Market Town loans are channelled through the commercial banking system. The ICIs are weak financially and in terms of human resources to do a quality job of project lending and follow-up supervision. Yet given Bolivia's stunted financial sector, the commercial banks are the only instruments available to serve this capital need.

The banks are currently facing serious problems. As an example, the Banco de Cochabamba, in Cochabamba, is currently doing 30% of the business it did 8 years ago. The banks are also facing a tightness of credit and the only two lines now readily available are MTCF and BID 213. For the most part, most banks expressed greater facility utilizing the BID line.

It must be noted, however, that various efforts are underway to restore liquidity to the banking system, and the central bank is taking seriously its obligations to supervise the system to guard its credibility. The central bank takes a strong position that the commercial banks should devote a portion of their portfolios to the medium- and long-term loans needed by the productive investment sectors. To this end, some of the banks have (in recent years) established development departments to evaluate project loans, and help make sound credit decisions. We encountered no banks which have yet organized departments to follow up these loans once disbursed, to insure that problems which come up are attended to as early as possible.

From the point of view of the banks, the Market Town project presents the following concerns:

- o The Market Town line is for long-term development projects, and the banks' historical role has been short-term commercial lending, and
- o The Market Town loan is restrictive in both the types of loans it will fund, and in the geographic limitations placed on the loans. The geographic limitations are also serious concerns of the private sectors in Santa Cruz, Cochabamba and La Paz.

From the point of view of borrowers, the MTCF project, because it is channelled through the commercial banks, requires guarantees that are above the reach of many potential investors.

Despite these drawbacks, this team recommends greater utilization of the private banking system in all aspects of project activity and the concurrent strengthening of the banks. This evaluation recommends that the MTCF utilize its technical assistance resources to help strengthen the banking system and that the project work with a selected number of the stronger banks over the remaining life of the project.

b. Technical Assistance Impact

1) Background

One of the key elements of the MTCF Project has been the provision of long- and short-term technical assistance. As originally envisioned, the long-term technical assistance would consist of three advisors for a two year period providing expertise in the areas of investment promotion, small enterprise development and marketing. Short term technical assistance would also be provided over the life of the project. The outside technical assistance team was to be located within the UCP and to act as advisors to it and to the UCFs.

Among the most important activities of the team, and especially of the Chief of Party/Investment Promotion Specialist, would be the selection of priority market towns and the supervision of market studies and promotional efforts designed to increase investment, especially in priority market towns. In addition, this specialist would provide advice and direction to investment promotion activities in coordination with the UCP and the UCFs.

The second line of activity to be undertaken by the outside team was to be assistance to the UCP, UCFs and private investors. A Small Enterprise Specialist would assist in the development of project ideas and in the preparation of sub-project proposals. In addition, this expert would train UCF personnel in small business management techniques.

Marketing would comprise the third activity area and this specialist would work with both UCP and UCF personnel to conduct regional and national market studies, assess the marketing plans of sub-project proposals and assist in making sub-project marketing arrangements. The total level of effort for the long-term personnel was to be 72 person-months of direct labor. Complementing this effort, the scope of work called for 48 person-months of short-term technical assistance to provide additional expertise in the areas outlined above, as well as in banking, financial analysis, and other areas of need which would surface over the life of the project.

A two-year contract was signed with Development Associates, Inc. on May 5, 1987. Two long-term specialists, including the Chief of Party, were fielded a month later. The third position was not filled until January, 1988. At that time, a new position was added and the team now totals four.

The contracting period has now passed its mid-point and progress to date has been mixed. This chapter will discuss both the accomplishments and the problems experienced in the past year. More importantly, this section will recommend what should be the future activities of the technical assistance team, especially given the recommended future directions of the overall MTCF project.

2) Accomplishments

Among the accomplishments of the Development Associates technical assistance have been:

- identifying and inaugurating three market towns;

- promoting private investments and facilitating loan applications and approval processes in the three market towns;

- providing management services to the UCP in terms of clarifying goals, objectives and procedures;

- preparing and disseminating studies in banking, angora rabbits and chickens, as well as several smaller papers. These included:

  - distributing the Angora Rabbit Industry Study to the UCFs and training their evaluators in the use of the Study's data and standards;
  - disseminating the results of the Marigold Study to the UCF in Cochabamba for it to share with potential investors;
  - circulating the La Paz Market Study for Chicken and Eggs to the UCF in Tarija and to Ronco;
  - sending the reports on the U.S. market for flowers and on marketing organizations to the UCF and flower growers in Cochabamba; and
  - assisting in the finalization of the new "Régimen Crediticio."

- providing technical assistance to projects, such as the flower growers in Cochabamba, the milk plant in Trinidad, the fur projects of Oruro and Huari and individual businesses such as Inestano, Cobolde, and Pach;

- searching for U.S. buyers for products originating from the fur projects of Oruro and Huari and from Agrosur;

- evaluating a marketing study prepared for Salvietti in Chuquisaca;

- designing and implementing seminars;

- disseminating publicity about the MTCF project through newspaper articles, advertisements and press briefings;

- identifying "implementation problems" and recommending "corrective actions" in their Quarterly Reports;

- drafting the 1988 Workplan for the UCP-FOCAS;

- visiting 100 DDC subprojects and identifying their technical assistance needs; and

- organizing the participation of the Corporaciones and FOCAS subprojects in the first Feria de Los Andes in 1988.

To a certain degree, Development Associates has provided technical assistance in the areas outlined in its contract scope of work. Investment promotion activities have led to the selection of three market towns and to the possibility of investment in these secondary areas (that otherwise would be excluded from traditional credit lines); business advice has been rendered to a few small enterprises; and marketing studies have been prepared on angora rabbits, chickens and fruit.

Yet it must be recognized that these "end product" accomplishments are only a small proportion of what could have been produced at this point in the contract's life.

3) Constraints

a) Delays

The overall FOCAS project is ten months behind schedule. Not surprisingly, many of the contractor's activities are also behind schedule. Some delays have been due to forces beyond the control of Development Associates, yet others are due to directing energy and manpower toward activities that have been process, rather than results oriented.

The first serious delay was in placing the marketing specialist. The individual originally proposed was unable to accept the position due to health reasons and the position was not filled on a full-time basis until 8 months after the contract was signed. It should be noted, however, that the current marketing specialist, who filled the post, provided short-term technical assistance to the project during the two months prior to his permanent posting. It should also be mentioned that a fourth position was created about the same time, and this additional manpower has eased the pressure caused by the shortage earlier on.

The second serious delay has been the provision of short-term technical assistance. Under the Development Associates contract, 48 person-months of short-term technical assistance valued at approximately $190,000 are to be provided to the MTCF project over a two year period. This essentially means that during the life of the contract, an average of two consultants could be working continuously with the project. As of June 30, 1988--midway through contract implementation--21 short-term consultants had carried out 7 assignments. Fourteen of the consultants had been contracted in the April to June quarter of 1988. Despite the fact the pace of technical assistance provision has improved, with only 9 months remaining in the contract, it seems unlikely that this valuable resource will be exploited to its full potential. Yet, this type of assistance was seen as the key instrument capable of producing real results by expediting future loans or strengthen existing projects to assure their success. All principal parties - Development Associates, UCP management and USAID/Bolivia - should have pushed to identify needs and then identify and field the appropriate personnel.

In addition to delays in the placement of long- and short-term personnel, there have been delays in providing substantive outputs as called for in the scope of work and as requested by the Project Manager. The team spent an inordinate amount of time debating, defining and refining goals, objectives, procedures, plans and project limitations. For example, in September of 1987 Development Associates identified six potential problems the project might face. This was a valuable effort and, while it was not necessarily within the DA scope of work, it focussed attention on broad and important issues. What is worrisome, however, is that the team spent months pressing these issues until they were finally recognized, and in the process, stalled the progress of much of the work delineated in their scope. What is even more worrisome, is that once the validity of the above issues was acknowledged, implementation delays continued. Most of 1988 has been dominated by the preparation of manuals and guides that affirm and describe the above agreed goals and procedures. In essence, more than one half of the technical assistance contract has focussed on definitions and process rather than on the provision of direct or third party technical assistance or on actions leading to increased investment. The talents of the consulting team could have been utilized much more effectively, and again, the fact that energies were not properly directed is not entirely the fault of the contractor. Stronger direction was warranted on the part of both USAID/Bolivia and the UCP to make sure results-oriented, rather than process-oriented activities were undertaken.

b) The Big Picture

Criticism has been leveled against Development Associates for failing to recognize the big picture and for concentrating energy on details. Given the fact the team identified and spent much time lobbying for the recognition of possible problems in the design and implementation of the MTCF project, it would be unfair to state that they failed to view the "big picture." It would be fair to say, however, that this view was somewhat academic and what the project needed, and continues to need, are results at the sub-project level. The Development Associates resource has been used to define management rather than to focus on concrete results, and to record priorities rather than to act on them. Action Plans have been prepared, but they have been interpreted so rigidly that they have been used as instruments to limit and to justify activities, rather than as tools to facilitate progress toward goals.

c) Communication

From the first Activity Plan prepared by Development Associates, communications problems were cited. The general consensus is that the situation has improved and that it continues to improve. This is due to the recognition by all parties - Development Associates, UCP and USAID - of the serious need to improve communications and coordination on both formal and informal levels. One result of this recognition has been the restructuring of the UCP which decentralizes responsibilities and facilitates communication.

4. Recommendations

There have been both accomplishments and problems in the implementation of the Development Associates contract. Most serious have been the delays in fielding personnel and facilitating needed outputs. Some of these delays were due to misplaced priorities and energies on the part of the contractor; others are due to lack of guidance from USAID/Bolivia and yet others to the lack of management support within the Unit. What is important, however, is that the activities of the next 9 months be as productive and useful as possible. USAID/Bolivia should rewrite the Development Associates contract to specify specific results in the following areas:

- ICIs- Provide training and technical assistance to strengthen ICI development departments and assist in creation of follow-up and work out departments;

- Sub-projects- Provide technical assistance to assure success;

- UPIs- Provide technical assistance and training to develop their investment promotion capabilities; and

- Market Towns- Limit efforts to three pilot towns.

c. Investment Impact/Self-sustainability

One of the primary elements of this evaluation is to determine if, within the limitations established by the project paper, the UCP and the UCFs can generate sufficient interest spread income to be self-supporting by project completion date in 1991. A preliminary analysis completed in March of this year indicates that this would be possible contingent upon the project's ability to achieve a certain level of new sub-project loan placements. Since the time of that analysis there appears to be no reason to change those placement goals, however, there has been one substantial alteration which indicates that the goal of self-sustainability cannot be reached by project completion date.

This alteration refers to the collectability of a substantial portion of the DDC portfolio. Although the total amount of funds disbursed has not yet been reconciled, the value of the portfolio is, nominally $13.2 million. The repayment history to date, plus the uncertain status of the sub-project loans with the Banco de Credito de Oruro, now in liquidation, made it necessary to reduce the value of the portfolio by 30%. This, of course, will have an effect on cash flow to the Capital Fund and on the interest spread income available to the UCFs and the UCP, to the extent that self-sustainability will be pushed beyond project completion date.

The five-year projections which are discussed in detail later in this section make certain assumptions that lead to the conclusion indicated above. The most important variable concerns the goals set for new sub-project placements funded both by the MTCF project and by reflows from the DDC portfolio. These goals appear to be realistic given the geographic limitations currently imposed by the project. They are, however, subject to revision depending on future performance and any changes that might be made in project guidelines. Placements could increase, for example, if the geographic and working capital restrictions were lifted.

Self-sustainability will depend, therefore, on the future growth of the portfolio. Its current status is discussed below.

1) Status of Project Loan Portfolio

As of June 30, 1988 funds for 29 sub-projects had been disbursed for a total of $3,467,613, of which $1,459.000 had been disbursed by year end 1988.

<u>MTCF Funds Disbursed by Department</u>

A breakdown of total funds disbursed by Department is as follows:

BENI	$267,260
CHUQUISACA	86,253
COCHABAMBA	771,946
LA PAZ	225,327
ORURO	17,000
PANDO	200,000
POTOSI	77,127
SANTA CRUZ	1,813,700
TOTAL	$3,467,613

A breakdown of total funds disbursed by financial institution is as follows:

MTCF Funds Disbursed by Financial Institutions

BOLIVIANO AMERICANO	$180,825
COCHABAMBA	117,770
BIG BENI	20,000
HIPOTECARIO	1,238,876
LA PAZ	201,579
NACIONAL	50,301
SANTA CRUZ	564,832
UNION	455,000
BLADESA	438,430
CACEN	200,000
TOTAL	$3,467,613

As of the time of this evaluation (July/August 1988), five-year projections indicate that the project will not be self-sustainable by 1991. (See spreadsheet which follows for five-year projects.) As per the spreadsheet's bottom line (Section F6 of Projects) the project does not have sufficient capital in the form of lending funds to generate a loan portfolio large enough to sustain all the participants over the long term. With a static loan portfolio and increasing expenses, the project will eventually start eating into capital.

The following comments apply:

Funds to be provided by AID are projected to be fully loaned out by year-end 1990.

Total portfolio loans will essentially peak at $30 million and will then be supplemented only by the interest spread earned and contributed to the Capital Fund for re-lending.

Starting in 1992 when AID ceases to contribute new funds, the only source of lending capital will come from loan repayments from the existing portfolio plus interest paid into the capital fund. (Section D 3).

Therefore, it is unlikely that the project will have sufficient resources to generate the cash flow necessary to sustain the UCP over the long run.

2) Five-Year Projections

DEPARTMENTAL DEVELOPMENT CORPORATIONS
MARKET TOWN CAPITAL FORMATION
Project Loan Portfolio Analysis
Five Year Projections
(000's)

CAPTION	1987	1988	1989	1990	1991	1992	1993	1994	1995
A. New Loan Placements									
1. DDC	9,377								
2. MTCF	1,459	6,500	6,500	6,500					
3. REFLOW	91	966	2,697	3,625	5,103	6,545	7,844	10,726	12,050
TOTAL	10,927	7,466	9,197	10,125	5,103	6,545	7,844	10,726	12,050
B. Reflows									
1. DDC	365	1,998	2,805	3,447	2,092				
2. MTCF				486	1,653	4,820	6,500	6,500	6,500
3. REFLOW				30	352	1,251	2,429	3,808	5,091
TOTAL	365	1,998	2,805	3,963	4,097	6,071	8,929	10,308	11,591
C. Investment Total									
1. PLACEMENTS	10,927	16,395	22,787	28,949	29,955	30,429	29,344	29,762	30,221
D. Interest									
1. UCFs	218	284	426	592	753	922	934	906	917
2. UCP			230	319	405	496	503	488	494
3. C. FUND	601	699	820	1,139	1,447	1,773	1,796	1,742	1,763
TOTAL	819	983	1,476	2,050	2,605	3,191	3,233	3,136	3,174
E. UCFs									
1. INTEREST EARNED	218	284	426	592	753	922	934	906	917
2. DDC SUPPORT	462	425	283	117					
3. PREVIOUS BALANCE	0	0	0	0	1	45	257	482	679
4. TOTAL INCOME	680	709	709	709	754	967	1,191	1,388	1,596
5. TOTAL EXPENSES	680	709	709	709	709	709	709	709	709
6. PROFIT/LOSS	0	0	0	0	45	258	482	679	887
F. UCP									
1. INTEREST EARNED	0	0	230	319	405	496	503	488	494
2. USAID SUPPORT	434	1,724	1,168	0	0	0	0	0	0
3. PREVIOUS BALANCE	0	0	0	230	99	43	66	85	76
4. TOTAL INCOME	434	1,724	1,398	549	504	539	569	573	570
5. TOTAL EXPENSES	434	1,724	1,168	450	461	473	485	497	509
6. PROFIT/LOSS	0	0	230	99	43	66	84	76	61

UPC expenses were projected to show a very conservative annual increase (Section F 5). Nevertheless net profit is on a downward trend which would be dramatically accelerated should expenses prove to be unrealistically low.

From a strictly technical point of view, the project is viable in the short term and at Project Completion Date only <u>if the assumptions used in these projections are accurate</u>. If, however, there are any significant changes in the variables the very small profit figures in Section F 6 will move to the negative side and lending capital and/or reflows will be needed to pay operating expenses.

It should be noted that since the time of the evaluation, substantial lending has taken place. The next several paragraphs are based on information received by the evaluating team between September 1988 and January 1989. Because the evaluation took place in July/August 1988, approved subproject loans through June were used in the analysis. By that time 29 subproject loans had been approved. In the months between June and September, 1988, thirty six additional subproject loans had been approved.
By year-end 1988, actual total loan disbursements from FOCAS were reported to be $6.9 million. Projections in this evaluation indicate that they should have been $7.959 million (Section A2 1987 plus 1988) showing a shortfall of 13%. This will reduce interest earnings to the capital fund as well as capital repayments for on-lending.

Whether new-loan targets from reflows of $996 M (Section A 3) were achieved should also be investigated as any shortfall here would also affect future earnings.

The value of the DDC portfolio is still basically unknown although negotiations with the ICI's for the transfer of portfolio management is currently underway. Apparently a number of DDC loans are being restructured with revised repayment schedules that will further reduce reflows, interest earned, and, ultimately, project sustainability.

The main conclusion to be drawn from a review of the projections and the project's potential for self-sustainability is that, in the <u>short run</u> the project could be self-supporting if expenses can be restrained and earning asset placement goals are met. But in the <u>long run</u>, the capital available to the project for lending purposes cannot generate sufficient income without some adjustment.

The following steps could be taken to reverse this trend:

- o Continue AID support for operating expenses beyond the Project Completion Date;
- o Provide additional AID support to increase the ultimate size of the loan portfolio and thus generate more income;
- o Adjust interest rates upward to increase the interest spread paid into the Capital Fund for on-lending;
- o Reduce operating expenses of the Project (CPU);
- o Restructure the Project in terms of thee role played by the UCF's and the amount of interest spread paid to them.

3) Explanatory Notes to Five-Year Projections

For lack of readily available information at the time of the evaluation concerning the status and quality of each DDC project loan, a number of assumptions had to be made in order to prepare the five-year projections and determine the financial viability of the MTCF project. As of the time of the evaluation, the DDC portfolio had not been transferred to the UCP and current information concerning the repayment history of the subloans, and of the participating ICIs had not been made available and interest payments for these loans through the five-year period are a function of the value assigned to the entire portfolio as of the end of 1987.

A recently completed audit of the DDC portfolio has provided some information as of December 31, 1987 and March 31, 1988 so that figures for 1987 in the projections are actual, assuming the audit to be correct.

In March of 1988 a financial analysis of the MCTF project determined that the project could become self-supporting within the terms set forth in the Project Paper if projections for new loan placements were met. At the time the financial analysis was done, these projections were assumed to be the maximum that might be expected, given the geographic and demographic restrictions placed on the MTCF project. Although essentially the same new loan projections are being used in the current analysis, the results indicate that the participating units will not become self-supporting on schedule. This is the result of having reduced the value of the DDC portfolio by 30%.

In addition, although the ICIs are ultimately responsible for repayment, regardless of the status of the sub-project, it was felt necessary to reflect the potential loss of the loans channelled through the Banco de Credito de Oruro, which is now in liquidation. These loans account for 20% of the DDC portfolio and although the UCP is seeking permission of the Superintendent of Banks to transfer the loans to other financial institutions, it would appear prudent to consider their collectibility as a long-term work-out situation. Moreover, the ICIs with non-performing sub-loans are not meeting their own commitments to the UCF/DDCs to the extent that, according to the outside auditors, of the total loan amortizations due in the amount of $641,551 as of March 31, 1988, $182,515, or 28% is past due. Likewise, interest payments are 52% past due. Assuming that a number of loans with past due interest payments are still in the grace period, the question arises as to what will happen when these loans are obliged to begin repayment of principal. As a number of commercial banks are in a precarious position in terms of liquidity, it is more than possible that they will be unable to meet their own repayment requirements.

Under the circumstances it would appear that a projected loan loss of 30% in the DDC portfolio is not unrealistic. It is possible that many of the loans within the Banco de Credito de Oruro will be transferred and/or a number of the non-performing sub-loans will become collectible, but until such time as this takes place, interest earned as originally projected will not provide sufficient income to the UCFs and the UCP within the MTCF Project Paper timeframe.

4) Assumptions

a) New Loan Placements

The DDC loan portfolio in 1987 has been reduced by 30% to reflect potential collection difficulties.

MTCF loan placements are actual figures for 1987 and estimated for later years based on levels which the UCP can be expected to reach, based on current geographic and demographic restrictions.

New loans from reflows of the DDC portfolio are actual for 1987 and estimated for the following years. Latter estimates are derived from reduced projected loan repayments.

b) Reflows

DDC Loan repayments for 1987 are actual figures. Reflows in the following years are calculated on the assumption that the average loan is for five years with a grace period of two years. Therefore each loan will actually be paid over a three year period starting in year three after the first disbursement.

c) Investment Total

Total loan placements reflect the actual figure for 1987 plus new loans the following years, less loan repayments received during those same years.

Capital fund deposits refer to that portion of the interest spread earned which is deposited to that fund for relending purposes.

Figures represent distribution of interest spread to the units indicated. Interest spread due to the UCP will not be payable to the Unit until the last quarter of 1989 at which time AID support of operating expenses is scheduled to end.

d) UCFs

This section includes the figures for interest earned by the UCFs and the support required from the DDCs to meet operating expenses. It should be noted that UCF expenses are estimated as this information is not available from all of the UCFs. It should also be noted that DDC support is scheduled to end in 1991 at which time the UCFs are expected to be self-financing.

e) UCP

Until the last quarter of 1989 the UCP will continue to be totally supported by USAID grant funds. Interest rate spread currently due to the UCP is presently being held in a special account pending disposition.

5) Conclusions

- The MTCF project has not met its goals in terms of sub-project financing and UCF/UCP financial self-sustainability. This is due, in large part, to implementation delays. The most obvious indication of this short-fall is the Project Paper estimate of a total portfolio of $24.6 million by year end 1988 which would have brought self-sustainability by the end of 1989. While these projections were overly optimistic, the fact remains that, including the DDC portfolio, total disbursements at mid-1988 were approximately $16.6 million.

- o The less than projected portfolio size indicates a lack of promotional efforts on the part of the UCFs, limited interest on the part of the ICIs' bureaucratic delays in the approval process.

- o The repayment record of the DDC sub-projects indicates that project proposal analysis requires improvement. While there are several reasons for this record, including the current recession, it would appear that much of the problem lies with sub-project preparation.

6) Recommendations

In order to increase the pace of new loan placements and to increase interest spread income to the UCFs and the UCP, it will be necessary to consider the following actions:

- o Increase promotional efforts directed toward the ICIs;

- o Provide technical assistance in sub-project proposal analysis to those financial institutions that do not maintain a development banking department;

- o Reduce project operating costs by reviewing staff requirements at both the UCF and UCP levels; and

- o Eliminate geographic and demographic limitations in determining sub-project eligibility.

An analysis of the MTCF's investment impact and the possibility for self-sustainability would be incomplete without a discussion of the financial environment. Factors of risk, interest rates and guarantees determine, to a large degree, the numbers and types of borrowers who are acceptable and attracted to commercial banks. the characteristics of the MTCF loan portfolio, including its potential for self-sustainability, also will be affected by these factors.

d. Risk, Interest Rates and Guaranties

The current level of interest rates in Bolivia is artificially high. Short term loans, denominated in dollars, are currently being loaned at between 25%-30% - with most at the 30% level. The terms of these loans rarely exceed 90 days. These high rates reflect primarily the scarcity of resources for relending in the hands of the banks. The GOB's stabilization program has squeezed inflation out of the economy primarily by imposing severe limitations on credit. Perhaps the most influential factor has been the disastrous history of the Bolivian economy over the past ten years. It is primarily this history which has left the Bolivian economy with little or no national savings.

The only funds made available to the commercial banks for relending to their customers are provided in dollars, for short fixed terms, at interest rates of 16%-18%. These funds are very volatile, and no bank can count on their renewal when the fixed term expires. The one bank with a solid history of good management and in good financial condition - BISA - seems to be able to attract this money at about 13%, but the term is also short, reflecting not lack of confidence in the bank, but in the consistency of the political management of the economy.

The only loans longer than one year that are made by the commercial banks use the resources provided by the relending facilities of external assistance agencies through the central bank. These loans are made to the banks at LIBOR (currently 8%); the banks in turn lend to their customers at 13% and for terms up to five years. The DDC and MTCF loans have been made in this fashion, however, the central bank has not been used as the channel to the commercial banks. Therefore the commercial banks are able to earn a spread of 5% points on refinancing lines for "development lending", in contrast to about 10% points for the short term lending using their "own" resources. Currently, commercial bank loans comprise 60% short term loans made with their "own" resources, and 40% development loans made with refinancing lines from the central bank or USAID.

These refinancing lines made available to the commercial banks by the external agencies constitute the only sources of credit for productive investment in Bolivia today. It is to be expected that as confidence in the permanence of the economic stabilization program grows, and growth induces further investment and risk taking, that the demand for credit will exceed these limited capabilities.

The past two years of sensible economic management under the guidance of the IMF, and the return of positive economic growth, have brought some perceptible return of confidence to investors and creditors. There is already some evident competition returning to the credit markets with consequent downward pressure on interest rates. The IBRD loan for commercial bank restructuring is expected to restore substantial liquidity to the banking system which will further pressure interest rates downward. In sum, a restoration of more normal conditions - i.e. healthy liquid banks, under central bank supervision, in a climate of economic growth and sensible policies will remove the need for excessive risk premiums now being demanded by creditors.

Nevertheless, commercial banks are coming under pressure to submit to the regulatory force of the central bank. For the first time in many years, the banks are subject to audit, and are being required to classify their portfolios, and reserve against their non-performing loans. Further, the central bank is pressing the banks to form development departments to be able to evaluate projects and assess risk in the making of credit decisions. The clear aim of the central bank is to require the commercial banks to assume a primary role in medium and long term lending to productive investment in Bolivia.

In the face of these pressures, the banks are exercising extreme caution in their lending practices and policies. At the present time, total past due credits of the banking system approximately equal the total system's net worth. Thus it is no mystery that the banks are seeking high levels of personal guaranties from their borrowers.

Undoubtedly, the demand for these guaranties, which are said to run from one to three times the value of the loan, act to restrict access on the part of new borrowers,(i.e. those not having strong credit histories, and without qualified personal assets to encumber) yet who may have legitimate investment projects. This situation poses some conflict with USAID social and welfare objectives to expand the reach of credit to those who have not had access previously.

We do not believe that the requirement for personal guaranties to support lending need be such a potent force in the future on it has been in the past. There are courses of action which the USAID can take to ameliorate the situation. These actions fall under the general line of professional risk management.

Inevitably, improvements in bank liquidity and increased confidence in the economic system will induce some increased competition among banks to compete for credit placements. A strong flow of technical assistance to the banks to help create development departments, and add new department of follow-up and supervision of active loans, will complement the central bank's pressure to push the banks into development lending. The MTCF program could add incentives to the best of the banks to induce them to professionalize their risk management. An added point to the spread may help with the costs of added staffing. A willingness on the part of MTCF to change its way of dealing with the banks may add further incentives. For example, those banks which cooperate in the program and show progress should receive a blanket authorization of MTCF funds, say $1 million, to disburse for qualified loans without further prior approval by MTCF.

While more professional management of risk will indeed lead to lower loan losses, and allow risk judgements to be made more heavily on the merit of the project to be financed, it would be unrealistic to suggest that all personal guaranties would be eliminated from the process. Indeed, it is arguable that the existence of personal guaranties is a strong inducement to the project sponsor to go to any lengths to make the project a success. To eliminate this factor entirely, assuming it were possible under central bank regulations, would be to weaken substantially the motivation of the borrower, and imperil the validity of the credit.

D. RECOMMENDATIONS

This final section of the MTCF evaluation recommends new directions for the project. It first proposes a reorientation of the project's goals. As a result of this new emphasis, it then recommends changes in the institutional framework and new options for financial intermediation and investment promotion.

1. Goals and Objectives

Given the current economic realities of Bolivia, the goal of the MTCF project should be to support economic development and reactivation through private productive investment throughout Bolivia with priority to small and medium sized projects that have forward and backward linkages to the rural areas.

The implications of this restated goal include: elimination of geographic restrictions; reduced emphasis on "market town" activities; and elimination of working capital restrictions. These issues are discussed below.

a. Eliminate Geographic Restrictions

The MTCF project should provide loan resources for small and medium projects which meet criteria for employment and income generation in the industrial, agro-industrial, tourism and artisan sectors without restriction to location.

As presently stated, the main goals of the MTCF project are multiple and somewhat contradictory. The project's rural emphasis and its restriction of credits to Bolivia's main urban areas have been given excessive importance. As a result, the project has failed to reach its programmed level of implementation. The project has concentrated limited human resources on defining, selecting and trying to develop projects in areas that lack natural entrepreneurial sponsorship. The demand for productive project credit in so-called secondary areas is low, and will not change except slowly, over a long period of time.

In addition, the project has failed to identify and finance sub-projects which, although located in urban areas, have important linkages to the rural productive sectors. The evaluation team recommends that such projects be included due to the possible beneficial effects they would have on target groups in the rural areas. Those projects which have the greatest possible impact on these target groups, should be given high priority for financing.

b. Reduce Emphasis in "Market Town" Activities

The MTCF project should continue to support the market town concept, but at a reduced level, with concomitant reductions of human and financial resources. It should be considered a pilot concept.

This recommendation does not call for the total abandonment of the goal to create Market Towns and to support sound projects within these towns with MTCF credits. Indeed, the support of a limited number of

Market Towns, with a limited allocations of the human and financial resources would provide USAID/Bolivia with valuable experience to demonstrate whether this concept is workable and viable. At the present moment, this concept must be regarded as unproven.

c. Eliminate Working Capital Restrictions

The current restrictions on working capital loans should be dropped in favor of sub-project-based analyses of working capital needs.

The team found a great need for working capital financing. This view was expressed by all the banks and numerous members of the private sector. Indeed, it is hard to understand the project's bias against the use of MTCF funds to finance working capital needs. Working capital is the lifeblood of any business organization, and the lack of sufficient working capital will doom to failure any project, regardless of its impressiveness. The team feels that there is no general rule to determine appropriate levels of working capital. Each sub-project will be different and have different needs.

Working capital is needed by start-ups and by going concerns. This evaluation team learned that a large number of DDC projects are having severe difficulty reaching their planned goals. The many reasons for this have been elucidated above. The correction of these problems will require additional loans for working capital, especially to those borrowers who have suffered due to forces beyond their control.

In the context of Bolivia's current economic circumstances, it is clear that there are many existing industries that are working at fractions of capacity. This is due particularly to the extreme volatility of economic policy over the past years. The damage to the country's savings, including industry's working capital, by "de-dollarization", 23,000% inflation, followed by a severe economic contradiction including a credit squeeze, has been enormous. The ability of industries to regain higher levels of productive capacity and sales will depend, in large part, on access to working capital credit to build inventories and to mount marketing efforts and sales campaigns. Those agencies concerned with the immediate reactivation of Bolivia's private sector should address this potential and there are many precedents in external agency support for economic stabilization programs in Latin America.

2. <u>Institutional Framework</u>

The institutional framework established to implement the MTCF project needs to be altered. The roles of the UCP, UCFs, ICIs, USAID/Bolivia and the U.S. technical assistance team need to be realigned.

a. UCP

The role of the UCP should be the following: 1) verify the qualification of sub-project loans; 2) administer the pilot "Market Town" project; 3) channel technical assistance to the banks to improve their capacity to evaluate and supervise sub-project loans; and 4) make agreements with participating banks to improve the quality and quantity of resources devoted to project evaluation and supervision.

The UCP should delegate directly to the ICIs the responsibility for project analysis and evaluation and for credit judgement. The UCP should not make an independent evaluation of sub-projects, but should limit its role to certifying that a sub-project fits the criteria of the program. The UCP should guarantee to the ICIs quick and efficient decisions.

In its role as provider of technical assistance, the UCP should direct sufficient technical assistance resources to assure that the ICIs develop the required quantity and quality of personnel to make credit judgments and to properly supervise ongoing projects. The UCP should assure, through post audit of the projects, that the ICIs are performing these functions in an effective manner.

The implementation of these recommendations would significantly alter current responsibilities. It would put the responsibility for the project decision where it belongs, with the banks. In so doing, it would build and strengthen Bolivia's banking system, the benefits of which will continue on into the future.

With respect to the UCFs, the UCP should provide technical assistance in investment promotion. The UCFs should also be assisted whenever one of them is chosen to participate in the pilot project of a Market Town development scheme.

b. UCFs/UPIs

The UCFs should become UPIs, Unidades de Promoción de Inversiones, or Investment Promotion Units. They should receive technical assistance and training to build up their strengths in this area. In addition, the UCFs should be removed from the credit process. The two functions -- investment promotion and project evaluation/credit approval should be separated to prevent the bias of enthusiasm for theories from clouding objective judgement concerning project feasibility and credit worthiness.

The evaluation team's review of past experience suggests that the best work done by the UCFs has been the investment promotion of their regions. Indeed, their close connections with their sponsors, the DDCs, have led most of them to act as promoters for investment ideas and schemes favored by the DDCs. If some of these schemes have proven less than successful to date, this does not challenge the validity of their basic work. In may cases, the source of the problem was the fact that the promoter of the scheme became involved also in the subsequent project evaluation and even in the ultimate credit judgement.

This evaluation recommends that the UCFs be reintegrated more intimately with their sponsoring DDCs in a new role as investment promoters for their regions. These new entities "Investment Promotion Units" should consist of three persons rather than the four to five which the system currently averages. They would promote the comparative advantages and opportunities of their departments by contacting investors and encouraging them to locate or invest there.

These investment promotion units would benefit also from close relationships with the private enterprise associations. Many UCFs already enjoy a close private sector relationship since the composition of their boards of directors has private representation. Strong participation by regional private sectors will add credibility to investment promotion and will provide an excellent channel for the private sector to make its views known in an effective way.

Finally, the team recommends that the UCF be removed from the credit process and not issue certificates of eligibility. The immediate effects of this measure will be to remove a bureaucratic layer, simplify judgement, and provide efficient and timely service to the ICIs.

c. ICIs

The ICIs should evaluate and approve sub-project loans. The only exception might be for individual loans in excess of $500,000, which would involve USAID/Bolivia's participation in the decision-making process.

The ICIs should take steps to improve their project lending capabilities and should add new departments for project follow-up and work-out. These departments would supervise sub-project loans and assure a much lower rate of sub-project failure.

In order to accomplish this, the ICIs -- along with sub-projects -- should be the primary recipients of technical assistance channeled through the UCP. Strengthening the capacities of the private commercial banks will be a far more permanent institutional development achievement than would be the continued support to UCFs to handle tasks the banks should be doing in the first place.

This team further recommends that the UCP qualify those ICIs which are interested and able to invest in and dedicate good human resources to the evaluation of projects, and the supervision and follow up of the portfolio. Those banks which are willing to improve their capabilities in a tangible way could be given incentives. For example, in the form of a temporary increase in interest spread, and a reduction in approval procedures (i.e., a blanket approval of an amount, say $1 million to be used for qualified projects without prior approval, but subject to post audit). For those few institutions that would today qualify as excellent institutions, (the Banco Industrial S.A., for example), the program would be well advised to offer general lines of authority to commit without prior approval by the UCP.

This new and closer relationship with the ICIs should be formalized by agreements which not only define each party's obligation to the other, but also reiterate the bank's responsibility for credit judgments, as well as their obligations to repay the program, regardless of a subsequent outcomes. Some authority, with appropriate limitations, should be conceded to reprogram loans when necessity dictates.

Over the longer term, Bolivia needs a richer and more complex environment of financial institutions. Those required include venture capital sources, equity capital sources, bond financing, etc.. In the short term, however and until confidence in economic stability is established, these measures seem premature. Strengthening the existing system, while exploring future options, is the most appropriate short-term course of action.

d. USAID/Bolivia

USAID/Bolivia should remain outside the credit approval process. If the Mission decides that its participation is necessary to ensure consistency and compliance with policy, then the team recommends that a separate approval step (i.e., USAID approval) be confined to projects over $500,000, as is currently the case.

e. U.S. Technical Assistance

The current contract with Development Associates Inc. should be revised to conform with these design changes. Specifically, the contract should now emphasize training ICI and Investment Promotion Units staffs and providing technical assistance to the sub-projects (including the DDC projects that are foundering).

3. Financial Intermediation

The financial intermediation system established in the MTCF project must be redesigned. It must address both original design shortcomings and the problems that have appeared in practice. Some of the major shortcomings and problems to be addressed are:

- A costly, bureaucratic, structure and image;
- Financial dependence on USAID of UCP/UCF structure;
- Competition from other lines of credit;
- A weak institutional framework;
- Slow bureaucratic procedures for loan processing;
- Slow disbursement rate;
- Lack of technical capacity in ICIs for credit evaluation and supervision as well as medium term credit experience;
- Excessive guarantee requirements that keep away an important number of entrepreneurs; and
- Unrealistic geographical limitations.

This section on financial intermediation will address these constraints in terms of both short and long-term recommendations. Short-term actions -- to be implemented between now and the end of the project -- are aimed to correct problems and exact overdue results. An array of longer-term options is presented and further study of their applicability and viability is recommended. A combination of these short and long-term measures will serve to institutionalize the objectives of the MTCF project.

a. Short-term Actions

Short term financial intermediation actions are recommended to improve the existing system. They include: 1) streamlining the UCP/UCF structure and procedures; 2) accelerating the commitment and disbursement of funds, and 3) strengthening the existing ICI structure. Details of each of these recommendations will be discussed in turn.

1) Streamline the UCP/UCF Structure and Procedures

Reduce the UCP's functions to an ex-post supervisory function.

Limit the UCF's project approval functions to verifying the eligibility to, and compliance with, project requirements.

Simplify loan requirements, particularly for loans under U.S.$25,000.

2) Accelerate Commitment and Disbursement of Funds

Increase availability of working capital financing, to at least 30% of new projects, and for existing operations which demonstrate an increase in activity and employment.

Eliminate current geographical restrictions and manage the regional balance of loans through periodically established targets.

Increase the size of the rotating fund and simplify disbursement procedures, to be verified by ex-post analysis, also penalizing misuse.

Carry out a marketing effort with banks and users.

Implement the UCF central credit fund with DDC loan reflows in order to accelerate placement of those funds.

3) Strengthen the Existing ICI Structure

Increase the number of credit worthy ICIs, in particular those with "outreach capacity".

Strengthen ICI capacity for credit analysis, evaluation and follow-up through the provision of technical assistance and, possibly, a larger spread to finance new and enhanced technical departments. To ensure more effectiveness, this effort could be concentrated in three or four of the more active users of MTCF funds.

Improve evaluation of ICI credit worthiness and establish limits for each.

b. Long-Term Alternatives

The following long-term financial alternatives are proposed to improve the intermediation structure, achieve financial self-sufficiency and create a more stable long-term institutional structure for the MTCF project.

One of the crucial aspects to bear in mind over the longer term is the current presence of conflicting goals. For example is it possible to achieve financial self sufficiency while at the same time maintaining geographic restrictions that limit capacity to disburse funds? It is possible to get banks to lend in impoverished rural areas, while maintaining the same guarantee requirements? The answers most likely, are no, and this evaluation recommends that project goals be broadened to encompass more generally defined objectives, such as support of the GOB's reactivation plan and of private sector development.

Just as a redefinition of goals will determine the project's future path, a restructuring of the system will determine how one moves down the path. The longer-term view mandates a change in the existing UCP/UCF structure, which is costly and may not be necessary in a redesigned project. Here again, economic goals conflict with social and political goals; the UCFs have achieved a decentralization goal and created an awareness among DDCs of the need for private sector development, but they are too costly for a private financial venture to support. Furthermore, there is also the question of DDC control over UCFs at the local level; will the DDCs allow their independence or permit major changes?

The financial intermediation alternatives described below aim to achieve the project goals stated at the beginning of this chapter.

Long-term options include continuing and improving the present financial intermediation structure; transferring the project to the Central Bank; strengthening ICI intermediation and reorienting UCF activities and creating a new financial vehicle. Such a financial vehicle could be a second story bank, regional financieras, an existing bank, a guaranty fund or a venture capital fund. A discussion of each, as well as advantages and disadvantages, follows.

1) Continue and Improve Present Financial Intermediation Structure

This alternative entails implementing some of the measures detailed as short-term actions to rationalize the UCP/UCF structure.

Advantages: Can obtain immediate short-term results, particularly for accelerating loan approval and disbursements, as well as improving ICI technical capacity to evaluate and supervise credits. Would move the project faster toward financial self-sufficiency.

Disadvantages: Does not define or strengthen the institutional structure, and maintains a potentially dangerous UCF/DDC direct relationship.

2) Transfer Project to Central Bank to be Repassed Like Other Foreign Loans

This is an extreme alternative, but it would allow for more rapid processing and disbursing as well as the reduction of a great deal of project overhead. It would entail the elimination of a number of existing restrictions.

Advantages: Would accelerate loan approval and disbursements, more in line with the GOB's objectives of economic reactivation.

Disadvantages: The loan could lose some of its decentralization characteristics and "social objectives". It could also "get lost" among a multitude of lines of credit in the Central Bank.

3) Expand and Strengthen Present ICI Intermediation Structure, and Limit or Reorient UCF Activities

This alternative would entail a number of options, or a combination of them. They include:

Include other financial institutions in the project to perform an intermediary role. These could be, for example, Banco Agrícola, Banco Minero or other state entities that have "outreach capacity". This effort would involve technical assistance and the creation of mechanisms to ensure repayment of funds to project.

Utilize CACEN and the savings and loan system, as ICIs, particularly in secondary areas. Assist them in the creation of development departments.

Include more cooperatives, credit unions (FENACRE, etc.) as ICIs also providing them with the necessary training and technical assistance.

Reorient UCF activities by reducing their presence in the major urban areas (where their responsibilities would be handled by the ICIs), and concentrating their investment promotion and technical assistance activities in secondary areas, where ICI outreach capacity is limited.

<u>Advantages</u>: Expansion of the ICI network by the inclusion of other financial institutions in the system would allow greater "outreach capacity" to place loans in secondary areas where the commercial banking system cannot or does not want to go. Moreover, increased UCP/UCF activity and technical assistance in the less developed departments and secondary areas will facilitate investment promotion and project preparation and implementation.

<u>Disadvantages</u>: The quality of the loan portfolio could suffer from poor credit evaluation as well as from the low credit worthiness of the ICIs. Supervision of projects could become more complex and costly.

4) Creation of New Financial Vehicles to Assist in Achievement of Project Objectives and Consolidate Institutional Framework

The idea of creating one or more financial institutions based on the UCF/UCP structure has always been a possible long-term outcome of the DDC and MTCF projects. It would also serve to institutionalize the more valid and useful parts of the existing structure.

The decision to create a new financial institution, however, cannot be based on the existence of a portfolio made up of DDC/MTCF loans and a 40 year USAID loan, nor can it be based on the existing UCP/UCF structure which is costly, bureaucratic and lacks businesslike management. The viability of the new institution must be analyzed on its own merits, market conditions, the overall evaluation of the financial sector, and the GOB's policies toward the development of new financial mechanism and institutions.

Another factor to be considered is the downtime required to establish new financial institutions. This process includes conducting the feasibility study, finding investors, organizing management, setting up infrastructure, and obtaining the necessary government approvals. An optimistic estimate of this time frame is about 18 months, which means that during that period the existing structure should be streamlined and improved.

Finally the objectives for setting up a new financial institution(s), must be clearly defined and should also be consistent with the DDC and MTCF project objectives. Some of these possible objectives could be:

Achieve financial self-sufficiency for the MTCF project;

Create a profitable venture that will improve development credit intermediation;

Institutionalize in a more definitive way, the existing UCP/UCF structure;

Create an institution that will channel funds to secondary areas, now not being adequately attended, and involving the DDCs in this effort;

Develop new financing techniques such as leasing and project financing, and enhancing the local financial system; and

Participate with equity in viable projects where the entrepreneurs do not have sufficient capital.

The alternatives for new financial vehicles, which need not be exclusive of each other, could be a) second story bank; b) regional financieras; c) an existing bank;

d) a guaranty fund; and e) establish a venture capital fund. The advantages and disadvantages of these option are presented below.

a) A Second Story Bank

A second story bank would act as intermediary for MTCF project loans as well as other sources of funds, and could eventually undertake certain "first floor" financiera activities.

This institution would act on a nation-wide basis, absorbing part of the existing UCP/UCF structure, adding on whatever expertise is necessary.

The ownership of the bank would be preferably private, otherwise the DDCs could be allowed to have 40% of shares. The bank would be expected to operate in a professional and businesslike fashion. To maintain a regional focus the bank could be headquartered in Cochabamba.

Advantages: The bank would be a vehicle to institutionalize the existing UCP/UCF structure, and at the same time, allow for a more rapid generation of revenue to ensure financial self-sufficiency. The bank would also possibly be able to implement better evaluating and disbursement mechanisms, as well as orient funds on a more regional basis. The bank could eventually enhance the financial system by creating a new mechanism as well as competition.

Disadvantages: The creation of another financial institution would take place in an unsettled money market, still less than half the size it was in 1980, and with a number of existing institutions in financial trouble.

There could be possible difficulties in intermediating other lines due to the spread structure and competition from Central Bank channeled lines. In addition, there could be difficulties in mobilizing domestic resources. Also, such a bank could be burdened with a narrow charter, impeding it from providing a full range of services and maintaining a balanced portfolio. Finally, there is the possibility of creating a costly, bureaucratic institution which can also become politicized if there is too much DDC intervention.

b) Regional Financieras

This plan would involve the creation of one or two regional financieras, in Cochabamba and Sucre for example, where the UCFs are strongest and in Santa Cruz, and La Paz by strengthening FINDESA and utilizing BISA.

These financieras could operate nation-wide, but would have a regional focus, as follows:

FINDESA -	Santa Cruz, Beni
COCHABAMBA -	Cochabamba,
SUCRE/FONDESA -	Chuquisaca, Tarija, Potosi
BISA -	Oruro, La Paz, Pando

The DDCs could participate as minority shareholders in most of these financieras which would deal directly with the public, and obtain their funding from the MTCF project and other sources. Special emphasis would be made on loans to secondary areas, where they could be given an additional spread as incentive.

<u>Advantages</u>: The financieras would strengthen regional financial capacity. Local or regional projects or initiatives would also have more access to financing.

<u>Disadvantages</u>: Lack of adequate management at the local level, and lack of capital and investors would be the main drawbacks. Increased operating costs due to redundant staffing (as compared to a large central financiera), and in some cases limited local business for generating enough financing to reach break even could also be problems.

c) Buy Into an Existing Bank or Financiera

This would entail identifying a suitable financial institution for sale, that has the necessary structure and orientation to do development banking, and is not burdened with excessive overhead and high loan-loss ratios.

The type of bank to be purchased would depend on whether the objective is second story banking, first story or retail banking or both. In the first case, possibly a streamlined version of the present UCF structure would be sufficient, and for retail purposes a branch network would be desirable.

The purchase of an existing bank is a complex matter that requires an in-depth analysis of the market, the institutions targeted and its portfolio, the establishment of a price, lining up potential investors, and negotiating with the sellers. Nevertheless, it is a serious option to consider, and would merit an initial survey of existing institutions to determine whether there are any available institutions worth purchasing.

Advantages: This option would provide a shortcut around government red-tape to obtain a license, and, if well organized, could provide a trained staff, and an existing administrative structure and market. It could also provide an on-going stream of earnings that could facilitate the financial self-sufficiency of the project.

Disadvantages: Unforseen difficulties could crop up in its portfolio, as well as in its operating systems and costs. There may also be problems in merging with the UCP/UCF structure (business mentality vs. bureaucratic management). It may be more difficult to line up investors, particularly DDCs, if so desired. Finally, image problems may crop up in the market particularly vis-a-vis other financial institutions if it is to be a second story bank.

d) Establish a Guaranty Fund

The guaranty requirements of the banking system as well as their limited capacity to evaluate projects and have a presence in secondary areas, have definitely been stumbling blocks to increasing loan volumes to small borrowers or to viable projects that lack guarantees. A loan guaranty fund would be a useful instrument not only for the MTCF project, but eventually for others as well.

Some of the general characteristics of the fund could be:

Cover 50% of loans;

Guarantee only small loans (such as those less than US $25,000), and loans to secondary areas;

Add on a percentage to the spread to re-capitalize the fund;

Technical and administrative assistance should be required of borrowers;

The fund could be capitalized by USAID and other donors, the DDCs and private banks; and

The management of the fund would be entrusted to a board of directors, and a guaranty committee made up of board members; the day to day operations and administration would be entrusted to the UCP.

e) Establish of a Venture Capital Fund

The lack of investment or seed capital has kept many viable medium-sized projects from being implemented, both in primary and secondary areas. A venture capital fund can be established within, or in conjunction with a new development financing institution in order to take minority positions in certain ventures whose viability has been evaluated, and which qualify for the goals of the project. The fund could also serve as support for the creation of a capital market, by eventually selling its holdings to shareholders directly or through the future bolsa.

The fund could be capitalized by USAID, private banks, private investors and some DDCs. Its policies and investments would be approved by a board of directors, and the evaluations and administrative aspects handled by the UCP or its succeeding institution. Part of the US $4.2 million earmarked in the MTCF project for "market towns" could be destined to fund the guaranty fund and/or the venture capital fund.

5. Consequences

Implementation of any or a mix of the above alternatives have implications for the existing structure. The creation or purchase of a new financial entity to institutionalize the UCP/UCF structure will call for significant changes in policy, and administrative and economic matters. These questions and consequences are presented below.

Policy

What will be the function of the UCP? Will it be absorbed totally or partially into the new institution? What will be the function of the UCFs in each region? Should they continue to exist in the major cities? Will they become branches and be partially absorbed into the new bank? Who will handle the investment promotion function and how? How will the UCFs be removed from the DDCs?

Administrative

What will be authority and capacity of the UCFs? How will loan approval operate? Which of the existing staff will be required, which will not? How will reporting and control requirements with USAID/Bolivia be handled?

Economic

What part of the UCP/UCF structure costs can or should the new institutions absorb? Who will pay for the investment promotion function, and how? What spread structure will be necessary to absorb UCP/UCF structure into a new financial institution. The following section discusses possible future roles of the UCFs.

6) Reorient the UCFs

The organization of the UCFs will change as does the overall project structure. Possible future roles include maintaining the present structure in all regions, improving UCF structure in secondary areas only, transfering UCFs to a new institution or converting them to SAMs. Each of these options is discussed below.

a) Maintain Present Structure in all Regions

This would include streamlining the UCFs, redefining their functions and in particular, eliminating credit evaluation and the issuance of certificates of eligibility. The basic structure and relations with the DDCs would be maintained.

The advantage of this option is that improvements can be made on the existing operating structure, but the main disadvantage is the non-institutionalization of the structure.

b) Maintain and Improve Present UCF Structure in Secondary Areas Only

The UCFs in the stronger cities of Cochabamba, Santa Cruz and Sucre would be converted into branches of the new bank, or alternatively would be closed. The UCFs in secondary regions would be maintained as presently structured but streamlined, and strengthened with human resources and technical assistance until a sufficient loan portfolio is built up.

The advantage of this option is that it takes a major step towards institutionalization, while it established a calendar for the strengthening and eventual conversion of UCFs in secondary areas until they are financially viable. Cost-wise, it would also benefit the new bank as it will not be able to absorb immediately the secondary UCFs. The major disadvantage is an incomplete institutionalization.

c) Transfer the Entire UCF Structure to the New Institution

This option would imply streamlining and redefining the functions of the UCFs, negotiating the change with the DDC and the immediate assumption by the new institution of all the operating costs of the UCFs. Some of the UCFs in the major areas could become branches or the head office.

The major advantage of this option is that it accelerates the institutionalization of the UCF structure and extracts the UCFs form the influence of DDCs. The major disadvantage would be the immediate absorption of high operating costs by the new institution.

d) Conversion of the UCFs into Sociedades Anonimas Mixtas

This proposed option would convert the existing UCFs into SAMs, where the DDCs would hold 60% of the shares; and the private sector 40%. These new SAMs in addition to having UCFs investment promotion role would eventually be the shareholders of the new financial institution to be created.

The principal disadvantage of this option is that it would institutionalize an existing inadequate structure where DDCs control operations. Furthermore, it would create nine new state-owned enterprises which may evolve in ways quite different to the original conception, and contrary to USAID's privatization policy. Finally, cost-wise it would not achieve any savings, on the contrary a nonremunerative activity, like investment promotion can increase costs, and it is not realistic to expect the private sector to support it indefinitely.

e) Integrate UCFs into other investment promotion efforts (e.g., CAF).

c. Conclusion

The alternatives proposed in the past sections cover a number of options, some of which are complementary, for improving and reorienting the financial intermediation process of the MTCF project.

The recommendations are oriented to achieving the following objectives:

- o Improve loan processing and disbursing;
- o Improve credit evaluation capacity in ICIs;
- o Streamline UCP/UCF structure and procedure;
- o Improve outreach capacity of the MTCF program;
- o Reduce operating costs;
- o Improve the use of technical assistance available;
- o Institutionalize a definitive structure;
- o Attain independence from political structures as DDCs; and
- o Attain financial self-sufficiency.

The above proposals consist of two types of actions, one is oriented to the immediate implementation for the short-term and the other is directed at the long-term.

The main objective of the short-term recommendations is to streamline the UCP/UCF structure and procedures, accelerate commitment and disbursement of funds, and strengthen and increase ICI structure and "outreach" capacity. Simultaneously, the ground work should be laid for longer term options. A study should be initiated to determine the feasibility of improving the development lending roles of private ICIs. The study would explore, among other options, the viability of a second story bank that could eventually do retail financiera activities, the developmentt of guarantee and venture capital funds as complementary activities, and the creation of privately controlled regional financieras in Santa Cruz, Sucre and Cochabamba. Once the feasibility study is done, the start-up period of the new institution should take at least a year, including obtaining the government permit.

The short-term actions could be implemented in a very short period of time provided a task force is created with sufficient technical capacity and authority to carry out the changes needed. This work plan should have specified targets and deadlines.

The second part of the recommendations, especially the feasibility study phase can be carried out by external consultants. Once completed this would be handed over to a "promotor group" who would then find the investors, obtain their permits and establish the initial organization and staffing. The estimated time frame for this phase should be around 18 months.

4. Investment Promotion

Under the MTCF Project, investment promotion has not been carried out in a consistent and organized fashion for a number of reasons. They include the lack of an adequate definition of the activity, its objectives and priorities, the concentration by the UCP and UCFs on administrative activities and the lack of a comprehensive, detailed investment promotion plan.

The only full-fledged investment promotion activity of the project has been the identification and support of three market towns, with results yet to be evaluated.

This section outlines key elements for developing an efficient investment promotion activity in the MTCF project. It then discusses what sorts of activities an investment promotion effort entails. It discusses how this effort should be organized and describes the roles of each of the participating entities. Finally, it presents how investment promotion could be financed and how it should be supported by technical assistance.

a. Definition

Investment promotion under the MTCF project should involve assistance in the development of individual sub-projects, at the regional and local levels. Investment promotion must be carried out by a trained staff and should be <u>targeted</u> to the characteristics and needs of each region and the types of investors. Specific objectives should be established for each region, in accordance to its particular characteristics.

The proposed activities which follow are both general activities applicable to all areas, and specific activities applicable to certain regions.

b. General Investment Promotion Activities:

Policy dialogue with local authorities and private sector institutions;

Support and promote infrastructure development for investment;

Maintain information and databases on possible projects, markets, raw materials, comparative advantages, cost, etc., in the region;

Prepare and distribute information for investment assistance; and

Maintain active investment marketing program.

c. Specific Investment Promotion Activities

Each department should carry out investment promotion activities according to its regional characteristics and the needs of potential investors.

1) In the Primary Cities:

For medium-sized investors:

Project Analysis and preparation assistance;

Preparation of financing package; and

Technical Assistance for project implementation.

For small investors

Project preparation and analysis;

Market Analysis;

Technical Assistance for project implementation;

Preparation of financing package, including guaranty identification;

Find ICI

Administrative assistance (accounting systems, etc.); and

Legal Assistance.

2) In the Secondary Area for All Types of Investors

Fulfill the role of consultants;

Do project preparation and analysis;

Carry out market studies;

Provide technical assistance during project implementation;

Prepare financial package and guarantees; and

Find ICI.

d. Activities to Avoid

The IPU should avoid, among others, the inducement or orientation of investors to pre-conceived projects that are believed "good for the region", and secondly the preparation of lengthy studies for projects which have no entrepreneur to carry them out.

e. Institutional Framework

Investment promotion in the MTCF project has a major role to play to assist small businesses, especially in secondary areas. The organization therefore, must be oriented in that direction.

1) UPIs

The present UCF structure should be relieved of its credit analysis and evaluation functions, and should concentrate solely on investment promotion. The name of the units should be changed from Unidad Crediticia Financiera (UCF) to Unidad de Promoción de Inversiones (UPI). The typical UPI would be made up of a manager, a promoter and a secretary.

To ensure proper orientation and effectiveness, annual plans and targets would have to be developed and evaluated on a quarterly basis.

The UPI would report to an investment promotion officer at UCP level.

In the short-term, a continued relationship with the DDC, including the present board composition is foreseen. Eventually, as financial self-sufficiency is achieved, a more autonomous set up is envisioned, where the UPIs operate on the basis of yearly plans and targets, and a regional board of directors including private and public sector is retained.

2) UCP

The UCP will have a policy role, approve plans, and monitor results. It will also have a key role in the provision of technical assistance.

3) ICIs

Although no direct investment promotion role is foreseen for the financial intermediaries, it is expected that a close relationship be established with the UPIs, particularly for identification and support of projects, especially in secondary areas and for urban small businesses.

4) DDCs

The orientation of the DDCs to the promotion of private sector investment as one of their principal activities has been one of the major achievements of the DDC and MTCF projects. This orientation should be preserved and increased in order to ensure long term regional private sector development. It would not be a wise decision to withdraw the DDCs from the UPIs and the investment promotion activity. The presence of the DDCs on the UPI boards, albeit, in a minority position should be institutionalized, and their stake in private sector development strengthened.

5) The Private Sector

The private sector should be more active in investment promotion activities particularly the regional private sector associations. New private sector associations, in particular small business associations should be incorporated into the UPI boards, where the private sector should eventually have a majority.

Investment promotion is, in essence, a non-profit activity, and the Bolivian private sector cannot realistically be expected to carry a significant portion of the direct costs, but it can provide some complementary support, (not-out-of-pocket expenses) to investment promotion activities.

f. Financing of Investment Promotion

The existing UCF structure costs about US $700,000 per year. At this time it is premature to have a final cost estimate for a new streamlined UCF structure, but a general estimate could be a reduction by 50% which would reduce total yearly costs to about US $350,000.

Assuming the above cost levels, and the application of the 2.4% spread, the break-even point would be around US $15,000 of total loans outstanding, which is expected to be reached by end 1989. Until such time break-even point is reached, the present financing mechanisms, i.e., DDC and USAID support, should be continued.

Assuming a new financial institution is created, the question arises if a business-oriented entity should be expected to finance a non-profit making activity such as investment promotion? The answer is no, unless it can be compensated for those efforts. This would probably mean increasing the spread to accommodate for additional costs.

A transitory scheme could be also established whereby, as UPIs become business promotion branches of the new financial institution, and the costs become absorbed by financiera.

g. Technical Assistance

Investment promotion will be more successful and have greater credibility if it can supply technical assistance both at the policy level and at the project preparation and implementation level.

Technical assistance should be provided through the MTCF project to the UPIs in the following areas:

- Training UPI staff in investment promotion; activities and techniques;
- Training UCP and UPI staff in development of investment promotion plans and strategies;
- Preparing regional development studies to support investment promotion;
- Preparing projects and providing implementation support; and
- Conducting specific studies, e.g., local or international market studies for products.

It is recommended that a larger component of the MTCF project be destined to short term technical assistance for investment promotion. When feasible, part of this technical assistance should be reimbursable.

In sum, technical assistance is one of the more significant inputs that investment promotion can provide and would be the best product that the new UPIs can "sell".

Appendix I

Model Agreement for Trust Fund Creation

SAMPLE AGREEMENTS FOR TRUST FUND CREATION

Conste que por el presente documento que se suscribe en dos ejemplares iguales el contrato que celebran el Banco Central de Reserva del Perú, con domicilio en el Jr. Miró Quesada Nº 445, Lima, debidamente representado por el Presidente y Vice-Presidente del Banco Central de Reserva del Perú, señores Richard Webb y Javier Otero, quienes proceden autorizados según Acuerdo adoptado por su Comité Ejecutivo, en Sesión celebrada el 13 de agosto de 1981; y de la otra parte, la Corporación Financiera de Desarrollo - COFIDE, con domicilio en la Avda. Inca Garcilaso de la Vega Nº 1456, Lima, representada por el Presidente de su Directorio Sr. Ing. Tulio de Andrea, y su Gerente General, Sr. Ing. Ismael Benavides Ferreyros; quienes proceden autorizados según Acuerdos de su Directorio Nos. 170-81 del 07-07-81 y 404-81 del 18-08-81; se acuerda celebrar este convenio, en los términos y bajo las condiciones siguientes :

PRIMERO : De conformidad al contrato de préstamo celebrado el 04 - 04 - 81 entre el Banco Interamericano de Desarrollo (en adelante denominado - BID) y el Banco Central de Reserva del Perú (en adelante denominado BCRP), la primera de éstas entidades ha otorgado a la segunda un préstamo por la suma de treinta millones de dólares de los Estados Unidos de América (US$ 30'000,000.00) para cooperar en la ejecución de un Programa Global de Crédito Multisectorial en adelante denominado el Programa, cuyo monto total es del equivalente de setenta millones de dólares de los Estados Unidos de América (US$ 70'000,000.00) de los cuales el BCRP aporta una contrapartida nacional por el equivalente de cuarenta millones de dólares de los Estados Unidos de América (US$ 40'000,000.00) destinados todos al otorgamiento de crédito a empresas no públicas de los sectores industrial, minero y pesquero a través de instituciones financieras intermediarias del Sistema Bancario del Perú.

SEGUNDO : Por el presente documento y de conformidad con lo establecido

80

unanimidad con fecha 13 de agosto de 1981, el BCRP transfiere en "Comisión de Confianza con Responsabilidad" a la Corporación Financiera de Desarrollo, la totalidad de los recursos del Programa a que se refiere la cláusula que antecede para que sean administrados por COFIDE en base a las condiciones previstas en el contrato celebrado entre el BID con el BCRP, y su Reglamento de Crédito correspondiente.

TERCERO : Por Acuerdos del Directorio de COFIDE Nos. 170-81 del 07-07-81 y 404-81 del 18-08-81, ésta acepta la transferencia de los recursos del Programa en los términos a que se ha hecho referencia en las cláusulas que anteceden y en consecuencia, será COFIDE quien asuma la responsabilidad por la adecuada administración de los mismos, debiendo velar celosamente por que se cumplan las disposiciones contractuales y el reglamento correspondiente del Programa.

CUARTO : Dentro de la estructura orgánica de COFIDE, la ejecución del Programa será realizada a través de la División de Fondos e Intermediación, unidad a la cual ha sido transferido el personal que se encontraba adscrito a la Oficina de Fideicomisos del BCRP que se detalla en el Anexo "A" sin variar su relación de dependencia con este último Organismo. COFIDE se reserva la facultad de dar conformidad a cualquier movimiento de este personal que así lo requiera el BCRP.

QUINTO : La totalidad de los gastos directos e indirectos en que incurra COFIDE para la adecuada administración del Programa serán cargados al Programa".

SEXTO : A efectos de lo expresado en la cláusula Cuarta, COFIDE se obliga a prestar todas las facilidades necesarias para que el personal transferido por el BCRP pueda coordinar su acción con el personal que COFIDE designe o participe en la administración del Programa, así como para que pueda desarrollar sus actividades de trabajo en las mejores condiciones posibles.

la deuda del BCRP al BID, serán utilizados por COFIDE en operaciones de crédito con los mismos objetivos del Programa.

OCTAVO : El plazo por el cual el BCRP transfiere a COFIDE la ejecución del Programa bajo la figura de "Comisión de Confianza con Responsabilidad" será el mismo previsto contractualmente entre el BCRP y el BID para su ejecución. Al vencimiento del plazo indicado, COFIDE devolverá al BCRP los importes disponibles del Programa y mantendrá a su cargo y bajo su responsabilidad la cobranza de los créditos otorgados, así como sus intereses, comisiones y gastos, para los efectos de la devolución antes indicada, así como los muebles y enseres de propiedad del BCRP.

NOVENO : COFIDE se obliga a integrar dentro de su sistema de contabilidad general el movimiento de las cuentas correspondientes al Programa que sean operadas por su División de Fondos e Intermediación para el manejo del mismo. Esta integración deberá hacerla COFIDE de manera que permita un adecuado control financiero - contable del sistema de contabilidad que opere la referida División. COFIDE elaborará trimestralmente un balance de dichas cuentas el cual una vez aprobado por el Comité de Crédito y Finanzas de COFIDE, será remitido al BCRP.

DECIMO : COFIDE se obliga a presentar anualmente al BCRP y al BID los estados financieros del Programa, debidamente auditados, para lo cual habrá de utilizar los servicios de los mismos contadores públicos, independientes que hayan sido seleccionados por la Contraloría General de la República para auditar sus propios estados financieros. Los costos de la auditoría del Programa serán cubiertos por COFIDE con cargo al Programa, previa conformidad del BCRP.

DECIMO PRIMERO : El presente contrato podrá ser rescindido total o parcialmente por las siguientes causales :

92

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Suscrito el presente documento en dos ejemplares iguales, en la ciudad de Lima, a los 31 días del mes de agosto de 1981.

BANCO CENTRAL DE RESERVA DEL PERU

Javier Otero G.
Vice-Presidente

Richard Webb D.
Presidente

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83

Appendix II

List of Persons Interviewed

PERSONS INTERVIEWED IN BOLIVIA

Cochabamba

Mario Aguirre Saucedo	Manager, Banco de Santa Cruz de la Sierra, Cochabamba
José Candia Ayllon	Cámara Departamental de Industria de Cochabamba
Javier Cortés Baptista	Manager, Banco de Cochabamba, Cochabamba
Juan Gamarra Ibero	President, Cámara Departamental de Industria de Cochamba
Gonzalo Guzmán S.	Manager, Unidad Crediticia y Financiera, UCF, Cochabamba
Eduardo La Fuente Roca	Manager, Cámara Departamental de Industria, Cochabamba
Omar Medrano D.	Manager, Banco Boliviano Americano, Cochabamba and President, ASOBIN, Cochabamba
Juan Carlos Orsini Puente	First Vice President, Federación de Empresarios Privados de Cochabamba
Roberto Peña R.	President, Federación de Empresarios Privados, Cochabamba
José Rivera E.	Executive Secretary, Federación de Empresarios Privados de Cochabamba
René Saavedra A.	Presidente, Corporación de Desarrollo de Cochabamba (CORDECO)

La Paz

Mario Aguilar	Banco Nacional de Bolivia
José Arias	Manager, Banco Boliviano Americano, La Paz
Enrique Blanco	Banco Hipotecario Nacional, La Paz
David Blanco Z.	President, Asociación de Bancos e Instituciones Financieras, ASOBIN and Executive President, Banco Hipotecario Nacional, La Paz
T. Dwight Bunce	Senior Associate, Development Associates, MTCF Project, Inc., La Paz
Peter Fraser	Development Associates, Inc. MTCF Project, La Paz
Ernesto García	USAID/Bolivia
Rodolfo García	Banco Boliviano Americano, La Paz

Leonora Hamilton-Mann	Development Associates, Inc., MTCF Project, La Paz
Miguel Hoyos	USAID/Bolivia, MTCF Project Coordinator
Rafael Indabura	USAID/Bolivia, MTCF
David Jessee	USAID/Bolivia, Project Manager
Reynaldo Marconi Ojeda	Chief, FOCAS/MTCF Project, La Paz
Gaston Martinic Reyes	Director, Coordination Unit MPC/USAID/B, La Paz
Alfredo Moscoso Velarde	General Manager, Banco Industrial S. A., La Paz
Reese Moyers	Head, Private Sector Office, USAID/Bolivia
Raúl Quintana	MTCF Project
Ronald Paz	PL-480 Secretariat
Victor Rojas	MTCF Project
Ramón Rosales	Banco Central, La Paz
Manuel Salsa	Development Associates Banking Study Team Member
Edgardo Sanjines	Manager, Unidad Crediticia Financiera, UCF, La Paz
Dino Siervo	USAID/Bolivia
Davis Vargas	Banco de La Paz, La Paz
Gustavo Vega	USAID/Bolivia
Guillermo Vivado	Development Associates Banking Study Team Member
Ken Weis	Development Associates, Inc., MTCF Project, La Paz

<u>Oruro</u>

Lucio Arce	Cámara Agropecuaria, Oruro
Héctor Bustillos	Manager, Banco Boliviano Americano, Oruro
José Calderón	Manager, Unidadd Crediticia Financiera, UCF, Oruro
Sr. Navarro	Cámara Agropecuaria, Oruro
Wilson Sandy	Manager, Banco Boliviano Americano, Oruro

86

Santa Cruz

Jorge Adriázola	Finance Department, FINDESA, Santa Cruz
Juan Carlos Alvarez F.	Clerk, Banco de Santa Cruz de la Sierra Santa Cruz
Juan Carlos Chávez	Regional Manager, Banco de La Unión, Santa Cruz
Juan Javier Estenssoro	Assistant Manager for Development, Banco Hipotecario Nacional, Santa Cruz
Jaime Fajerstain Malicka	Assistant Manager, Banco de la Unión, S.A. Santa Cruz
Mario Franco Teixeira	Regional Manager, Banco Hipotecario Nacional, Santa Cruz
Juan Gálvez Pardo	Unit Chief, Corporación Regional de Desarrollo and CORDECRUZ, Santa Cruz
Eduardo Lea Plaza	Clerk, Banco Hipotecario Nacional, Santa Cruz
Luis Hernán López Vaca D.	Assistant Manager, Banco de Santa Cruz de la Sierra, Santa Cruz
Walter Núñez Rodríguez	Planning Manager, Cámara Agropecuaria del Oriente, CAO, Santa Cruz
Karin Steinback L.	General Manager, Unidad Crediticia Financiera, UCF, Santa Cruz
Edmundo Soruco Núñez	Clerk, Banco de la Unión, S.A., Santa Cruz
Justo Yepez K.	General Manager, Cámara de Industria y Comercio, Santa Cruz
Carlos A. Vaca Diez Bowles	General Manager, FINDESA, Santa Cruz

Sucre

José Luis Aguirre	Manager, Unidad Crediticia Financiera, UCF, Sucre
Mirko Gardilcic	Head of Technical Analysis, Unidad Crediticia Financiera, UCF, Sucre
Antonio Landivar G.	General Manager, Cámara Departamental de Industria, Sucre
Alvaro López	Head of Operations, Unidad Crediticia Financiera,, UCF, Sucre
Saúl R. León Ortuño	Manager, Banco de Santa Cruz de la Sierra, Sucre
Pablo Mier Garron	President, Federación de Empresarios Privados de Chuquisaca, Sucre

Gustavo Mirabal Alvarado	General Manager, Compañía Boliviana de Alimentos, COBOLDE, Sucre
Angel Ramos Diez de Medina	Regional Manager, Banco de Cochabamba, Sucre
Marcelo Santa Cruz U.	Commercial Manager, Ferreteria Santa Cruz, Sucre
Marcelo Vargas Vacaflor	Presidente, Corporación Regional de Desarrollo de Chuquisaca (CORDECH), Sucre
<u>Washington, D. C.</u>	
Thomas Morris	Senior Program Officer, Development Associates, Inc. Arlington, VA
Leveo Sánchez	Chairman, Development Associates, Inc., Arlington, VA

Appendix III

List of Projects Visited

Projects Visited

Project	Funding	Description
Cochabamba		
Flower Project	MTCF	Roses
Saaflor	DDC	Roses
Artesanias de Cusroy Lane	DDC	Leather and Wool
Asociacion de Tiguipaya (ASARTI)	MTCF	Wool Sweaters
Avicola Fernandez	MTCF	Chicken Farm
Santa Cruz		
Silos Pailon-Anapo	MTCF	Grain Silos
Chocolates Princesa	DDC	Chocolate Factory
La Paz		
Angora Rabbits (Landivar)	DDC	Rabbit Breeding
Inestano	DDC	Pewter
	MTCF	Farm
	MTCF	Paint Factory
Sucre		
COBOLDE	DDC	Ham & Sausage Factory
IPAC	CORDECH	Corn Snacks Factor
Yeseria MILLUNI	MTCF	Plaster Factory
PACH	DDC	Ham & Sausage Factory
Oruro		
Laminor	MTCF	Steel Mill
Granja Imperial	DDC	Farm

90

Appendix IV

Scope of Work

.91

PART I - SECTION C - WORK STATEMENT

INTRODUCTION

This evaluation concerns two related projects (A) Rural Development Planning/Departmental Development Corporations and (B) Market Town Capital Formation. Separate reports will be submitted for each of the two projects.

I. BACKGROUND

A) Rural Development Planning (RDP)/Departmental Development Corporations (DDCs) Project

The purposes of this combined grant-loan Project were (a) to improve the technical competency and rural focus of the Bolivian planning system, including project implementation, managed by the Departmental Development Corporations (DDCs) under Ministry of Planning and Coordination (MPC) guidance and (b) to improve the capability of the DDCs to promote, design and carry out productive rural development projects, especially in cooperation with the private sector.

Grant funds were used to finance (a) long and short-term technical assistance advisors in various aspects of planning and project development for the participating DDCs and the MPC, (b) in-country training courses and workshops and (c) materials, office equipment and vehicles. The Project loan primarily financed subprojects undertaken by the private sector.

The project reached its PACD on March 31, 1987. Preliminary findings indicate that the Project has attained the following:

1) Improved methodologies for regional planning and project management were designed and implemented by the DDCs, thus improving their technical capabilities in planning and project implementation.

2) Eight Investment Promotion Units (IPUs, actually named Unidades Crediticias Financieras) were established within the DDCs, which helped to promote, design, monitor and carry out private sector productive projects at the departmental level. These units participate in the implementation of the follow-on Market Town Capital Formation (MTCF) Project.

3) The well-being of people in rural and semi-urban areas has been improved by creating jobs, generating foreign exchange and increasing productivity and production.

A progress evaluation was carried out by Development Alternatives Inc. in August of 1985.

qv

The experience of the Project has been documented in a video presentation, comprehensive reports and well organized Project files. This documentation is being used as reference material in the implementation of the MTCF Project, and is available to the Consultant.

B) Market Town Capital Formation (MTCF) Project

This project was designed as a follow-on to the RDP/DDCs Project, and was developed in order to (a) to increase the level of productive private sector investment in Bolivia's rural and semi-urban areas (b) improve the capability of the Intermediate Credit Institutions (ICIs) and Investment Promotion Units (IPUs) to perform more effectively, and (c) establish a credit fund which will be used to finance projects through the IPUs and ICIs.

Grant funds finance (a) the contract with a United States firm which provides long-term and short-term technical assistance in the areas of investment promotion, small enterprise development and marketing, (b) training, in-country workshops/seminars and orientation/observations trips to Latin America and the United States, (c) Project support costs of the Project Coordination Unit (PCU), commodities, investment research and a Project Coordinator and d) evaluations and audits. The loan component of the Project finances eligible investments undertaken by the private sector.

As of April 31, 1988, the project has achieved the following results:

- Twenty nine subprojects, for a total financing of US$4.7 million, have been approved in eight departments.

- The long-term technical assistance has initiated its activities in the areas of investment promotion, small enterprise development and marketing.

- A series of guidelines were published for selecting, evaluating and monitoring agroindustrial, industrial and artisanry subprojects.

- Priority market towns were selected in Chuquisaca and Potosí.

- Two marketing studies are being carried out through the external TA.

- A series of seminars were carried out for IPU, ICI and private sector technical staff on identification, design and evaluation of subprojects and marketing.

Two years into the Project, there are a number of issues which must be analyzed. Most of these issues have arisen due to implementation experience and changed circumstances since the preparation of the Project Paper. These issues are briefly defined in Article III, their analysis and development of alternative courses of action to solve them constitute the Scope of Work.

II. CONTRACT SCOPE OF WORK

1. Contract Objectives

- To carry out a final evaluation of the RDP/DDCs Project in order to determine the extent to which the purposes were achieved, and to determine lessons learned from the Project.

- To carry out a mid-term evaluation of the MTCF Project to review the original project design, to consider certain fundamental issues which may affect the eventual success of the Project, and to measure progress toward attainment of the stated purpose of the Project.

2. Statement of Work

A) The final evaluation for the RDP/DDC Project will determine the following:

1) Socio-economic impact of subprojects on clients.

2) Institutional impact of Project on ICIs, UCFs, DDCs, and USAID/Bolivia.

3) Extent to which the Project purpose was achieved.

4) Status of the DDC loan portfolio.

5) Lesson learned.

B) The mid-term evaluation of the MTCF Project shall evaluate a number issues detailed below. For each issue, the evaluation shall further define the issue, propose and evaluate alternative strategies for resolving the issues, recommend a preferred strategy, and recommend actions to implement the preferred strategy. The issues are as follows.

1) Definition of the Purpose of the Project.

The statement of the Project Purpose presented in the Project Paper deserves review based on the implementation experience to date. The following are statements of three elements of the Project Purpose found in the Project Paper:

- Promote private sector equity mobilization (page 31),

94

- Promote private sector investment in rural and semi-urban areas (page 14), and

- Promote private sector investment in agribusiness (page 76).

The contractor is to restate the Project Purpose based on the various elements found in the Project Paper and review whether the statement is still adequate. Several specific issues are to be addressed as part of this task:

- What should the Project be doing to assure that the quantity, quality, and variety of equity capital being invested in sponsored projects is maximized?

- What is the nature of the economic linkages between urban areas and rural areas and urban areas and agriculture? When does an urban-based investment have a significant beneficial impact on a rural area?

- Businesses which contemplate locating outside the "eje central" frequently face serious disadvantages in terms of intrastructure, amenities, business contacts, and access to markets. This Project can provide only minor incentives to investors to locate outside the "eje central." Does the success of the Project depend on stronger incentives? Or should the Project respect market forces and accomodate firms which locate in urban areas?

- In order for the UCP/UCFs/ICIs system to become self-financing, what volume of lending is required?. If the system cannot acheive that volume based on lending outside the "eje central," the system may not survive. Should a case be made for some urban lending to increase volumes and assure survival of the system? Why?

2) Logic and Organization of Investment Promotion.

The rationale or methodology of investment promotion deserve review since investment promotion is the key activity in this Project. The question, for example, of which aspects of investment promotion are a public responsibility, which can be carried out for a profit, and which should be paid for by the investor has not yet been dealt with. The contractor is asked to develop a coherent conceptual framework for the investment promotion activity, and in the process address two specific issues:

- There may be private sector alternatives to the UCFs (e.g Industrial Chambers of Commerce, private consulting companies, a UCF with private sector stockholders, or a unit owned jointly by banks operating in a particular area). Are there strong reasons for seeking out alternatives and what alternatives might be most feasible?

- What investment promotion services are demanded by the client, by the bank, by private sector associations, by the local government?

3) Incentives and Disincentives for Financial Intermediation.

When the Project was initiated, local private banks were anxious to participate because access to cheap credit was very limited and loan portfolios of the banks were relatively sound, although they were small. Also, faced with high operating costs and low volumes of business, the banks were attracted by the prospect of new business. The banks now, however, have easy access to substantial IDB funds, but are also faced with serious repayment problems with their loan portfolios. They are becoming quite conservative. The contractor shall explore the existing incentives and disincentives to bank participation in the Project and shall make recommendations for improving the incentives (and decreasing the disincentives). A timetable with performance benchmarks for the banks will be established to monitor implementation of the recommendations and the response of the banks.

The guarantees that the private banks presently require of borrowers substantially reduce the potential clientel of the Project. These guarantees may, in fact, be one of the most serious obstacles facing the Project. The contractor shall also evaluate the situation of guarantees required by banks and recommend solutions.

4) Performance of the UCP/UCFs/ICIs System.

The contractor shall review the operation of the overall system (which includes USAID/Bolivia, the Ministry of Planning and Coordination Subsecretary for International Cooperation, the Ministry of Finance Project Coordination and Control Unit, the Project Coordinatin Unit, the PL 480 Secretariate, the Departmental Development Corporations, the UCFs, and the ICIs) and make recommendations for simplification, if possible, and improvements in operations.

The contractor shall also look specifically at the performance of the Project Coodination Unit and of Development Associates, the firm providing long term technical assistance to the Project. The contractor shall evaluate (and make recommendations for improving) the effectiveness of the Project Coordination Unit in terms of:

- The new organizational scheme, which includes functions, responsibilities, information systems, delegation of authority, decision making levels, operating manuals and guides prepared to ensure compliance with the Project Paper and USAID policies and regulations.

- Planning instruments and procedures such as work plans and the degree of accomplishments.

- The technical assistance provided to the UCFs, ICIs and investors to: 1) prepare annual investment plans, 2) identify, prepare, evaluate and monitor subprojects, 3) support investment promotion in secondary towns and priority market towns, and 4) support institutional strengthening.

- Financial, accounting and administrative management of the Project.

- Nature of relationships with the other participating institutions (UCFs, ICIs, PL-480, UCCP, USAID and Development Associates).

- Financing operations and accomplishments with respect to revised financial projections.

- Professional and technical capacity of the PCU personnel.

The contractor shall evaluate (and make recommendations for improving) the effectiveness of the Development Associates contract team in terms of:

- Design and implementation of methodologies for investment promotion.

- Strengthening of the capabilities of UCFs and PCU personnel in investment promotion activities.

- Training of UCFs, ICIs and private investors on the developing of subproject proposals for small enterprises.

- Identification and implementation of marketing studies.

- Identification and description of mechanisms for attracting private or mixed capital agro-industrial ventures.

- Assessment of factors that affect supply, demand, prices and other factors that impede a smooth implementation of the project.

- Use of short term experts.

- Adequacy of expertise provided by the long-term experts to achieve project goals.

5) Financial Sustainability of the UCP/UCFs/ICIs System

What are the prospects of acheiving financial self-sufficiency of the system before the PACD? If the prospects appear good, the contractor shall establish benchmarks for the acheivement of self-financing and provide any recommendations considered necessary. If, on the other hand, the prospects appear dim, the contractor is asked to provide recommendations for an as complete restructuring of the Project as is necessary to acheive self-financing by the PACD.

The contractor shall also review which aspects of portfolio management theory are relevant to the management of the Project portfolio and the contractor shall make any recommendations necessary in this respect.

6) Other Issues

The contractor, identifying any other issues which might seriously affect the chances for success of the Project, shall define the issues and make recommendations for resolving them.

3. Level of Effort

The contractor shall provide four consultants (three for six weeks and one for four weeks) in the areas of investment promotion, institutional analysis, financial analysis and banking. All consultants must be fluent in Spanish.

4. Reports

The contractor shall submit and make an oral presentation to USAID/Bolivia staff of a draft report covering all items described in the Statement of Work three days before the end of the contracting period. After review by appropriate USAID staff, all substantive comments or recommendations will be incorporated into the final report. A clear and bound final version of the report with 10 copies shall be submitted to Mr. Moyers, Chief, Private Sector Office, USAID/Bolivia within three weeks after departure of the team.

UNITED STATES GOVERNMENT

memorandum

DATE: July 14, 1988

REPLY TO ATTN OF: Reese Moyers, PS

SUBJECT: Scopes of Work for RDP/DDC final evaluation and the MTCF mid-term evaluation to be conducted by ISTI - Contract No. 511-0573-C-00-8245

TO: THE FILES

The following memorandum clarifies requirements to perform the final evaluation of the RDP/DDC Projects and the mid-term evaluation of the MTCF Project to be conducted by ISTI during July and August, 1988.

RDP/DDC

Methodology

The progress of the DDC/RDP projects has been well documented by periodic interim evaluations, as called for in the Project Paper and PIL No. 16. These documents are considered primary sources of information. As such, review of the DDC loan portfolio, as well as the assessments of the projects' socioeconomic and institutional impacts can be evaluated in La Paz through a review of these documents and through local interviews. Travel outside La Paz is not contemplated in order to perform the DDC/RDP evaluation as there is no need for on-site interviews at the Departmental level.

Goals

Because the goals of the project changed over time, the team will evaluate their attainment measured against those stated in PIL No. 16, which supersede those outlined in the Project Paper.

Market Town Capital Formation/FOCAS

This evaluation will cover six principal points which include: 1) the project purpose, 2) investment promotion, 3) financial intermediation, 4) performance of the overall system, 5) financial sustainability, and 6) other issues.

Financial Intermediation

In the third point, "Incentives and Disincentives for Financial Intermediation," the contract scope calls for the contractor to assess the existing organizational and financial system. If the contractor judges that the existing structure does not appear to be feasible, the scope states that the contractor shall develop a plan to establish a new development bank. This memorandum deletes the requirement to "develop a plan to establish a new development bank, incorporating the UCP and the UCFs only if the contractor judges these institutions to be a sound base for a new bank" and substitutes for it the "recommendation of alternatives to the present institutional structure." Nevertheless, it has been agreed by the Mission that the question of "permanent institutional structure" for the project is completely open to examination, and, therefore, these recommendations might include the conceptual framework for establishing a development bank.

Performance of the UCP/UCF/ICI System

Accomplishment of the fourth point, Performance of the UCP/UCF/ICI System, will in large part, result from the assessments carried out of points 2 and 3 (investment promotion and financial intermediation). By evaluating how well or poorly the project is accomplishing its investment promotion and lending goals, by definition, the contractor will be evaluating the overall project design as well as the various project entities. The evaluation will ascertain whether progress, or lack thereof, is due to structural issues, or to the effectiveness of the units themselves or to their personnel. In addition to assessing the overall design, the contractor will examine key institutional and organization elements of the UCFs and the PCU which facilitate or impede project effectiveness. With specific reference to the Project Coordinating Unit, the contractor will assess its overall operation and make recommendations, where necessary. This assessment of the unit will entail a review, rather than an in-depth analysis of the specific points outlined in the scope of work regarding the Project Coordinating Unit.

PS:RMoyers:rca.
CONCURRENCE:

PS:MHoyos 7/14

EXO/P:PKeirnan

ISTI:BFriday