XD-ABC-323-A

ISN 69711

USAID/BOLIVIA

Project 511-0573/T-071

Second Mid Term Evaluation:

Market Town Capital Formation Project

(Phase One and Phase Two)

Prepared by:

Phase I
Jacques Trigo
Edgar Pereira
Eileen Evans

Phase II
Jacques Trigo
Eileen Evans
Oscar Rodriguez
Rodrigo Ortiz
Michelle Coffee

August 1990

MANAGEMENT SYSTEMS INTERNATIONAL

600 Water Street S.W., NBU 7-7
Washington, D.C. 20024

telephone (202) 484-7170
telex: 4990821MANSY fax: (202) 488-0754

ACRONYMS

GOB	Government of Bolivia
ICI	Intermediate Credit Institution
MPC	Ministry of Planning and Coordination
FOCAS	Spanish acronym for Market Town Capital Formation Project
MTCF	English acronym for Market Town Capital Formation Project
UCFs	Financial Credit Units, which act as financial intermediaries between the borrowers and ICIs
UCP	Project Coordination Unit, under the MPC, located in La Paz, which acts as the implementing unit for the FOCAS project
PACD	Project Agreement Completion Date

OUTLINE

K

L

EXECUTIVE SUMMARY

This study covers the mid-term evaluation of the USAID/Bolivia Market Town Capital Formation Project (the "Project", or "FOCAS"), #5110573/T-071, based on data available from July 1986 through June 1990. The Project Agreement completion date (PACD) is July 1991. The evaluation was conducted in two phases from May 10 through August 11, 1990. Phase I is the actual evaluation of the first four years of the Project. It examines Project objectives, and presents findings and conclusions of: the investment financing mechanism, self-sustainability, the institutional framework and socioeconomic impact. Phase I gives recommendations for the last year of the Project. Phase II gives recommendations for creating a permanent institutional structure. Both are presented in this report. A.I.D. contracted with Management Systems International (MSI), which provided a three person team for Phase I: Jacques Trigo (Team Leader), Edgar Pereira (Institutional Specialist), and Eileen Evans (Credit Specialist), and a five person team for Phase II: Jacques Trigo, Eileen Evans, Oscar Rodriguez (Finance Specialist), Rodrigo Ortiz and Michelle Coffee (Investment Promotion Specialists). Interviews were conducted in every Department except Pando, and the evaluation has been handled in the most transparent way possible vis a vis the Bolivian counterparts in the Project, the GOB, USAID, and beneficiaries throughout the country.

Project Background and Objectives

Until recently, Bolivia had not actively promoted agro-industrial investment outside of the principal cities (La Paz, Cochabamba, and Santa Cruz). By not doing so, the country had not been able to take full advantage of the opportunities available for development within the agricultural sector. Failure to invest in secondary commercial centers means that market linkages were not developed between rural producers and processors, or with suppliers of production inputs. The consequences of this failure are less national production than otherwise possible, less employment generation, lower exports of non-traditional products, and slower growth in national income.

Against this background the Project was designed to address the key constraints to more efficient financial markets in secondary towns. The Project's goal was to achieve a higher standard of living, through increased employment and production, in Bolivia's rural and semi-urban areas. The purpose was to increase the level of productive private sector investment, which would fuel production in these regions, create employment and generate economic growth. This would be accomplished by improving the capabilities of the institutions, the Project Coordination Unit (UCP), the Financial Credit Units (UCFs), and the Intermediate Credit Institutions (ICIs). The Project was also suppose to develop UCFs as investment promotion entities, and encourage ICIs to expand their rural and semi-urban loan portfolios.

The inputs for the Project were: US$15 million from USAID/Bolivia, US$6.5 million from PL-480 Title III Program (the Bolivian Government), and US$17.4 million to be carried over from a predecessor USAID project (DDC Project). A permanent, centralized UCF Credit Fund was to be created with US$21.5 million from this Project and US$17.4 million from the DDC Project. However, the DDC Project has a high percentage of past due loans and its transfer to a UCF Credit Fund, or another permanent institutional structure, is uncertain.

There were five to ten priority "market towns" identified in rural and semi-urban areas at the beginning of the Project. However, due to reluctance by the commercial banks to lend in these areas, and lack of adequate infrastructures, only two towns, Riberalta and Camargo, actually benefitted under this Project. This regional limitation caused delays in disbursements, and jeopardized the Project's ability to generate sufficient fee income to sustain itself. As a result, the Project was amended in February 1989 (Amendment No. 6) to include the major cities of Bolivia (including the central axis of La Paz, Santa Cruz and Cochabamba), provided the investments had forward and backward linkages to rural areas. Also, the amendment allowed for working capital loans exclusively.

Findings

The investment finance mechanism has gone through four distinct periods. The first period, from July 1986 until January 1989, was characterized by limited lending to market towns and cities outside the central axis, and a very centralized, slow loan approval process: only US$3.5 million was disbursed. The second period began in February 1989 with the amendment to include La Paz, Cochabamba and Santa Cruz, and working capital loans, when disbursements reached US$17 million. During the second period, decision making was decentralized under the automatic refinancing scheme. The third period was a time of crisis, from October 1989 through January 1990, when a few existing projects, but no new projects were financed. There was uncertainty over the future of the project based on USAID's decision to suspend undisbursed funds (US$7 million), in order to develop a private financial institution (Carana Study). This decision created much controversy with the UCFs and the Bolivian Government, both of which pressured USAID to abandon the private financial institution idea and continue the project. The fourth period began in January 1990, when USAID followed the Bolivian Government's advice. There is still US$3 million which has been set aside pending decisions after this evaluation.

As of June 1990, 303 projects had been financed with US$18.3 million, therefore the last year of the Project will involve relending loans that have been repaid (reflows). Some loans have fallen past due, and rescheduling is being done on a case by case basis. Commercial banks take all of the credit risk, and must repay the UCP immediately after a loan falls past due. Finally, the financing mechanism has not been able to meet the demand, (nor have ICIs lent on their own), as there were 400 viable projects approved by UCFs without financing.

The Project was to achieve financial sustainability based on fees charged by the UCP (1.4% of the total national portfolio) and by the UCFs (2.6% based on portfolio in their regions). The ICIs earn a spread of 5% on the Project's loans. This fee structure created wide disparities in the level of income generated by the UCFs, and generous income levels for the UCP and ICIs. This is due to the size of each UCF portfolios, and also contributions from the Regional Corporations (DDCs) for operating expenses. The UCFs in the less developed regions (Tarija, Beni, Potosi and Oruro), have much smaller portfolios, and insignificant DDC support. All of the UCFs have operating surpluses except Potosi and Oruro, which have been, and will continue to be supported by the UCP for several years.

Can the system sustain itself? The UCFs and UCP believe that by the end of 1990, the UCP should be self-sustaining, but the UCFs will receive enough income to cover only 60% of their operating expenses. This will increase to 80% by June 1991, and by June 1992 the system should be self-supporting. A recent agreement to redistribute 40% of the reflows from the larger, profitable UCFs to the less developed regions, in order to increase the size of their portfolio, will be implemented soon. The accounting and budgeting systems of each UCFs and the UCP are currently being consolidated to satisfy requests by the Superintendent of Banks.

The Project was suppose to <u>improve of the capabilities of the institutions</u> involved in the investment financing system. It has achieved this with the UCP and UCFs, but not the ICIs. The UCP/UCF/ICI system has managed to mobilize the resources available, in spite of uncertainties and bureaucratic delays. However, the system has not achieved its objective to be fully decentralized. Even though all investments under US$250,000 do not need UCP approval under the automatic refinancing mechanism, there still is involvement by the UCP in checking compliance with the Project's norms. Most decisions by the ICIs are centralized in La Paz. Also, loans are made on a first come, first serve basis. On the other hand, the Project had another purpose, <u>the development of the UCFs as investment promotion entities</u> and intermediaries between potential investors and ICIs. This has been only partially met. Technical assistance from Development Associates was not able to transfer these skills (see Institutional Options Study by Development Associates). The UCFs see themselves primarily as financial intermediaries which have mobilized the funds, and have not developed skills in investment promotion.

The number of players and competing interests involved, makes the UCP/UCF/ICI system a difficult activity to implement. However, the Project has delivered loans to small and medium size businesses in secondary areas where it would not have been possible before. The system has stimulated private sector participation in the development process. The private sector participates with 3 members in most UCFs' directorates. As the system is functioning now, no component has complete control over the loan granting process. UCFs have complete control on project evaluation and on issuing certificates of eligibility. The ICIs perform this function in the central axis, however, they rely on the UCF in the outlying areas, where they don't have offices or sufficient staff, and the cost of project evaluation is high. This is where UCF activity had the largest impact. The ICIs have control on loan approval, since they take the credit risk. The UCP has control on disbursement to ICIs and on loan approvals for loans above $250,000. Finally, the whole system is outside of the supervision of the Superintendency of Banks, and not subject to internal audits.

As of June 1990, the Project met its <u>socioeconomic objectives</u> to increase production, foreign exchange, and employment. The cumulative effect of the four years included an increase in demand of local inputs of US$23.5 million, creating indirect value added (backward linkages) of US$21.8 million, based on a multiplier of 0.94. (Multipliers for this analysis were provided by the Central Bank.) Net foreign exchange earnings generated by the Project for the first four years equalled US$20.8 million, or based on a multiplier of 3.29, US$68.4 million. Together, the cumulative total value added was US$111.8 million, or more than 6 times the actual funds disbursed through the Project, or 2.4% of GDP in 1989.

The Project created 3,250 new jobs since July 1986, or an average investment of US$5,631 per job, based on US$18.3 million outstanding as of June 1990. The Project has also contributed to export diversification and import substitution, such as the case of Brazil nuts and milk, respectively. The Project has been quite successful in achieving an equitable distribution of funds throughout the country; 69% was concentrated in the central axis, compared to 86% channeled by foreign credit lines through the Central Bank. Finally, the Project also helped create new economic activities in depressed areas.

Conclusions

The MTCF Project has:

- Achieved the highest socioeconomic impact in the less developed regions of the country, and was successful in secondary market towns of Camargo and Riberalta.

- Generated the most employment in small, medium, and export-oriented businesses, in particular.

- Obtained better regional distribution than other foreign credit lines, and has helped create new economic activities in depressed areas.

- The Project has financed projects that otherwise would not have been financed through the commercial banking system.

- Improved the capabilities of the UCFs and the UCP.

However, the MTCF Project:

- Did not directly address the constraints to increasing capital formation in secondary market towns.

- Emphasized financial sustainability over other Project goals. To increase disbursements, the Project channeled funds to some large projects which generate little employment, and lent working capital for medium and large projects which probably could have obtained financing from commercial banks.

- Has not fully achieved its objective to be decentralized, in spite of the automatic refinancing system, mainly due to centralization of decision-making by the ICIs.

- Did not develop the investment promotion capabilities of the UCFs.

- Created a complex, cumbersome structure outside of the Central Bank refinancing system, which will not be sustainable in its current form after PACD.

- Has not directly addressed the constraints in the banking system, such as improving project evaluation.

Recommendations for the last year of the Project

- Continue the project through to PACD, emphasizing lending to small and medium projects, and export oriented projects, in less developed regions of the country since that is where there has been the highest impact.

- Carry out pending administrative matters to the project, such as: reschedule problem loans, write down the DDC portfolio, consolidate accounting systems, coordinate efforts with the Superintendency of Banks, and redistribute portfolio to less developed regions.

- Improve the participation of ICIs by strengthening their development departments in project evaluation and supervision, by encouraging decentralization of decision-making, and by requiring more flexibility on guarantees/collateral requirements.

- Support the increased participation of the private sector, in particular to obtain a majority on the Board of Directors of each UCF.

- Provide technical assistance for investment promotion, marketing and economic studies.

- All project evaluations and credit analysis should be done by the ICIs which have skilled personnel, otherwise by the UCFs in the less developed regions, as it has been done in the past.

Recommendations for Creating Permanent Institutional Structure

- There is general consensus that new financial intermediaries are needed to introduce competition to the banking system.

- There is a need for a private development bank (PDB) to address the unmet demand for long term credit in Bolivia, especially with the closing of State banks.

- The GOB does not intend to be an owner in the financial sector, therefore the proposed PDB would be private, for profit, with a wide shareholder base.

- The PDB would initially have three core departments: project financing (for medium and large businesses), foreign trade, and small business. The PDB would lend in all sectors of the economy.

- The UCP/UCF system could be absorbed into the small business department of the new PDB. This would include absorbing the personnel, loan portfolio, fixed assets, and learning experiences as much as possible.

- The PDB would be complemented by a separate project, an investment promotion program called FINDES, which would conduct marketing studies and help attract foreign investment.

v

Lessons Learned

- o There should not be a multiplicity of objectives, such as supporting secondary areas vs. financial sustainability, or financial intermediation vs. investment promotion, which cause confusion and require tradeoffs in implementation.

- o AID should ensure any investment financing mechanism it creates be subject to adequate supervision and control (by the Superintendency of Banks, and subject to regular internal audits), to contribute to institutionalization after PACD.

- o The fee structure throughout the country should be more flexible to accommodate different stages of development and risk. Also, investment financing projects will always need to have clear guidelines for rescheduling.

- o Rash decisions to suspend project funds may undermine the Project and create disrespect for AID's work in the financial sector.

COUNTRY CONTEXT

In the decade of the seventies, the Bolivian economy showed high investment GDP growth rates, in a context of low inflation and equilibrium of the external sector. That was possible because the country benefitted from a period of relative political stability, exceptional prices for export of its products and an important flow of foreign loans with international private banks. However, the surplus generated by favorable terms of trade and the resources from external loans were utilized to increase the State bureaucracy and to finance numerous costly investment projects with doubtful financial, economic and social viability.

At the end of the seventies and the beginning of the eighties Bolivia underwent a strong period of political instability due to its fragile democratic process and to the ambition of some military groups to remain in power. At the same time, investment and internal savings started to fall, external financing was reduced and the external debt increased. The grace period of commercial loans came to an end and the principal had to be repaid.

In 1982 a coalition of leftist parties, "Unidad Democrática y Popular" (UDP) took over power claiming political freedom and greater social justice. The UDP Government confronted a difficult economic-financial situation, since the lack of internal and external equilibrium became more acute as a consequence of world crisis that was reflected in the deterioration of terms of trade, the increase of interest rates and the exhaustion of external resources. On the other hand, in the absence of a clear and coherent economic strategy to mitigate the crisis, contradictory and counter-productive macro-economic policy measures were adopted which hindered financial stability and savings and investment.

These factors, combined with the strong drought that whipped the high plains and the valleys, and the floods that affected the Eastern region of the country in 1983, caused the GDP to further contract. The fiscal situation deteriorated rapidly due to an excessive increase of expenditures that could not be offset with increased taxes. As a result, the public sector deficit increased from 8% of the GDP in 1981 to 28% in 1984. The high fiscal deficit was financed with expansion from internal credit by the Central Bank, which generated the highest inflation in Latin America. As of September 1985, the annual inflation rate reached 24,000%.

In 1984 the external public debt was higher than the GDP and its repayment represented over one third of exports of goods and services. The Government's policy with respect to a fixed exchange rate lead to a significant over-valuation of the currency and to a parallel rate more than twenty times the official exchange rate. This caused acute distortions in the allocation of resources and discouraged exports. More people dedicated themselves to speculation, since it was more profitable, than productive investment.

The crisis was also the result of structural problems inherited from the past. After the 1952 Revolution, intervention of the State in the economy was overpowering. The participation of the public sector was not limited to the provision of social, educational and health services, and the construction of basic infrastructure, but also to the production of goods and services. Thus, a significant number of public enterprises and decentralized entities were created. The majority of them turned out to be inefficient, and in order to survive had to have direct and indirect Government subsidies. Another structural problem worth mentioning is the lack of capacity of the economy to increase and diversify its exports. The macro-economic policies implemented prior to 1985 lacked the necessary incentives for exporters since it was more profitable to produce for the domestic market, instead of producing for export purposes. In 1985 tin exports and natural gas represented over 80% of total exports.

Under these circumstances, the Government of President Paz Estenssoro took power in August 1985. He inherited a very acute economic, social and political crisis. The most important economic objective in the short term was the drastic reduction of inflation and to restore external equilibrium, so as to immediately reconstruct the economy and to establish the basis for sustained economic growth. In this sense, the Government implemented a program to achieve stability and structural changes known as the "New Economic Policy" (NEP), designed to attack, in the first place, the non-financial public sector deficit. At the same time they carried out a set of structural measures tending to eliminate controls and restrictions imposed by the State, as well as to reduce the role of the public sector in production.

On the other hand, measures were adopted to promote a free trade economy, where decisions to produce and invest would be oriented by the needs of the market, and the price of production factors would be freely determined in accordance to the rules of the offer and the demand. The most important elements of the economic strategy were:

1. unified exchange rate and flexible exchange rate policy;
2. liberalization of interest rates and the financial system;
3. elimination of tariffs and other trade restrictions;
4. the liberalization of labor;
5. more discipline in expenditures and tax reform;
6. the restructuring of public sector entities;
7. the modernization of the State with the implementation of financial information, non-financial systems and fiscal control;
8. Improved relations with Bolivia's official creditors.

The program initiated in 1985 has been very successful, in spite of adverse external factors, such as: the drop in tin prices in international markets during 1985, that compelled the Government to dismiss 23,000 miners from the Mining Corporation of Bolivia; the reduction in export prices of gas and the non-payment of gas invoices by the Republic of Argentina. It is estimated that in the period 1986-88, the terms of trade dropped 46 percent.

During the next three years the economy showed positive growth rates, even though in per capita terms, this is still insufficient to improve the standard of living of the population and to reduce the still high unemployment rate. Public investment recovered its traditional levels. Nevertheless, the private sector showed rather low investment rates; partly due to the high rates of interest prevailing in the financial market and also due to the lack of a clear legal framework for direct foreign investment.

Inflation has been fully controlled thanks to the austere fiscal and monetary policies and to a cautious wage policy. The public sector deficit has been greatly reduced due to strict controls on expenditures, realistic prices in the public sector enterprises, decentralized entities of the Central Government and the implementation of the Tax Reform. All of these have increased fiscal revenues from 8% of GDP in 1986 to 16% in 1988.

In spite of the fact that the current account of the balance of payments still shows a considerable negative balance, the international reserves of the country have been strengthened due to a massive repatriation of capital and to financial support from multilateral and bilateral credit organizations. Exports did not reach the amounts registered at the beginning of the eighties, as a consequence of the external shocks aforementioned, and to the lack of dynamics in the export sector, in spite of foreign exchange, tax and credit policies granted by the Government.

The successful renegotiation of the external public debt with the international private banking system and with bilateral creditors also helped strengthen international reserves. In effect, an agreement signed with the international banks in 1987 has allowed the country to re-purchase 65% of its commercial debt for an amount of US$ 387 million, at a price of 0.11 cents.

The new Government that was inaugurated in August, last year, announced that it would maintain the general guidelines of the economic policy determined by the previous Government, but would place greater emphasis in social development. This resulted in Supreme Decree No. 22407, which gives the guidelines and regulations on: the Law of Investments, the Law of Hydrocarbons, the Mining Code, and rules for joint ventures.

On the other hand, the new authorities continued negotiations with the International Monetary Fund and the World Bank and established the objectives for 1989/90 structural adjustment program. In turn, the Governments of Argentina and Bolivia renegotiated their debts, which resulted in a substantial debt reduction for Bolivia. Likewise, Bolivia paid its debt to Brazil with discounted Brazilian debt purchased on the secondary market. Also, Bolivia was able to obtain the terms and conditions established in the Toronto Agreement that had been granted until now only to the poorest African countries.

II. PROJECT BACKGROUND AND OBJECTIVES

A. Background

Until recently, Bolivia, had not actively promoted agro-industrial investment outside of the principal cities. By not doing so, the country had not been able to take full advantage of the opportunities available for development within the agricultural sector. Failure to invest in secondary commercial centers means that market linkages were not developed between rural producers and processors, or with suppliers of production inputs. The consequences of this failure are less national production than otherwise possible, less employment generation, lower exports of non-traditional products, and slower growth in national income.

B. Goals and Objectives

The Project goal was *"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 was to increase the level of productive private sector investment in Bolivia's rural and semi-urban areas. This would fuel production in the region, create employment and generate economic growth. Increased economic activity would stimulate *"financial markets to respond more effectively to the financial requirements of enterprises located in the rural and semi-urban areas, primarily small and medium in size"*. The penetration of financial institutions to new markets will generate more business increasing services and profits. The component's dual purposes were:

1. The improvement of the capabilities of the institutions involved in the investment financing system: the UCP, the UCFs, and the participating ICIs.

2. The development of the UCFs as investment promotion entities and intermediaries between potential investors, and ICIs interested in expanding their rural investment loan portfolios.

C. Component Inputs, Outputs and Beneficiaries

The component's inputs were expected to be:

1. By USAID:

   a. Investment Financing: A permanent, centralized UCF Credit Fund composed of $17.4 million in DDC Project reflows and $26 million in new funds from AID ($14.5 million) and the PL-480 Title III Program ($6.5 million).

b. Technical Assistance and Training: This item includes funding for:
(1) Three long-term advisors in the fields of investment promotion, small and medium enterprise development and marketing.
(2) 48 person-months of short-term assistance.
(3) In-country seminars and overseas training.

c. Project Support Costs: This item includes funding for salary and commodity support to the UCFs and the UCP. It also funds investment research in priority market towns and an AID Project Coordinator.

d. Evaluations and Audits: Yearly local audits and the two project evaluations.

2. By the Bolivian Private Sector:

a. Private Sector Investment: A total of approximately $16.5 million, assuming 30% equity investment by potential borrowers and an average of 20% of each loan financed by ICI deposits.

b. Participation of private financial institutions in credit granting activities according to the UCF Credit Fund's operating procedures.

3. By the Bolivian Public Sector:

a. Regional Corporations: Approximately $400,000 for the UCFs operating costs.

b. Management of the Project Coordination Unit (UCP) of the Ministry of Planning and Coordination.

c. Support of the proposed activities, to reach out to a broad sector of the population engaged in small and medium size business activities in rural and semi-urban areas.

D. Based on the Project Amendment in February 1989, the component's outputs were expected to be:

1. Private sector investment in rural and semi-urban enterprises, totalling approximately $32 million.

2. A self sufficient system which will finance and promote private sector investments.

3. Five improved and strengthened ICIs for better management of their development lending programs throughout Bolivia.

4. The UCFs will have improved their capability to promote investments.

5. Three functioning priority market town pilot projects.

(Note - See Appendix D for discussion on whether outputs were achieved.)

E. The beneficiaries were expected to be:

1. Primary beneficiaries:
   a. Owners and employees of rural enterprises which will receive credit that would not have been granted otherwise.

   b. Owners and employees of intermediate credit institutions which will have expanded their markets to rural and semi-urban areas that would not have been possible without the program.

2. Secondary beneficiaries of this component will include exporter, supplier and clients of the rural enterprises. The entire Bolivian society through improved access to new ventures and credit facilities.

III. FINDINGS

The findings of the evaluation team are based on extensive interviews in La Paz, Santa Cruz, Beni, Tarija, Oruro, Potosi, Cochabamba and Chuquisaca, where the are functioning UCFs with portfolios. The team wishes to thank USAID/Bolivia, all of the Bolivians directly associated with the Project at the UCP and UCFs, government officials, private sector leaders, and individual borrowers, for their kind cooperation during this evaluation. (See Appendix G for list of persons interviewed.) Findings are based on: A. The Investment Finance Mechanism; B. Financial Sustainability; C. The Institutional Structure; and D. Socioeconomic Impact.

A. The Investment Finance Mechanism

1. Sources of Funds

The Loan and Grant Agreement to establish the FOCAS project was signed on July 23, 1986 between the governments of Bolivia and the U.S. The USAID Loan was for $15 million, and has a maturity of 40 years, with 9.5 years grace. (The loan was subsequently reduced to $12 million, and the grant component was increased $3 million in Project Authorization Amendment No. 2.) Interest payments are 2% p.a. for first ten years after disbursement, and 3% p.a. thereafter. Principal repayments will begin in 1996 and will be paid in 61 equal semi annual installments. The Bolivian Government, acting through PL480, made a loan for US$6.5 million, for 7 years, with two years grace. Interest payments to PL480 are currently 6%, but discussions are underway to lower the interest spread. Principal repayments begin in September 1990 to PL480, and will be made in five equal, annual installments. PL480 funds will therefore be paid back by 1995. There is the possibility that PL480 funds will be made available again to the project, but it is not explicit in the Letter of Understanding between FOCAS and PL-480. USAID funds will be available for thirty five years after the project ends in July 1991. Therefore, a permanent finance mechanism is required for the US$15 million from USAID, which may or may not be augmented by the US$6.5 million from PL480.

2. Evolution of the Investment Finance Mechanism

The investment finance mechanism has gone through four distinct periods. The first period was a startup phase and was very slow in disbursing funds. By September 1988 FOCAS was significantly behind schedule; only US$3.5 million had been disbursed. At this time USAID recognized that the original idea to develop five to ten priority market towns would not produce a large enough portfolio to sustain the system. A decision was made to have only three "pilot" market towns (Camargo, Riberalta and Tupiza), and to include La Paz, Cochabamba and Santa Cruz, provided that the projects had backward linkages to rural areas. This decision created Amendment No. 6, passed in February 1989, which was the beginning of the second period. The amendment also allowed for working capital lending, and lending to large businesses. Another significant change during the second period was the Automatic Refinancing Mechanism which allowed each UCF to approve loans up to $250,000. During the second period, from February 1989 until October 1989, disbursements increased over US$12 million.

During the third period, from October 1989 until January 1990, disbursements came to a near standstill as a result of USAID's decision to freeze all remaining funds (approximately US$7 million) due to internal uncertainties over the future of FOCAS. During this "crisis period", there was a proposal within USAID to use the funds for a private financial institution, "financiera", and to end the FOCAS project. This caused doubts by all participants, and there was some turnover of staff. The UCP and UCFs lobbied USAID to stop the idea for a financiera, since it did not build on the system which existed. In January 1990, the Government of Bolivia intervened and requested that the project continue. As a result, the proposal for a private financial institution was put on hold and will not affect the future status of FOCAS. The project should continue until July 1991, as originally planned.

The fourth period started in January 1990 and continues to the present time. Since January 1990 the UCP is under completely new management. Most of their efforts have been directed at solving the problems that arose during the crisis period, and working with the reflows from the loans.

In summary, the investment finance mechanism has not been evenly disbursed during the first four years of the project. Instead, it had a false start in the beginning, and then disbursed too quickly during the second period with changes introduced in Amendment No. 6. The financing mechanism came to a complete halt for four months during the crisis period. Now, the new management at the UCP is concerned with managing the reflows ($4-5 million per year), and institutionalizing the system.

3. Status of the Portfolio

As of March 31, 1990, all of the available AID Loan Funds were committed, US$400,000 was pending disbursement, and only US$600,00 of the PL480 Loan was uncommitted. In other words, at the time of this evaluation all of the available funds were placed, more than one year before project completion. A breakdown of total funds disbursed by region follows in Table 1.

Table 1 - Status of the FOCAS Portfolio as of March 31, 1990
In US$

Region	No. Projects	Disbursed	% of Total
Beni	21	1,687,348	9.4%
Chuquisaca	41	1,335,784	7.5%
Cochabamba	91	4,593,373	25.6%
La Paz	43	3,750,474	20.9%
Oruro	16	866,443	4.8%
Pando	3	366,451	2.0%
Potosi	29	753,174	4.2%
Santa Cruz	36	4,052,930	22.6%
Tarija	18	512,436	3.0%
Total	298	17,918,413	100.0%

Source: UCP, March 1990 most recent data available

By March 1990 298 projects had been financed by FOCAS, although over 400 projects had been evaluated and approved by the UCFs. The borrower bears full foreign exchange risk, as the loan must be paid back at the official dollar/boliviano rate. The interest rate to banks is Libor + 1% for fixed investment only, and Libor +2% for working capital. The banks then pass on a spread of 5% to the borrower, making an effective rate of 14-15% with current interest rates. The average amount coming due from 1990 until 1996 is estimated at US$5-6 million per year. By January 1991, approximately 26% of loans, or US$4 million should be repaid, excluding any rescheduling of problem loans. The average size project in the FOCAS Portfolio is $30,000, excluding five large projects over $500,000, or $60,000 including them. This compares to $95,000 on average for rural projects the DDC's Portfolio (first mid-term evaluation by ISTI).

Relevant case studies to compare this Project are found in Appendix I. This includes CINDE from Costa Rica and FOPINAR, is a similar project in Ecuador, which lends to small businesses. By 1988 FOPINAR had made 7,467 loans averaging US$14,000.

4. The Automatic Refinancing Mechanism

In May 1989 the Automatic Refinancing Mechanism was introduced. This was a significant step towards decentralization. In essence, this enabled each UCF to have automatic refinancing approval for projects up to $250,000, with UCP approval needed for projects above US$250,000, and AID approval needed above US$500,000. The automatic refinancing mechanism enabled more diversification between regions and with participating ICIs, as demonstrated by Table 2.

It is interesting to note that concentration in La Paz, Cochabamba and Santa Cruz decreased from 78% to 64%, and concentration in the top 3 banks decreased from 63% to 46%, after the automatic refinancing mechanism was in place. The automatic financing system was hindered by the lack of decentralized decision-making within the ICIs, however. For example, in Potosi, Banco Nacional can approve projects up to US$20,000, otherwise it must go to its office in Sucre for approval up to US$50,000. All projects above US$50,000 must be sent to the head office in La Paz for approval. The original project document differentiated between the approval limits of each type of UCF, ranging from $75,000 for "A" rated UCFs, $40,000 for "B" rated UCFs, and only up to $15,000 for "C" rated UCFs. The Automatic Refinancing Mechanism increased these limits substantially for every UCF.

Table 2: DIVERSIFICATION OF PORTFOLIO BETWEEN REGIONS

	Befores Auto. Refin.			After Auto. Refin.		
	Projects	US$000	%	Projects	US$000	%
Beni	2	311	2	11	1,376	11
Cochabamba	9	886	22	71	3,335	25
Chuquisaca	1	33	1	38	1,259	10
La Paz	2	282	7	37	3,058	24
Oruro	2	17	--	14	854	6
Potosi	5	222	6	19	471	4
Santa Cruz	3	1,965	49	30	1,988	15
Tarija	---	---	--	18	513	4
Concentration in LPZ, SCZ & Cochabamba			78%			64%

DIVERSIFICATION BETWEEN PARTICIPATING ICI

	Before Auto. Refin.			After Auto Refin. (Mar 90)		
	Projects	US$000	%	Projects	US$000	%
Hipotecario	2	1,320	33	19	3,053	18
Santa Cruz	5	671	17	44	2,578	16
B.B.A.	2	206	5	23	1,714	10
La Paz	5	341	9	31	1,807	11
Union	1	455	12	26	1,782	11
CACEN	2	266	7	30	2,032	12
Nacional	3	50	1	41	1,222	7
Big Beni	1	20	0	25	881	5
Mercantil	0	0	0	14	578	3
Bladesa	3	535	13	3	535	3
Cochabamba	2	118	3	11	364	2
BIBSA	0	0	0	6	201	1
Concentration top 3 banks	10	2,526	63%	93	7,843	46%

Sources: UCF La Paz and UCP.

5. Relationship with ICIs

There are two reasons that more than 400 projects have not been financed by the Project. One is that there are no more funds available, until reflows come in, and USAID decides what to do with the remaining US$3 million. Another reason is the high collateral requirements of the banks, which is usually 200-300% of the loan amount, in the form of fixed, mostly urban assets. Obviously, many of the smaller borrowers do not have enough fixed assets to meet this requirement. In the less developed regions, real estate has a lower value than in the larger cities. In Potosi, for example, the average cost of a house is less than US$4,000, and ICIs won't accept other forms of collateral, such as land, equipment or future sales. The Project has addressed this issue recently by utilizing the US$2 million Loan Guarantee Facility provided by AID/Washington. This Facility guarantees up to 50% of the risk, and some ICIs have agreed to reduce their collateral requirements to 1:1 with this support. There are some limitations to the Facility, however. There is only US$2 million available, which is not enough for projects already identified, and the guarantees are for up to three years. The Portfolio has an average maturity of five years, however, with one year grace. USAID Bolivia has requested that the terms of the guarantees be extended to five years to better suit the terms of the Project's loans.

One banker suggested that other items need to be addressed to lower collateral requirements. Banks need to improve project evaluation capabilities, and there needs to be clear policies to allow the restructuring of loans. (Currently, if a loan falls past due, even one day, the ICI must pay the UCP immediately.) Finally, a better understanding is needed of the risks posed by contraband activities to projects, which has resulted in problem loans in the past. Also, some ICIs have been very reluctant to finance any agricultural or mining projects, even if there are sufficient guarantees. This may be do to a lack of expertise to evaluate projects in these industries, and the high risk associated with the projects.

The history of development credit facilities in Bolivia is ample and well documented. The Central Bank of Bolivia (BCB) currently manages at least 20 different guaranty and direct lending facilities from different donors. Among them, institutions like IDB, World Bank, AID, UN, and several European governments. Many of these facilities have been hindered by problems within the BCB.

Extensive interviews with the banking community revealed that, in spite of the cumbersome UCP/UCF system, there were some advantages:

- When FOCAS became available, there was a general scarcity of funds in the banking system. This situation has since changed and now the banking system is very liquid.

- The offer of automatic refinancing and the opportunity of by-passing the Central Bank bureaucracy was appealing.

- The 5 point spread and the control over the credit authorization process was attractive.

- Since they were not required to modify their collateral requirements, they were not increasing the risk.

Essentially, the ICIs perceived the new activity as an opportunity to broaden their markets without materially increasing the risk, when lending funds were difficult to obtain. However, at the onset of the program, funds moved slowly. All credits had to be approved by the UCP and USAID. Some of the UCFs were not organized for the credit evaluation activity. Additionally, it was difficult to reach the secondary areas because the ICIs were not there.

Some ICIs began organizing development departments overlapping much of the UCFs' activities, especially in the major cities. One of the major problems with the Project is that ICIs must reimburse the UCP immediately for loans that fall in arrears.

6. UCF Credit Fund

A proposed document at the UCP establishes the rules for "institutionalizing the system". It describes the mechanism to unify the portfolios under control of the new system, for the first time. (The Corporation's portfolios are currently outside of the control of the UCP.) The Project Paper assumed that by the end of the project a permanent UCF Credit Fund would be established with DDC (Corporations) Project Reflows ($17.4 million), USAID ($15), PL480 ($6.5), or a total of $38.9 million. The new UCF Credit Fund document assumes there will be US$34.5 million available, by reducing the DDC portfolio by $4.4 million. In fact, it will still be less, considering the uncertainty of PL480 funds, and the potential losses in the Corporation's portfolios of up to 50%.

The Fund will be centralized to allow the GOB to allocate resources rationally among the UCFs. Also, the UCF Credit Fund supports a permanent, decentralized financial mechanism whic', responds to the regional financing needs. Specifically, it tries to improve the loan operations, and regional distribution of the portfolio. One of the goals is the ability to generate sufficient financial income to sustain the UCP and UCFs. The new criteria under the UCF Credit Fund are:

- Diversification and equal distribution of the portfolio;
- Reduction of risk;
- Better supervision of credit;
- Decentralization of the approval of credits;
- Compatibility with monetary policy of the Bolivian government, especially regarding interest rates.

This will be discussed in more detail in the section on recommendations for the institutionalization of the system.

B. Financial Sustainability

One of the stated goals in the Project Paper is financial sustainability. As mentioned earlier, the UCFs receive 2.6% interest spread of their own portfolio, and the UCP receives 1.4% of the total portfolio. In order to increase disbursements and help sustainability, Amendment No. 6 was passed. This has enabled some UCFs to achieve a sufficiently large portfolio, but some UCFs in the less developed regions have not been able to sustain a large enough portfolio to support themselves. Table 3 presents the future value of the income earned by the UCFs on their portfolios.

Table 3: Income Earned by UCFs on their Portfolio
As of March 31, 1990, in US$

Region	Disbursed	% of Total	UCF's Fee (2.6%)
Beni	1,687,348	9.4%	43,871
Chuquisaca	1,335,783	7.5%	34,730
Cochabamba	4,593,373	25.6%	119,428
La Paz	3,750,474	20.9%	97,512
Oruro	866,443	4.8%	22,528
Pando	366,451	2.0%	9,528
Potosi	753,174	4.2%	19,583
Santa Cruz	4,052,930	22.6%	105,376
Tarija	512,436	2.9%	13,323
Total	17,918,412	100.0%	465,879

Source: UCP

The UCP earns 1.4% of the total portfolio, or US$250,858 based on the portfolio in March 1990. (The income is realized on the reflows, so it is spread over time, but it is nevertheless substantial). The UCP has been supported by USAID with grant money of US$248,000 per year for the first three years. This is apparently the amount needed to cover all operating costs. One would assume that the costs of running the UCP should decrease towards the end of the project, as the system became more efficient and automated. This does not seem to be the case, however. As of June 1990, cumulative surpluses by the UCP totalled US$746,551.

The level of personnel and total expenses of each UCF varies significantly, as seen in Table 4.

Table 4:Expenses of the UCFs
December 1989

Region	Personnel Expenses/ Total Expenses	Total Expenses/ Total Portfolio
Beni	57.6%	3.8%
Chuquisaca	77.0%	17.9%
Cochabamba	48.0%	2.2%
La Paz	58.0%	6.7%
Oruro	89.0%	17.5%
Potosi	81.0%	7.8%
Tarija	n.a.	19.1%

Source: UCP (Santa Cruz was not available)

Cochabamba has the lowest expenses relative to other UCFs. Oruro and Potosi appear to have high personnel costs, however, Potosi's total expenses were only US$54,337, compared to US$167,512 expenses for Oruro. Chuquisaca has relatively high expenses, but it is fully supported by DDC funds.

Table 5 presents the operating surpluses (deficits) of the UCFs for 1989, and forecasts for 1990.

Table 5:Operating Surpluses/(Deficits) of UCFs
In US$

Region	December 1989	Forecast 1990
Beni	3,105	2,518
Chuquisaca	98,419	153,923 (April 1990)
Cochabamba	48,959	33,711
La Paz	9,688	288,046 (April 1990)
Oruro	(75,921)	(40.175)
Potosi	(24,443)	(30.000)
Santa Cruz	n.a.	n.a.
Tarija	18,520	n.a.

Source: UCFs
n.a. - not available
Exchange Rates - Bs. 2.69/US$1.00 in 1989 (period average)
- Bs. 3.09/US$1 in April 1990

At this time, it is impossible to have an audited, consolidated version of the operating budgets. The best impression obtained on the system is the level of expense, and surpluses (deficits) shown above. We must therefore qualify our analysis due to lack of consistent accounting methods. The UCP is going to implement a standard accounting system for all of the UCFs, and has contracted a local accounting firm to help with the effort. Most of the UCFs now provide the Superintendency of Banks with monthly statements, and so consistency is improving. This will be necessary before advancing to Phase II, the institutionalization of the system.

Can the system sustain itself? The UCFs and UCP believe that by the end of 1990, the UCP should be self-sustaining, but the UCFs will receive enough income to cover only 60% of their operating expenses. This will increase to 80% by June 1991, and by June 1992 the system should be self-supporting. It is hard to confirm or deny this, however based on the accounting differences mentioned above. It seems that the profits of some UCFs (especially La Paz, Chuquisaca and Santa Cruz) are more than sufficient to carry the losses of Potosi and Oruro, however. Obviously, there is a wide disparity in the level of income generated by the UCFs. This is a function of the distribution of both the FOCAS and Corporation portfolios, the level of DDC support, and other resources available to the UCFs. Table 6 presents the breakdown of the UCFs Portfolio and the level of DDC support.

Table 6: Breakdown of UCF's Portfolios and DDC Support
In US$

Region	Focas Portfolio (Dec.1989)		Corp. Port. (1988)		DDC Support (1986-89)
Beni	1,502,130	(52%)	1,376,673	(48%)	12,968
Chuquisaca	1,280,391	(43%)	1,713,016	(57%)	14,000
Cochabamba	3,844,659	(61%)	2,510,393	(39%)	76,000
La Paz	3,113,187	(63%)	1,803,848	(37%)	52,000
Potosi	645,892	(93%)	49,009	(7%)	8,000
Oruro	847,612	(88%)	110,336	(12%)	8,000
Santa Cruz	3,952,929	(56%)	3,116,574	(44%)	46,000
Tarija	489,912	(19%)	2,122,219	(81%)	50,218
Total	15,676,712		12,802,068		267,187

Source: UCP

Tables 5 and 6 demonstrate the gap between UCFs in the more developed regions, which have larger portfolios and more DDC support, from the smaller UCFs. Potosi and Oruro, in particular fall short in level of portfolios and DDC Support.

The Project Paper projected that both Oruro and Potosi would have larger portfolios (over US$2 million), and that both would receive more support from the DDC. Obviously, this was optimistic, and it seems that for the foreseeable future these two regions will need additional support. In 1989 the UCP provided an interest free loan to Potosi for US$12,146, and will provide another interest free loan for US$30,000 in 1990. The UCF in Potosi needs a portfolio US$2.5 million just to break even. In the case of Oruro, interest free loans of US$40,175 and US$24,580 were provided in 1989 and 1990, respectively. This extra support, combined with the decision to reallocate 40% of the reflows from the FOCAS portfolio, will help the less developed regions, but may not be the long term solution to cover their operating deficits There is an Institutional Support Fund aimed at supporting the less developed regions, which should be implemented shortly.

In comparison, some UCFs, such as Chuquisaca, La Paz and Tarija, are generating substantial levels of income. (Most likely the UCF of Santa Cruz is also.) Also, several have substantial resources beyond either the FOCAS or Corporation portfolios. For example, Chuquisaca's operating budget originates mostly from their own resources (65%), and 35% from both the Corporations and Focas portfolios. Finally, the difference in size of portfolios between regions is significant. The largest UCF, Santa Cruz has a combined portfolio of more than seven times the portfolios of Oruro or Potosi.

The main issue regarding the sustainability of the system concerns sharing profits and losses between the UCFs, and the level of support for the UCP. At the present time each UCF acts as an autonomous unit, and there is obviously reluctance to consolidate the accounts by those that are better off. Profits are not shared at all, but the 40% of the reflows from the portfolio will be distributed to the smaller regions. This is further complicated by the lack of ICIs and inflexible collateral requirements in the less developed regions. Eventually, a decision will have to be made to subsidize the operations of Oruro and Potosi permanently, (or perhaps raise the interest rate spread to 3.5% or 4%, as was anticipated in the Project Paper). Finally, the current interest rate spread of 1.4% to the UCP seems high, in comparison with the spreads earned by the UCFs. The original spread allocated to the UCP of 1% was supposed to be sufficient to cover its operating costs.

C. The Institutional System

1. Overview

Despite the less than anticipated receptivity among ICIs to participation, the UCP/UCF/ICI system has placed all the credit line available -- 303 loans totalling nearly $18.0 million.

The number of players and competing interests involved, however, makes the UCP/UCF/ICI system a difficult activity to implement. In view of its complexity the system has done well. It has delivered loans to small and medium size businesses in secondary areas where it would not have been possible before.

The system has stimulated private sector participation in the development process. The private sector participates with 3 members in most UCFs' directorates. Recently, a representative of the private sector has been included in the UCP's board. Only privately owned ICIs are actively engaged in the financing. The beneficiaries of the loans are privately owned companies.

As the system is functioning now, no component has complete control over the loan granting process. UCFs have complete control on project evaluation and on issuing certificates of eligibility. The ICIs on loan approval and the UCP on disbursement to ICIs and on loan approvals for larger loans (above $250,000).

Their respective activities and interests frequently clash causing frictions and controversies among them. The role of the UCP is viewed as redundant by ICIs and customers who frequently complain on the long time it takes to complete a transaction.

The UCP has not performed well the expanded responsibilities envisaged by the Project Paper. It has been unable to consolidate the budgetary information it receives from the UCFs, (although this is underway, and should be complete by September 1990). During the crisis period, the UCP did not provide information to the ICIs that funds were no longer available. After four years of the project the UCP does not have procedural manuals in place, although there are drafts. Finally, the UCP only recently went through an internal audit, something which should have been done on a regular basis.

Very little investment promotion is done by the system beyond an occasional visit to producer associations and contacts with local ICIs. Much of this criticism is based upon the failure to transfer investment promotion skills by the long term advisors under the Development Associates contract. Some UCFs have participated in local trade fairs.

The UCP has an investment promotion officer who recommends investment promotion activities to the UCP Board and publishes the newsletter "Promotor de Inversiones", however the last issue of the newsletter appeared in May 1989. The UCFs have advertised in some local newspapers and promotional leaflets. However, the amount spent and the impact of the advertising is not significant. At the UCP and UCF level there is agreement that investment promotion activities should be carried out by the government. For the ICIs investment promotion normally means giving information on credit lines available for different types of investment. As a result, potential loan beneficiaries contact the UCFs on the recommendation of ICIs.

In the principal markets the ICIs see this feasibility study as redundant because their own development departments are able to do this work. However, in the secondary areas they rely on it for their own decisions. In secondary and marginal areas, where ICI presence is relatively scarce, UCF activity has had an impact. On the strength of UCF intervention ICIs have entered into loan arrangements that normally would not have been made.

2. Project Evaluation

The larger ICIs perceive the project evaluation and credit analysis activity of the UCFs as redundant, at least in the principal markets. There, they already have their own development departments to evaluate credits. However, they acknowledge that they would not have given some credits in secondary areas had it not been for the credit analysis done by the local UCF. The same is true for the project follow-up performed by the UCFs. The ICIs perform this function in their principal markets, however, they rely on the UCF in the outlying areas. The cost of project evaluation in secondary and outlying areas is high, compared to the cost in principal cities. Normally, ICIs do not begin project evaluation until the potential borrowers have a certificate of eligibility from the UCF. However, UCFs do not issue a certificate of eligibility unless a feasibility study of the investment is done by a qualified consultant.

Prior to March 1990, UCFs would evaluate projects before the ICI approved. This resulted in 400 projects with UCF approval and without ICI financing. Many borrowers wasted time (and money) for their feasibility studies, to no avail. However, since March all projects must have ICI approval first, as stated in the proposed credit policy. The procedure is suppose to work like this. The borrower first approaches the ICI. The ICI evaluates the project and the collateral, and upon approval presents the following documents to the UCF: Application for eligibility, letter of credit with guarantees, notarized signature by borrower, their evaluation, and financial statements. Upon request by the ICI, the UCF will do the evaluation. Once the evaluation is complete, the UCF then determines if the project fits the eligibility criteria:

- Developing or expanding productive, privately-owned enterprises in rural or urban areas,
- Significant forward or backward linkages

- Creation of new jobs, directly or indirectly
- An increase in production for local consumption or export
- Financial viability over the long term.

The UCFs check to make sure the financing is not used for:

- Publicly owned enterprises
- Infrastructure development activities
- Traditional agricultural production
- Strictly commercial trading activities
- Mining activities, except in Potosi and Oruro
- Working capital loans for less than one year (this was later amended), since this was supposed to come from a line of credit from a commercial bank.

If all of the above criteria are met, the UCF will then issue a Certificate of Eligibility.

The initial responsibility for assessing the financial viability of the project is with the ICI, because they bear full repayment risk. However, since most ICIs do not have staff to evaluate projects outside of the central axis, they often depend on the evaluation by the UCFs in Oruro, Potosi, Tarija, Beni and Chuquisaca. There are no complete statistics on this, but a small survey done by the UCP showed that ICIs depend upon the evaluations by UCFs 41% of the time. While there are differences among the UCFs in terms of capabilities in evaluating projects, most have improved over the life of the project. Generally speaking, the ICIs look at financial rates of return on the project and evaluate the collateral requirements. The project was suppose to assist ICIs in improving their project evaluation capabilities, rather than rely exclusively on collateral. There is no evidence that this has occurred. The Superintendency of Banks supports the testing and licensing of Project Evaluators, to ensure a high level of competency.

The UCP has provided the UCFs with an analytical model and loan evaluation form to evaluate projects. The model is quite detailed, but not tailored for any specific industry. The UCFs in Oruro, Beni and Cochabamba use the model as it is; other UCFs tailor the model to fit their own needs, such as for smaller projects or for agricultural projects. The model rates the project based on socioeconomic criteria (60%) and financial criteria (40%). Projects which have scores above 60% are further distinguished based on their probability of receiving approval, with "A", "B" or "C". Projects that have an "A" rating have a higher probability of receiving approval, those with "C" rating have less chance. The UCP also "reviews" the evaluations prepared by the UCF and ICI, again to see if the project complies with all of the requisites. (In most cases, this is a duplication of efforts.)

3. Internal Operating Policies

Administrative decisions are taken exclusively by the Board of Directors of FOCAS, which consist of representatives from the Ministry of Planning and Coordination, USAID/B, PL-480, the UCFs, the Regional Corporations and the private sector. A Credit Committee exists within the UCP (consisting of the same members of the Board, and managers within the UCP) to approve projects above US$250,000, and to establish new policies, such as rescheduling on a case by case basis. General decisions are delegated to the Director of FOCAS according to the original agreement.

The internal operating documents which govern financial decisions within the UCP/UCF system are:

a. Credit Policy (and Credit Operating Manual)
b. Financial Policy (and Financial Operating Manual)

Both the Credit and the Financial Policies have been revised recently and should take effect in July 1990.

a. Credit Policy

The Credit Policy includes the overall conditions under which loans are made from the FOCAS and Corporation portfolios, including eligible activities, operating procedure, supervision and administrative responsibilities. This document has been revised several times, to accommodate changes in activities, amounts available for working capital, decision making authority, and regulations on reflows. Some UCFs have their own Credit Policies as well regarding their DDC portfolio. A new Credit Policy was passed in July 1990.

Projects must go to the Board of Directors of each UCF for approval. This process within the UCF can take up to one month, but the approvals from ICIs have taken longer than a year, in some cases. Once all of the documents are complete and approved by both the UCF and ICI, they go to the UCP for review and for disbursement.

Sometimes the UCP requires additional documentation, before it approves disbursement. The funds are disbursed within seven days after the UCP approves disbursement. When there is more than one installment, the ICI, in cooperation with the UCF, will monitor progress and obtain appropriate documentation before approving a second or third disbursement. During this initial monitoring phase, several credits have been retracted, due to misuse of funds.

During the crisis period, there many projects which had their Certificate of Eligibility from the UCFs, but could not get financing. In one case the UCF and the ICI (Banco de La Paz) had approved six projects, all of them relatively small (from $30,000-$50,000), but these were rejected by UCP with no official explanation. The Certificate of Eligibility issued by the UCF expired during this time, and in a few cases Banco de La Paz provided bridge financing. Communication with the ICIs especially broke down during this period, which has discouraged some from working with the project in the future.

The supervision, control and monitoring function is carried out by the UCFs, according to the Guide for Control and Monitoring Subprojects prepared by the UCP. The UCF in Sucre has developed a much more detailed monitoring plan for its projects, which may be useful for other UCFs to study. Each year they develop a plan for visiting every project, to monitor it at the most appropriate time. Each project is visited twice a year. This is a way to mitigate the risk in the portfolio. In fact, most ICIs rely on the supervision of the UCFs, or may jointly supervise the project with the UCF Evaluator.

In summary, the Credit Policy has changed frequently over the first four years of the project. Some UCFs find the guidelines provided by the UCP on project evaluation and supervision to be too general. The Project Paper states that one of the objectives of Decentralized Investment Financing System was to facilitate decentralized credit approval by the UCFs, ICIs. However, the Credit Regime shows that project evaluation and credit approval has not been completely decentralized.

b. Financial Policy

The previous Financial Policy did not really function as an distributive mechanism between the regions. Credits that had approval from UCFs and ICIs were first in line to receive disbursement from the UCP. (As a result, the more developed regions were able to place loans quicker than the less developed areas.) As shown in Table 7, the actual distribution of the portfolio during the last year did not completely follow the plan.

Table 7: Distribution of the Portfolio by Region
July 1989 - June 1990, Percent of Total
US$ Amount

	Planned	vs.	Actual (March 1990)
Cochabamba	31.9%		25.6%
La Paz	20.6%		20.9%
Santa Cruz	14.2%		22.6%
Oruro	13.4%		4.8%
Beni	6.0%		9.4%
Chuquisaca	5.8%		7.5%
Potosi	4.3%		4.2%
Tarija	3.8%		2.9%

Source: Annual Investment Plan 1989/1990, UCP statistics

During the last year, some departments (Oruro and Tarija in particular) ended up with shortfalls, while Santa Cruz had more than 8% of its planned amount. In order to address this inequity in the system, the larger UCFs (Santa Cruz, Cochabamba, La Paz and Chuquisaca) recently agreed to keep only 60% of the reflows from their portfolio (approximately US$12 million), and to reallocate 40% to a Fund to Equalize the Portfolio between Regions, which mainly involves reassigning 40% of the portfolio (US$4.8 million) to Tarija, Beni, Oruro, Potosi and Cobija.

This does not involve loan reflows from the Corporations portfolio, which will stay in the region. (In the cases of Cochabamba, La Paz, Santa Cruz and Tarija, the Corporation portfolios are substantial. The portfolio will be redistributed to the less developed regions.

The new Financial Policy establishes also accounting procedures to consolidate the UCF/UCP Credit System. This is difficult since each UCF has its own accounting nomenclature. During June and July each UCF, as well as the UCP, will undergo an external audit. The UCP hopes to consolidate the accounts before the end of 1990.

The roles of each participant are also clearly explained in the Financial Policy. ICIs will continue to administer the portfolio under norms and the Letter of Understanding signed with the UCP, and report on the status of the portfolio. It is interesting to note that the ICIs have not participated in designing the operating documents, even though they are an integral part of the project. The UCP views them only as intermediaries.

The role of the UCP is to administer the resources and establish computerized information and accounting systems, and to supervise the activities of the UCFs. It is supposed to help develop investment promotion activities. The UCP will continue to evaluate projects over $250,000 as per the automatic refinancing guidelines.

Each UCF will manage reflows from the Corporation portfolio, through ICIs, according to norms in the Financial and Credit Policies. Also, each UCF prepares an Annual Investment Plan, in accordance with regional demand for credit and private investment. (The document doesn't officially acknowledge that the UCFs act autonomously on many of the subjects, even through there is a centralized policy.)

The Pl-480 Secretariat, as an autonomous public entity, will continue to assign and disburse committed resources which uses its funds, and evaluates the application of those resources.

The legal documents binding the above relationships are:

- Letter of Understanding between donors-FOCAS and PL-480
- Letter of Understanding to implement projects with funds from FOCAS and establish a UCF Credit Fund
- Contract to regulate provision of banking services
- Letter of Understanding to finance productive investments to the private sector.
- Letter of Credit and Guarantee
- Notarized Letter by the ICI, which is a guarantee that the ICI will pay UCP in the event of a default, through its legal reserve or current account at the Central Bank.

The existing Financial Policy specifies how the interest spread will be divided between the UCP and UCFs to cover operating expenses. It says that 2.6% will go to support subsidiary operations of the UCFs, and 1.4% to support the operating costs of UCP. (In the Project Paper, the initial spreads were 3% for the UCFs, 1% for the UCP, and 4% for ICIs. As a result of legislative changes, the spread for ICIs increased to 5%, and a decision was made to increase the UCP's spread to 1.4%) The 1% or 2% spread, (from fixed investment or working capital) will go to an Investment Promotion Fund. Any remaining spread will go to a Capitalization Fund.

D. Socioeconomic Impact

The Project goal was to "achieve a higher standard of living, through increased employment and production in Bolivia's rural and semi-urban areas". The purpose was to "increase the level of productive private sector investment in Bolivia's rural and semi-urban areas". This would increase production, create employment and generate economic growth. In this section the socioeconomic impact achieved by the Project, in increasing production and employment, generating foreign exchange, and helping the less developed regions of the country will be presented. The socioeconomic impact is based on a portfolio of US$18.3 million which financed 303 projects, as of June 30, 1990. The methodology for measuring the socioeconomic impact is discussed in Annex D.

The quantitative information presented by the UCFs has some serious deficiencies, which prevented us from making a more scientific analysis of the socioeconomic impacts of the FOCAS Project. The most relevant problems were:

- There is no information on the aggregate value, employment and foreign exchange generation during the start up, or construction phase of the projects.

- In the operational phase the calculation of foreign exchange generated by project does not specify if it is due to exports or import substitution.

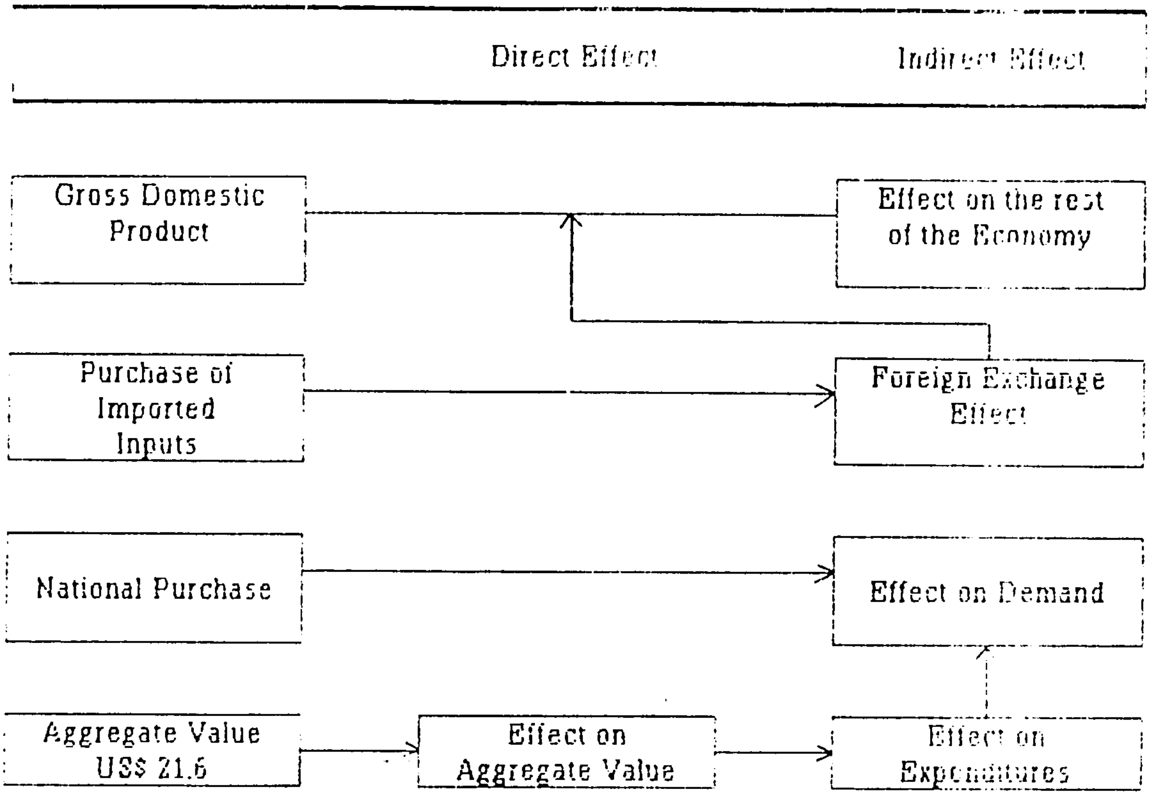
- There is no distinction between new investment, or expansion of an existing project.

- During the operational phase of the project the forward linkages to the rest of the economy are most important. For example, it is important that we consider marketing and transportation that results, to cite some examples. These impacts are difficult to measure with the information provided by the UCFs, and will require additional information to be collected in the future.

1. Increase in Production.

During the operation phase (vs. the startup phase) of the Project, the direct effect on aggregate value is equal to the total cost of production minus the national input expenditures and imports. This is equal to the sum of the perceived profits by the owners and the payment of wages. The direct aggregate value generated by the Project is US$ 21.6 million, based on the initial investment of US$18.3 million (using a multiplier of 1.18).

Table 8: Direct and Indirect Effects on the Economy
from the FOCAS Credit (Operational Stage)



The indirect effects can be distinguished between the increase in demand of raw materials and national input, and the increase in demad of final goods. The total projects financed by the Project using raw materials and national inputs is US$ 23.3 million. This amount also generates an increase in the aggregate value as a result of the effect of the demand by the sectors. For Bolivia, the multiplier impact of the raw material demand and national input is calculated to be 0.94. Thus, the indirect aggregate value would equal US$ 23.3 million multiplied by the factor of 0.94, that is, US$ 21.8 million.

On the other hand, in the case of Bolivia, the method of evaluating the impacts assumes external restrictions. This implies that net foreign exchange generated is incidental to the generation of the gross national product, due to the fact that the increase in foreign exchange allows for more importation of capital goods and inputs not produced nationally. Therefore, there exists a very important factor of recovered investment, growth and finally, aggregate value. The coefficient of the increase in the aggregate value owing to an increase in net foreign exchange has been calculated at 3.29. Therefore, the aggregate value in this case would be equal to the net foreign exchange produced by the projects, which is US$ 20.8 million, this multiplied by 3.29 all of which results in an increase in the aggregate value of US$ 68.4 million.

Therefore, the direct and indirect impacts during the startup stage of the project are not taken into account, which most likely means a negative foreign exchange position. The total aggregate value generated in the operation stage, as a direct impact, plus the effect in the purchasing of national inputs and the effect of foreign exchange reaches US$ 111.8 million dollars. This implies a multiplying effect of 6.1 x the amount of resources channeled through the Project. With a current GDP of US$ 4,168 million dollars in 1989, the total aggregate value obtained directly or indirectly through the project would be equivalent to 2.4 percent of the GDP.

Agroindustry has a multiplying effect on the agricultural industry, hence promoting products which would not have been produced in significant quantities if financed by the industries themselves. This is the case in fruits which are perishable, such as strawberries, cherries, pears, peaches, tumbos; and also vegetables, such as hearts of palm, asparagus, mushrooms and tomatoes, all of which have a high unit value in the international markets. Likewise, the yucca, which is utilized in manufacturing starch, is an important input to the paper industry. Another interesting example is the financing of a plant which manufactures flour from bone, an input to a balanced feed for poultry. Additionally, this last project has an effect upon the distribution of income in that an innumerable amount of indigenous people collect the bones from the trash and provide the factory with the bones.

2. Increase in Employment

The Project created transitional employment during both startup phase, but unfortunately the data is not available, as mentioned. It also created permanent employment during the operation stage. Similarly, during the two stages, direct employment related to the actual activity of the project and indirect employment induced by the project in other activities was created.

The furnished information indicates that the Project created 3,250 employments which, considering the amount invested at US$ 39.7 million dollars, signifies an average of US$ 12,218 dollars per job. If one takes away the largest projects financed by the Project which had almost no effect on employment, the average investment per job is reduced to US$ 7,584. For example, US$1.5 million was used to finance four harvesters, or US$ 375,000 dollars per job. Another example, the Cabanas Nelori project had a total investment of US$ 387,756 dollars per job. Also, the Central Aguirre project, with US$ 1,278,095 dollars, created only 13 direct jobs worth US$ 98,315. Although these are examples of projects which did not contribute to an increase in employment, they are a very small amount, compared to the majority of the portfolio which was used for productive activities with a large social impact an employment creation.

Although some criticism of the Project has been made about financing larger businesses which could have access to financing from the Central Bank, resources have nevertheless been channeled to the medium and small producer and to the regions in which it is difficult to obtain formal credit.

It is important to note that within the small productive units and the artesans, those that are oriented toward export are also those with a higher incidence of creating employment. This is due to the fact that primitive technology is used and manual labor is more intense. On the other hand, the larger businesses tend to incorporate more modern technology which uses automatized machinery and equipment. There is less manual labor, and that which is utilized is more highly qualified.

For example, the cost of US$ 704 dollars for the small artesan business of Waldo Soria, Eliseo Orellana and Alejo García is impressive. The same for La Cochalita which employs 86 workers at a cost of US$ 862 dollars and for the Centro Artesanal ASARTI, which officially employs nine persons at a cost of US$ 2,901 dollars but also gives additional work to 100 workers who weave sweaters in their homes. This has a very positive effect on the quality of living because at the same time they can care for their children an other chores in the home.

It is worth mentioning that the impact of the loans given to the Brazil nut processing plants in the eastern part of Bolivia. The financing of these four projects created 982 jobs, or an average of US$ 3,000 dollars per job. This is even more relevant when considering the social impact; 90% of the workers are women who contribute to the family income. Additionally, during harvest season the number of employees can easily triple with the incorporation of eventual personal.

Finally, in order to calculate the impact of the project on indirect employment, the total aggregate value created must be considered. For the project, the total aggregate value was US$ 111.8 million dollars and this was divided among the average productivity of each employed person, estimated to be US$ 2,071 dollars. In this manner, it would have generated 53,984 indirect employments which is very significant.

3. Generating Foreign Exchange

The data obtained from the UCFs show an increase of net foreign exchange (during the operation phase) of US$ 20.8 million dollars, and does not define whether it was created through exports or savings on imports by substituting domestic products.

However, in visiting some of the projects and through information obtained from other sources, one can conclude that the high percentage of the foreign exchange came from export activities. Furthermore, these activities were non-traditional exports which reduces (although still not substantially) the large dependence upon a few export products such as minerals and gas.

The exports supported by this credit are composed mainly of industrial, agroindustry and agricultural products and tourism. The industrial exports are: furniture and spare parts, clothing, textiles, sweaters and footwear. Exports from the agriculture industry include: food products, flowers, coffee, rabbit hair and Brazil nuts. Also, hotels were financed, especially in Potosi.

Apart from this, FOCAS financed various dairy projects in Beni and Santa Cruz, which served as a substitute to the powdered milk consumed before in these areas. Also, a project for processing steel products was financed, which substituted steel imports worth US$ 2.5 million dollars.

The impact of the export of Brazil nuts deserves special attention. Bolivia was the principal exporter of Brazilian nuts to North America last year and is estimated to be the world leader this year.

TABLE 9: ANNUAL EXPORTS OF BRAZIL NUTS
(Volume in 44 lbs. boxes, value in US$ millions, price US$/lb)

	YEARS					
	1985	1986	1987	1988	1989	1990
Value	0.65	0.25	5.00	8.00	12.10	15.90
Price	0.65	0.85	1.26	1.39	1.61	1.10
Volume	22,500	60,000	90,000	130,000	170,000	330,000

Source: Asociación de Productores y Beneficiadores de Castaña.

4. Geographic Distribution and Credit Activities

As can be observed in tables 10 and 11 on the following pages, the Project had a more equal regional distribution than the BCB. The Project concentrated 69.1% in the main regions (La Paz, Cochabamba, and Santa Cruz), compared to the 85.8% financed through BCB. However, a clear difference in favor of Santa Cruz, at 59.1 percent, is clear, to the detriment of Cochabamba when considering the credit given by the BCB. This high concentration of credit in the Santa Cruz region was the result of the line of credit 213-BO furnished by the Interamerican Development Bank for agriculture activities. This was principally utilized by the large agriculture businesses.

On the other hand, while the loans distributed by the Project for the rest of the country equal 30.8 percent of its total, the BCB only lent 14.3 percent to the less developed regions. This difference is even more accentuated in the Departments of Oruro, Chuquisaca, Beni and Pando. Apart from this, there also exists a large regional difference in the central region and the rest of the country. We believe that a better equilibrium would have been achieved if the original project was maintained, that is, furnishing loans to secondary areas and the more depressed regions of the country. Likewise, a better equilibrium would be attained if limits are placed on working capital loans, at market rates (instead of subsidized rates) of interest.

In referring to the credit distribution for economic sectors, the difference between FOCAS and the BCB is not as marked. With the loans by FOCAS, a more profound emphasis on Agroindustry is encountered whereas the BCB emphasizes the agriculture sector.

Table 10: Distribution of Credit by Department and Sectors

FOCAS
(Thousand US$ and percentages)

SECTORS	LA PAZ	CBBA.	STA.CRUZ	ORURO	POTOSI	TARIJA	CHUQUIS.	BENI	PANDO	TOTAL	%
Agriculture	518.7	1,318.5	887.6	0.0	36.0	167.9	343.0	840.5	0.0	4,109.2	22.9
Agroindustry	1,350.3	2,020.0	747.0	129.0	199.3	198.5	465.2	846.8	366.5	6,322.6	35.3
Industry	1,606.7	1,127.6	312.2	737.4	139.5	29.2	447.6	0.0	0.0	4,400.2	24.6
Tourism	0.0	0.0	0.0	0.0	363.4	0.0	0.0	0.0	0.0	363.4	2.0
Other	274.8	127.3	2,106.1	0.3	15.0	119.8	80.0	0.0	0.0	2,723.0	15.2
Total	3,750.5	4,593.4	4,052.9	866.4	753.2	512.4	1,335.8	1,687.3	336.5	17,918.4	100.0
%	20.9	25.6	22.6	4.8	4.2	2.9	7.5	9.4	2.0	100.0	

Source: DCF's

CENTRAL BANK OF BOLIVIA - 1989
(Thousand US$ and percentages)

SECTORS	LA PAZ	CBBA.	STA.CRUZ	ORURO	POTOSI	TARIJA	CHUQUIS.	BENI	PANDO	TOTAL	%
Agriculture	1,809.0	705.0	21,496.0	640.0	9.0	2,639.0	233.0	3,073.0	58.0	30,662.0	31.7
Agroindustry	3,519.0	1,943.0	20,334.0	196.0	0.0	257.0	0.0	58.0	0.0	26,307.0	27.2
Industry	6,558.0	2,258.0	14,245.0	0.0	177.0	0.0	0.0	131.0	0.0	23,369.0	24.1
Tourism	888.0	1,803.0	374.0	0.0	0.0	0.0	250.0	51.0	0.0	3,366.0	3.5
Other	5,604.0	731.0	785.0	1,544.0	3,840.0	0.0	627.0	0.0	0.0	13,129.0	13.6
Total	18,378.0	7,440.0	57,232.0	2,380.0	4,026.0	2,896.0	1,110.0	3,313.0	58.0	96,833.0	100.0
%	19.0	7.7	59.1	2.5	4.2	3.0	1.1	3.4	0.1	100.0	

Source: Central Bank of Bolivia

It is worth mentioning that the FOCAS program contributed to the mitigation of recession which threatened some of the regions by creating new economic activities. For example, due to the fall in the price of tin, mining in Potosí suffered a heavy recession. This was diminished somewhat by the construction of hotels. This is similar to the situation in the zone of Riberalta (Beni) when the price of rubber fell. Brazil Nuts have proven to be an attractive substitute. Likewise, in the region of Camargo (Chuquisaca) where the price of grapes has continually been low, the harvesting of peaches has helped immensely.

The concentration of credit by FOCAS in large enterprises, however, is only 26.8 percent. The Superintendency of Banks does not have a classification system of credits according to the size of the business. Still, the fact that 57 percent of the total portfolio of the banks has been directed to 2,000 credits gives us an idea of the degree of credit concentration in the banking system.

III. CONCLUSIONS

A. Achievements of the Project

1. The Project has achieved the highest socioeconomic impact in terms of direct and indirect employment, and backward linkages in the less developed regions of the country: Potosi, Beni, Oruro and Tarija.

2. More employment has been generated in the small and medium businesses, and in projects that are export oriented. In addition, female employment is high in these industries, which complements family income.

3. Compared to other credit lines, the Project has achieved a better regional distribution of credit by channeling funds to less developed regions of Bolivia.

4. The Project has also supported non-traditional exports, such as Brazil nuts in Beni, leather production in Tarija and sweater production in Cochabamba. In the case of almonds, it has been particularly successful. By 1989 Bolivia became the largest exporter of Brazil nuts to the U.S., and by 1990 it will be the largest exporter in the world.

5. Many of the UCFs have developed professional evaluation and supervision capabilities. In several instances the ICIs depend exclusively on the evaluation and supervision by the UCFs.

6. In spite of difficult economic circumstances and lack of ICIs in the less developed regions, the Project supported two of the three priority market towns, Camargo and Riberalta. The impact could have been greater if there were ICIs, and the terms of the mechanism were more flexible in these and other areas.

7. The Project helped local production by increasing intermediate goods used in agroindustry, which contributes to GNP growth, such as drying peaches in Cochabamba, Tarija and Camargo.

8. The Project contributed to the diversification of depressed economies, such as substituting Brazil nuts for rubber in Riberalta, and tourism and small industry for mining in Potosi. FOCAS has also indirectly contributed to better transportation and marketing in these economies.

9. The UCP/UCF system has managed to mobilize all of the resources available, in spite of uncertainties over the future of the project during a crisis period and bureaucratic delays.

10. USAID has recently begun to address the high collateral requirements required by ICIs, by integrating the Loan Guaranty Program from USAID/PRE Washington with USAID/Bolivia projects. A specific request has been made to accommodate the terms of the guarantees (which are up to three years) to the terms of FOCAS loans (up to five years). However, the guarantee fund for Bolivia is quite limited, only US$2 million dollars.

11. The Project financed investments that otherwise would not have been financed through the commercial banking system.

B. <u>Limitations of the Project</u>

1. Credit has been channeled to some large projects which generate little direct employment. These large borrowers usually have access to the formal credit system. This has taken away resources from other departments whose projects have more social impact and don't have alternative financing.

2. One project, Puerto Aguirre, is so large, has high risk, and may not be economically and financially viable. In fact, it is being rescheduled at the present time. This kind of project should not have been financed by FOCAS, but rather by the public sector or the regional corporation, as part of the national interest.

3. The original objective to increase capital formation in secondary areas was not fully achieved. Capital formation also requires developing markets, increasing investor participation, removing regulatory and other obstacles, and developing new products. The lack of technical assistance for these activities may have contributed to an over concentration and higher risk in the portfolio. The UCP should have supported the UCFs with marketing studies to identify opportunities and risks, as well as ideas for marketing the new products.

4. Working capital loans in some cases went to the medium and large projects, which could have been financed by the commercial banks. The interest rates for working capital loans charged by commercial banks are 8-10% higher than FOCAS rates, which are subsidized. This has been a great incentive for some borrowers to approach FOCAS, rather than the commercial banks.

5. The amendment to the project which allowed lending in the central axis and working capital financing only created a mechanism that disbursed too quickly, even though it contributed to sustainability of the system. There was a trade off between self sustainability and the original development objectives.

6. ICIs prefer to finance larger projects which require less staff to evaluate and supervise the projects. The credit limit of US$250,000 encourages this practice by the ICIs. (Nevertheless, the project has managed to finance small and medium sized businesses.)

7. The terms of some agricultural loans are inappropriate (too short, with too little grace period). Most agricultural projects are seasonal, and some projects need four years before the first harvest. However, current terms require amortization payments in the third year.

8. The system has not achieved its objective to be decentralized. The UCP has been criticized by the UCFs as an obstacle to the process, rather than a coordinator, as originally envisioned. This was particularly the case during the crisis period from October 1989, when USAID decided to freeze funds, until January 1990, when the GOB insisted that the project resume.

   - There was no communication ahead of time with the UCFs and ICIs of this decision. Also, communication was not handled well afterwards, as the UCP rejected projects with no explanation in several cases. As a consequence, many projects with Certificates of Eligibility (good for 90 days) expired without financing. This created bad will and discouraged many participants.

- Even though UCFs supposedly have automatic approval up to US$250,000, the UCP still "reviews" all paperwork, stating that some UCFs are not as capable as others in evaluation and project monitoring. We feel that there is no need to have further evaluation, or "review" of projects at the UCP, once they and the ICI have already approved them, since this has caused bureaucratic delays and frustrations.

- There has not been a decentralization of decision-making by the ICIs. Their central offices have rejected "viable" projects, due to lack of understanding of the local market.

9. There is some overlap on the evaluation of projects, particularly in the central axis, where most ICIs are located and have personnel in development departments. In the less developed regions, ICIs depend more on the evaluation of the UCFs, because they don't have development departments. The proposed credit regime attempts to eliminate this duplication, however.

10. The ICIs have been inflexible on guarantees, except in recent cases with USAID's Loan Guarantee Fund. In some instances this has resulted in financing wealthier individuals with urban real estate, and projects in the central region where real estate is more valued.

11. Although the ICIs take the credit risk, the UCP/UCF system should have been more realistic and better prepared for rescheduling loans. For example, if a loan is one day late, the ICIs pay the UCP immediately, which discourages ICIs from taking risk.

12. There are some projects which do not justify FOCAS financing in terms of financial need, since FOCAS is only 5-10% of the total amount.

13. There is no internal auditing system in place in at the UCP. The UCP has been audited by external auditors once, for the period 1987 through September 1988, and will soon undergo another audit through December 1989. A permanent internal audit function is necessary at the UCP to avoid any misuse of resources.

C. Lessons Learned

1. There should not be a multiplicity of objectives, such as supporting secondary areas vs. financial sustainability, or financial intermediation vs. investment promotion, which cause confusion and require tradeoffs in implementation.

2. AID should ensure any type of financial institution it creates be subject to adequate supervision and control (by the Superintendency of Banks, and subject to regular internal audits), to contribute to institutionalization after PACD.

3. The fee structure for UCFs throughout the country should be more flexible to accommodate different stages of development and risk. Also, investment financing projects will always need to have clear guidelines for rescheduling.

4. Rash decisions to suspend project funds may undermine the Project and create disrespect for AID's work in the financial sector.

IV. RECOMMENDATIONS

The recommendations which follow concern activities during the last year of the project only. The second phase of this evaluation will present recommendations for designing a permanent UCF Credit Fund.

A. Support Small, Medium Businesses and Projects in Less Developed Regions

Since the Project has achieved the highest socioeconomic impact in small and medium projects throughout the country, and all projects in less developed regions (Potosi, Oruro, Tarija and Beni), every effort should be made to support these areas the last year, by directing resources and providing technical assistance. Also, support for FOCAS could be integrated with USAID's projects in AHVA (alternative development) and Chapare in particular.

B. The UCP/UCF System

Since nearly all the funds have been committed and disbursed and since only 14 months remain to project completion, only minor adjustments to the system will be recommended.

Efforts should be made to complete the following tasks:

1. Reschedule of problem loans and create a mechanism within the UCP for future rescheduling.

2. Try to obtain financing for those projects whose certificates of eligibility expired during the crisis period.

3. Carry out all pending administrative and financial matters, including but not limited to:

   a. writing down the Corporation's portfolio
   b. resolving the current controversy over interest rate payable to PL-480 for the use of its funds
   c. consolidation of accounting systems
   d. coordinate efforts with the Superintendency of Banks
   e. carry out the recent agreement to redistribute 40% of reflows from FOCAS to the less developed regions, (60% stays within the department that where the loan was made).

4. Working capital loans should only be granted to projects which also have a fixed investment component. However, the interest rates for working capital should be at prevailing market rates.

5. Given the limited amount of funds available for the last year of the project, we propose a new lending limit of US$100,000 for reflows. New financing should be given to projects for small and medium businesses, with better geographical and sectoral distribution.

C. Improve Participation of ICIs

1. Strengthen the Development Department of the ICIS

Only a few banks have strong Development Departments, and these are located in the head offices. Technical assistance needs to be provided to these Development Departments in project evaluation and supervision, and encourage decentralization of decision-making. This should emphasize training to ICIs that have offices in less developed regions, and eliminate any overlap with the UCFs. In the future, all project evaluation and credit analysis, as well as disbursements and loan servicing should be done by the ICIs.

2. Help establish more flexible guarantees (collateral)

In order to expand the credit delivery system to the small and medium businesses, and the less developed regions, USAID should support the Government of Bolivia and the Banking Association, ASOBAN to create more flexible collateral requirements. (In particular, ICIs should consider accepting equipment, rural land and sales as collateral as well.) This could be done under USAID's Strengthening Financial Markets Project as part of policy dialogue. As a special incentive, USAID may want to direct its Guarantee Program to projects in less developed regions, that could not get financing from ICIs due to lack of guarantees.

D. Participation of the Private Sector

In order to increase transparency to the system, and adequately service the needs of the private sector in each region, we recommend that the private sector have a majority participation on the Board of Directors of the UCFs. This already exists with some UCFs, but should be introduced to the others as soon as possible.

E. Provide Technical Assistance for Investment Promotion, Marketing and Economic Studies

1. This area still needs much support during the last year of the project. There is a general consensus at USAID, the UCP and the UCFs that the technical assistance provided by Development Associates did not transfer skills (especially in investment promotion) to the UCP/UCF staff. Since the advisor left in June 1989, nothing has been done in terms of technical assistance. Now the UCP has a plan for technical assistance for the last year, and USAID has reserved funds for this purpose. We recommend the following be considered. Marketing studies need to be completed to help the different regions identify their comparative advantages, and understand the competition from other countries (including contraband). These studies could look into developing new products and markets, and identify local economic constraints. For example, an economic study of the Camargo region could identify pricing problems by the only monopoly which purchases the grapes, and alternative ways to lower the cost of transportation. Specific technical assistance could be offered to borrowers in new technologies or marketing.

VI. CRITICAL CONSIDERATIONS FOR A PERMANENT INSTITUTIONAL STRUCTURE

A. Introduction

The second part of the evaluation examine critical considerations and alternatives in creating a permanent institutional structure. The conclusions from Phase I of the evaluation indicate there are several achievements of the Project which are worth continuing after PACD. In the chapter on Financial Market Issues, we discuss the constraints in the financial system and proposed financial sector reforms currently underway in Bolivia. Ideas for a Guaranty System for Small Businesses are also presented. We then will discuss three alternatives for the Project: UCFs convert to Investment Promotion Units; UCFs convert to ICIs; or a new Private Development Bank (PDB) is created which absorbs the UCF/UCP system. We will advance some ideas on the structure and services of the new PCB, and how it will be integrated with a separate, but complementary project of USAID - Investment Promotion Foundation (FINDES). We will compare our recommendations with the Carana proposal and the UCFs proposal. Another recommendation is that USAID, with private sector commitment, move ahead to Phase III, which is implementing the recommendations included in Phase II for a private development bank. Terms of reference are proposed for Phase III.

B. Financial Markets Issues

1. Constraints in the Financial System

The Bolivian Financial System was very competitive during the seventies. There were several foreign banks, and one bank, BISA, was created as a development bank with IFC support. With the crisis of the early 1980s, most foreign banks pulled out of Bolivia. A majority shareholding of BISA was transferred to a group which turned the bank into a commercial bank. There have been no new development banks created since that time.

While the financial system has partially recovered from the crisis of the 1980s, there are persistent problems: financial savings have not reached the levels that they had at the beginning of the decade, the real rate of interest is too high. Some banks have profitability and solvency problems since their operating costs are very high and their portfolio is in default.

The new Economic Policy initiated in 1985 increased the past due loan portfolios of the banks. The enterprises that previously showed profits because they held a monopolistic position in the market, or received interest rate subsidies or access to preferential foreign exchange rates, are now confronting problems with the competition of foreign products, market interest rates and realistic foreign exchange rates. In many instances, the banks were not able to determine which were the activities and productive sectors that would confront difficulties, as a consequence of the NEP, and continued to refinance the portfolio of non-competitive enterprises. The inability to adapt to the new economic policies caused four commercial banks to file bankruptcy. This situation was also influenced by the existing close links between the financial intermediaries, individuals and economic groups, who used these banks to carry out fraudulent operations to their own benefit.

The concentration and relation of the banks, with economic groups is a serious problem of the financial system, since it extends the risk of its loan portfolio and prevents democratization of credit. The philosophy of Supreme Decree 21660 is very clear, to prevent the concentration of industrial groups with banks. Now this is one of the main concerns of the Superintendency of Banks.

No doubt, the main problem affecting the process of reactivation and growth of the Bolivian economy is the high level of interest rates. In order to be competitive, enterprises are working with very low profit margins, but the high cost of money is affecting the total cost, which tends to diminish the already precarious competition of the local industry. On the other hand, the generalized increase of the real rates of interest has negative effects on the growth of the economy, since some investment projects have stopped being profitable and therefore, are not carried out.

Obviously, it cannot be expected that the rates of interest in Bolivia approximate those in international markets, since Bolivia commands a higher risk premium. On the other hand, the lack of confidence in economic policies and the expectations regarding inflation, devaluation and the contraction of net credit to the private sector, on the part of the Central Bank, to finance the public sector deficit or to strengthen the precarious level of the international reserves, contribute to the persistent high real rates of interest.

Even though Bolivian deposit rates are 4-6 percentage points higher than those of the international markets, we believe that the domestic spreads between loans and deposits are still too high! The current dollar spread is 8-10 points, and in bolivianos the spread is 10-15 points. The factors affecting this situation are as follows:

- A good number of the banks in the system are operating with a high degree of inefficiency, with high operating costs due to a large number of employees in their payroll, too many branches and bulky overhead expenditures.

- Some banks maintain a high percentage of fixed assets (buildings and land), and non-mobilized resources, which cannot be loaned to the public and therefore diminish the profitability of total assets. Furthermore, these represent expenditures since maintenance costs have to be covered.

- An important proportion of the portfolio is in default or is classified as high risk. This factor compels the executives of the banking system to take precautions in advance against uncollectible loans. Thus, profits resulting from a high spread would offset future losses caused by bad loans. On the other hand, the Superintendency of Banks has become strict and is obligating the banks to make provisions against bad debts or high risk credit operations.

In some instances, the benefits derived from a lower cost of financial intermediation are retained by the banks and do not benefit the savers (higher deposit rates), nor the users of credit (reduced loan rates). This is because the banks still maintain an oligopolistic structure, due to lack of competition, (especially with the closing of the four banks), and the inefficiency and quasi paralyzation of the State banks.

Commercial banks, for the most part, do not evaluate the profitability of a project, but rather look to see there is sufficient collateral. Therefore, some viable projects with high socioeconomic impact do not obtain financing due to insufficient collateral. This situation could be mitigated if a guarantee system, or a type of insurance against uncollectible loans could be available, especially for small businesses.

There is a dire need for term credit in Bolivia's financial system. Productive sectors require resources from the capital market (at medium term from 3 to 5 years, or sometimes up to 10 years), while the savers provide funds to the monetary market (at very short term, maximum 90 days). The lack of confidence in macro-economic policies creates roadblock between funds available in the financial sector and funds needed by the productive sectors.

There is an excessive concentration of credit in the central axis of the country (La Paz, Santa Cruz, Cochabamba), mainly due to the absence of financial intermediaries in the other regions of the country and due to the rigid policies of the banks to lend to other regions. In the lesser developed regions it is quite possible that the risks are higher, and potential profits are lower. Since the GOB recently decided to restructure or eliminate the State banks, they should create the necessary incentives for the creation of new financial intermediaries, which also support the less developed regions. Otherwise, these regions will not attain the expected economic development due to the lack of sufficient financial resources to mobilize their productive capacity. Also, this is the best way to introduce competition to the financial industry.

A problem that the banking system is confronting is the low level of capitalization as a result of high inflation (and the de-dollarization) in the early 1980s. This prevents them from increasing their deposits and their lending operations. It is important that the financial intermediaries emphasize profitability in their projects, not just sufficient collateral. This will help ensure investors that it is profitable to invest in that sector. The financial intermediaries should have to compete for resources in a more aggressive manner, not only for financial savings to expand their credit activities but also to obtain investment resources to capitalize their banks. It is absolutely necessary that the banks become profitable, and their dividend payout ratios and the price of their shares are satisfactory, in order to attract investors and to convince them to channel a part of their available resources to the banking system.

2. Proposed Reforms to Modernize the Financial Sector

The Bolivian authorities, working closely with the international financial community, has initiated a series of reforms to modernize the financial sector. These reforms are aimed specifically at some of the constraints mentioned above. These measures try to eliminate distortions in the allocation of resources, which was heavily influenced by the large participation of the state, and also to create a more efficient economic system, where the decisions to invest and produce are based on the market. The reforms which will be introduced include:

- State intervention in the financial system will cease. The State development banks, such as "Banco del Estado", "Banco Agricola", and "Banco Minero" will be closed. These banks have accumulated large losses in the last twenty years, have large past due loan portfolios, and are in a position of near insolvency and illiquidity.

- The necessary conditions will be created to give more transparency and encourage competition in the financial system. This will be achieved by continuing to strengthen the Superintendency of Banks, and the passage of a proposed General Banking Law which will soon be presented to Congress. This Law does not include specific rules regarding Development Banks, however, which is very necessary.

- The creation of new intermediate financial institutions (ICIs) is being encouraged in order to democratize credit and to finance and support a more dynamic productive sector, especially those that are export oriented.

- Credit cooperatives and savings and loan institutions will be approved as ICIs, as soon as they comply with requirements by the Superintendency of Banks. These new financial institutions will focus on the small businessmen, artisans, and micro-entrepreneurs.

- The Development Department of the BCB will be restructured and development credits will be based on the needs of each economic sector.

- Interest rates will be liberalized for development credits, through a proposed auction system. The rationale is to eliminate the subsidy that exists, and prevent the diversion and misuse of funds.

- Credits granted from private international financial organizations will not receive the guarantee of the GOB.

3. Guarantee Fund for Small Business

In Bolivia credit is very concentrated among large companies; few resources are actually channeled to small businesses. This is primarily a result of the high collateral requirements already discussed in this report. For this reason, it would be wise to create a Guaranty Fund specifically to help small businesses obtain financing. This Fund would guarantee part of the risk, and thus would encourage more ICIs to lend to small businesses who otherwise would not have access to formal credit, because of insufficient collateral. (This could be similar to AID/Washington's Small Business Loan Guaranty Program). The incentives should be structured in such a way as to encourage voluntary participation by ICIs and borrowers. In consideration for establishing such a Fund, below are some desired characteristics:

- *Independent Management*

  The Fund will specifically be targeted at those borrowers which do not have access to credit, due to insufficient collateral., The Fund, and the participating institutions, should have complete autonomy from short term political decisions, and they should base their decisions purely on technical issues.

- *Solid Capital Base*

  From the very beginning it should be clear that the Fund is a way of addressing imperfections in the financial system and not a way of granting subsidies. To accomplish this the Fund will need to establish from the beginning the financial parameters (commissions, relation to capital, amount eligible for guarantee, etc.) in a realistic way which prevents the decapitalization of the Fund. Also, the Fund should not assume too high a level of risk which it cannot cover in the event of losses.

- *Operating Guidelines*

  It is important to establish clear rules and responsibilities of each of the participating institutions in the Fund.

- *Increase in Credit*

  The impact that a Guaranty Fund will have is directly related to the increase in credit that will result. One would hope that besides an increase in credit, the funds are used to finance profitable projects.

- *Avoid Transfers of Risk*

  Some ICIs may be tempted to transfer their projects with the highest risk to the Fund. It would be necessary to have controls which allow only new borrowers without sufficient collateral, but with attractive projects, to be eligible for the Guaranty.

C. Analysis of Alternatives

The current institutional structure of the FOCAS project is not viable over the long term, therefore it is not one of the alternatives presented. The institutional structure which divides responsibilities between the UCFs, UCP and ICIs will never function smoothly, due to competing interests between the participants, and constraints in the banking system. The system needs to be integrated under one roof. Also, FOCAS was never able to develop an investment promotion capacity, due to competing objectives which required a tradeoff in implementation. Nevertheless, there still is a persistent need for investment promotion. The trends in the GOB are to encourage new private financial intermediaries, and to bring those intermediaries under the supervision of the Superintendency of Banks. We present three alternatives for institutionalizing the FOCAS project:

1. UCFs convert to Investment Promotion Units
2. UCFs convert to ICIs
3. A new, private development bank is created which absorbs the FOCAS project, and works in conjunction with a separate investment promotion project, FINDES

1. UCFs Convert to Investment Promotion Units

In order to study this alternative, we will first examine the characteristics of a successful program, and then compare with the existing UCF/UCP system. Further in the report we will discuss the current efforts of USAID/B to create a separate investment promotion project for Bolivia, "FINDES".

a. Characteristics of a successful program

There seems to be confusion over just what is investment promotion in Bolivia, in spite of the fact that technical assistance was provided for that specific reason. In order to be effective and produce significant impact, an investment promotion program should ideally have the following characteristics:

Political Independence

A lack of political independence may subject the entire organization to severe pressure at staffing time and selection of priority programs. Political appointees are frequently forced to act with only a political viewpoint, delegating to a secondary position the necessary technical or development objectives

Effective Representation at the Board Level

An ideal Board for a promotion program should consist of innovative and creative private sector people who are capable of recommending alternative priority development programs. Frequently Boards are constituted by politically influential people, who though effective as a pressure group, do not have the technical or vocational background to produce effective change.

Budgetary Independence

The type and quality of effective investment promotion activity requires high operational budgets. The Costa Rican experience shows that public institutions find hiring and retaining qualified personnel for key positions extremely difficult due to budgetary constraints which do not allow for higher salary levels. This along with extremely cumbersome and inflexible systems inhibits the formation of a highly motivated group of individuals capable of producing results.

Quality Human Resources

The most critical element for success is having the necessary human resources to draw upon, both in terms of quality and quantity. Bilingual and bicultural staff with international business skills are needed. An essential part of this activity entails the ability to pay the appropriate salaries and offer compensation packages which will attract and keep key personnel.

This staff should have both sales and technical skills. In addition, it is essential that there be sufficient staff available to effectively serve as counterparts to the foreign office promoters, and also to attend the local volume of investor interest and service.

Selectivity of Services

A private sector promotional agency with complete operational independence should be selective in choosing with priority projects and areas with the most potential. This allows for short and medium term results to be obtained with a minimum of wasted efforts and resources. This selectivity avoids being overrun by a myriad of exporters, investors, students, politicians and others soliciting information and services which may be unproductive and of doubtful viability.

Active and Aggressive Presence in Foreign Markets

Only by direct operational presence in the market will effective investment promotion activities be carried out. These offices should be located in the principal business centers and successfully integrate its promotional activity with the local business community. This will achieve networking for effective penetration of target markets. Overseas promoters are highly specialized (and expensive) individuals that must carry out the tremendously sophisticated task of identifying and convincing target companies to carry out an offshore investment. This task can sometimes take months to achieve. This same promotional group will effectively access foreign commerce inputs and information. They should be intimately related to all foreign commerce activities carried out in Bolivia in order to interpret and process this information for their promotional activities.

The following countries, and many others, have effective investment promotion programs in place: Costa Rica, Dominican Republic, Honduras, El Salvador, Mexico and Jamaica. These programs are highly sophisticated and have already obtained significant results. Bolivia's proposed investment promotion program (FINDES) would have to contemplate competing with these programs for foreign investors.

Quick Response Time

The promotional field is plagued with changing world conditions and innovative competitive strategies, forcing developing countries to adapt to evolving foreign market requirements. These require a very fast response time on behalf of promotional agencies in order to structure and modify their programs. Public sector agencies are not very responsive to these types of changes, and have lost their competitive positions over time.

b. Relationship to the UCF/UCP System

Each UCF is governed by a Board of Directors with at least one member from the Regional Development Corporation (CRD). These are dependencies of the Ministry of Planning and are therefore subject to political staffing, pressure and intervention. Other members of the Board of Directors are appointed from the Chambers of Industry, Agriculture and the Federation of Private Businessmen. Under this type of integration it is very difficult to maintain objectivity and be cohesive with institutional goals while being subject to pressure from private interest groups and the public sector.

Another important consequence of being a public institution is the lack of budgetary independence. As mentioned above, this can severely inhibit contracting the appropriate people and can handicap the institution since programming and disbursements of public funds is frequently untimely and insufficient. As the UCFs are dependent upon the CRDs for financial support, political pressure as well as budgetary constraints are handicaps of the existing UCFs.

Investment promotion is a sophisticated and technically complex activity that requires market intelligence and foreign market presence. There is nothing within the UCF experience base, human resource and organizational structure that complies with the above mentioned prerequisites.

The nature of public sector dependencies is such that they must provide services to everyone. They cannot draw the line between unproductive exercises and institutional priorities. The end result is that frequently projects are not taken to conclusion due to the competition for time and resources. The UCFs play an important role within the context of the CRD's activities. It would be impossible to continue this role while also trying to promote foreign investment. The budgetary restrictions, political intervention and most of all the regional responsibilities would create significant conflicts of interest and, once again cause a multiplicity of objectives which could not be obtained.

The nature of the activities that the UCFs have carried out in the past does not prepare them in any way for the new types of activities and skills that investment promotion would require. There is no real possibility that the existing organization and staff could realistically undertake the required investment promotion activities for Bolivia.

2. UCFs Convert to Intermediate Credit Institutions

There are some positive aspects concerning the UCFs converting to ICIs. They could continue to provide credit in outlying regions to small businesses. They could break their dependence on the ICIs. Finally, they could capitalize on their regional expertise gained from the FOCAS Project. There have been at least three attempts to establish ICIs, (Santa Cruz, Chuquisaca and Cochabamba).

However, the negative aspects outweigh the positive aspects. The GOB is trying to privatize the financial system, and we would be creating a publicly owned ICI by converting the UCFs to ICIs. In fact, the Regional Corporations recently signed a document acknowledging inevitable privatization of their activities. Some of the larger UCFs have already looked into this, and probably have the expertise, capacity, and size to convert into ICIs, but the smaller UCFs would have difficulties converting to ICIs. The regional "financieras" or converting UCFs into separate ICIs is not a national solution for creating a permanent institutional structure. It is very difficult to think of a transformation of the UCF's into a national ICI because of regional differences and the ownership of each regional corporation. Thus, if the UCFs converted into ICI's they would operate with higher risk due to concentration by region and/or product. The essence of an ICI is to diversify risk, and this could not be achieved fully. By becoming ICI's, they would have to concentrate on the financial and credit aspects of the business, discarding the promotion functions. It is probable that by becoming ICI's, they would have normal commercial bank rates and spreads. Due to the small size of some UCFs and moderate spreads, it is doubtful that they could sustain their operations as an ICI. Up to now the UCFs have not been under the Superintendency of Banks. By becoming ICI's they would have to adhere to a more inflexible regulatory environment, thus reducing their present level of social impact. There does not seem to be any advantage in the UCFs converting into ICIs.

3. Private Development Bank is created which will absorb the UCFs/UCP

The only viable alternative, considering the financial sector constraints, recent reforms, the limited institutional structure of the FOCAS Project, and competing regional needs, is to create a Private Development Bank (PDB). The PDB could absorb the FOCAS Project (in terms of personnel, assets, goals and valuable experiences), and address several of the constraints in the financial sector.

Several arguments can be made for establishing a PDB:

- Bolivia needs to expand its productive capacity, and that can only be achieved by sufficient medium to long term financing handled in a professional way (guarantee requirements, promotion, T.A., debt rescheduling, etc.). This is not currently available in Bolivia.

- A successful investment promotion for Bolivia requires efficient and agile Development Banks.

- The scope of what needs to be done requires a professional staff in a central and several regional offices, to reach economies of scale.

- Bolivia is per aps at its peak in developmental financial assistance. It is an appropriate moment to establish a formal, credit-worthy, professional bank to channel and maximize the use of those resources, while they last.

- It is important to establish a broadly held private Bank as fresh alternative to the closely held banks of powerful interest groups or individuals.

- It is in the line with the GOB desire to privatize the financial system and to increase competition.

- Has far greater impact potential (by shear size, by complementing efforts with FINDES, the investment promotion agency), than leaving FOCAS as a separate, smaller project.

- It is better to incorporate the UCF/UCP system into the PDB an order to ensure continuity of programs and maximize UCF experience.

- Relative health of the FOCAS portfolio

There most frustrating aspects in establishing a PDB are:

- It will take one year to establish :, and 1-2 additional years to "take out the bugs" of the Banks' System.

- It will require higher proffesional staff requirements.

- Will require active private sector participation (this is not a negative aspect, but rather a temporary task requiring additional effort).

This alternative is recommended by the evaluation team. Below we will present preliminary ideas for the new PDB, which will be further developed during Phase III, when a comprehensive feasibility study is done.

VII. RECOMMENDATION TO CREATE A PRIVATE DEVELOPMENT BANK

A. Desired Characteristics

1. A private, for profit institution
2. With active private sector participation in its management
3. Broad capital base where no one controls more than 5% of outstanding shares, but still have an important stake and participation
4. Clearly established long term objectives and goals which allow postive return on investment along with developmental impact
5. Will not accept public sector deposits
6. Be under specific regulatory framework for development banks
7. Will coordinate with other related institutions
8. Will be self-sustainable while achieving socioeconomic impact

B. Objectives

There is more of a need than ever to establish an institution which provides medium and long term credit, with special support for the less developed regions and small businesses. The objectives of the new institution are completely in line with the public sector goals, and will continue to the original objectives of FOCAS. They are:

- Employment generation
- Foreign exchange generation
- Multisectoral development in traditional and non-traditional export sectors
- Foreign and domestic investment
- Regional development

Unemployment is estimated to be 20% on a national level, but is actually much higher outside of the central axis. This evaluation demonstrated that employment generation was especially impressive in the less developed regions. Also, this new institution will continue to help diversify the economies of the depressed regions, as did the FOCAS project. Finally, new employment opportunities could attract workers from the Chapare coca-leaf producing area, contributing to the alternative development strategies being implemented.

An analysis of Bolivia's traditional exports indicates an important reduction in foreign currency generation in the last decade. Even through non-traditional exports increased 25% in 1989, the total figure of $819 million is one third less than exports at the beginning of the decade. Investment projects promoted by the PDB should have export and foreign currency generation as a high priority. Experience in other countries has demonstrated that the most viable developmental projects are linked to exports and new markets. These projects typically represent between four and ten thousand dollars of exports for each new job created.

There are several sectors in the Bolivian economy where opportunities exist, such as mining, agriculture and agroindustry, and industry. The new institution will strive to have a socioeconomic impact in these traditional industries, as well as in non-traditional activities. One of the goals of the PDB would be to recover the export levels attained by the traditional sectors, as well as substantially increasing exports from non-traditional sectors.

Due to the multiplicity of objectives, the FOCAS project did not achieve its objective to promote investment. Although the project did generate domestic investment, the personnel were not trained adequately by the foreign advisors, and it did not have the resources to promote <u>foreign</u> investment. Investment promotion experts emphasize that it is a major commitment requiring trained staff and sufficient resources; investment promotion cannot be done "half way". In other developing countries foreign investment projects had significant impact in increasing employment and non-traditional exports, opening new markets, generating foreign exchange and transfering technology. The lessons learned from these foreign investments can be quickly transferred to the local sector, providing an important increase in export market orientation at the local level.

The PDB would continue the regional development objective of FOCAS, to emphasize lending outside of the central axis. Although loan applications would be processed on a first come, first serve basis as before, special technical assistance would be given to the less developed areas in identifying viable projects. This could include careful studies to determine opportunities and priorities on a regional level. Aggressive promotional activities would be carried out both in regional offices and internationally in conjunction with the proposed Bolivian investment promotion program (FINDES).

The PDB would have multilevel beneficiaries. Developmental Agencies have a tendency to focus on small enterprise projects, which may have social impact, but limited economic importance and long term viability compared to the larger projects. The PDB would serve small, medium and large scale enterprises. The large projects in particular can provide examples to the smaller projects in terms of vertical and horizontal integration, particularly subcontracting and sub-component sourcing. To ensure that the small business projects receive the appropiate priority and assistance, a specific Small Business Department would be created within the PDB with specialized personnel and specific objectives and goals.

Development projects frequently strive to produce economic and social benefits for a country, however gains in this area may produce an impact which is not necessarily the optimum. In a country like Bolivia where most inputs are limited, it is critical that the PDB choose and develop projects which maximize the use of resources through vertical and horizontal integration.

C. Core Services

1. Project Financing

This department would carry out medium to large project financings. This would be the unit most intimately linked to FINDES on a day-to-day operational basis.

2. Small Business Department

This department would engage in FOCAS-type financings, and would be the place to house the FOCAS portfolio and personnel. It would work in a more decentralized fashion than the above mentioned department. A delicate balance must be reached in limiting the cost of financing small businesses, while still achieving overall profitability. This could be supported by the Small Business Guaranty Fund in terms of sharing risk. Many international agencies would be attracted to the PDB because of the Small Business Department.

3. Foreign Trade Banking Services

This department would provide export and import financing (L/Cs, collections, etc.), and would contribute to export diversification. It would generate income in the short term, to balance the income derived over a long period of time from the other two departments.

D. Future Services

1. Second story bank (rediscounting of development loan portfolio)
2. Equity participation (when not a lender)
3. Leasing
4. Low and medium income housing (within the Small Business Department)

E. Funding

Funding must be appropriate for this type of activity, in terms of cost and repayment horizon. Refinanced lines of credit through BCB would not be adequate.

1. Equity
   a. Exact amount to be defined in Phase III when financial projections are made

   b. Based on scope of activities and impact sought, equity base possibly US$15-20 million

   c. Sources of Equity
      i. Undisbursed MTCF Funds, reflows MTCF, and GOB (through PL480) equity underwriting
      ii. Bolivian Private Sector investors
      iii. International Agencies/Development Banks (IFU, CDC, DEG, SBI, FMO, Swedfund, IFC, IIC, KFU, etc.)
      iv. USAID

   d. Potential breakdown of equity
      i. International Agencies (USAID) (33%-49%)
      ii. Private Sector (66% ideally, however it may be less if there is not enough investor demand initally, decreasing over time by sale of shares to private sector)

   The mechanism of having the GOB underwrite a portion of the PDB's capital with the Project's funds, is a fresh alternative that resolves the issue of transfering the funds to the private sector, while alleviating the need for raising substantial amounts of money from the Private Sector all at one time.

2. Credit Lines

   a. Development credit lines with 5:1 maximum leverage
   b. Correspondent banking credit lines
   c. Limited amount of market rate credit lines

3. Grants
   a. Technical assistance
   b. Other

F. Relationship to FINDES - a new Investment Promotion Program

As of mid-1990, a Bolivian private sector group initiated a private, non-profit investment promotion institution. FINDES - The Foundation for Investment and Development is the result of this initiative. USAID/Bolivia has been moving forward with FINDES under the Carana Contract for Export Promotion.

Thirty successful members of the Bolivian private sector will provide institutional support and an eleven member Board of Directors will provide program directives. The objectives of FINDES are to: generate considerable employment, contribute to the balance of payments through export earnings and attract significant foreign investment to Bolivia.

The statutes and Board representation are being constituted in such a way that it will avoid political intervention at the same time that public and private sector support is provided. Operationally, this organization will have an Executive Director, a General Manager, Investment Promotion Officers abroad and locally, as well as sector specialists for technical assistance.

Financing will be sought from international donors and the local private sector. Given the present worldwide interest in Bolivia and the alternative development programs being considered, this option has met with local enthusiasm. FINDES could well be the hoped for solution to integrate and coordinate foreign commerce activities in the future.

FINDES proposes a two stage chronogram of activities which hopefully will begin in Mid-1991. The first stage would create two foreign offices with a full local counterpart staff as well as contracting specialists and three sector specialists. (See Appendix J for Organizational Charts.) In the second stage two additional foreign officers would be staffed as well as two regional offices and a specialist for Bolivian exports to South America.

These local offices could share physical space with the proposed district offices of the PDB in three regions initially: La Paz, Cochabamba and Santa Cruz. The PDB activities could be complemented by coordinating with FINDES staff members and accessing local and foreign data bases. The selection of these three regions is based upon meeting FINDES objectives; the location of branches for the PDB will be analyzed in Phase III. The PDB staff members could disseminate FINDES information and act as receptors of regional inquiries outside of these main cities.

All staffing would be done based upon strict selection criteria and with technical assistance backup. This type of staff and organizational structure would ensure a rapid response time as well as access to critical foreign market information and networking.

The Bolivian private sector group adopted the CINDE - Costa Rica model which has proven to be successful. This model is highly transferrable to the prevailing Bolivian environment. If the project is supported by technical assistance from USAID/Bolivia, CINDE and Carana Corporation, it should also be successful.

G. Breakdown of Functions between PDB and FINDES

F - Financial
P - Promotion
T - Technical

1 - Head Office
2 - Regional Office

	Function	Office
Identification of regional opportunities,priorities	P	2
Identification of international opportunities,priorities	P	1
Project conception & development	P/F/T	1,2
Promotion (local)	P	2
Promotion (international)	P	1
Project evaluation	F/T	2
Approval Process	F/T	1,2
Disbursements/Follow up	F/T	2
Technical Assistance	F/T	1,2
Debt Rescheduling	F	1

H. Development Banks in other countries

Development Banks or Finance Companies are broadly defined as financial institutions which grant medium and long term loans. They may obtain their funds from a variety of sources, including the local government, foreign institutions, private investors and deposits. Their lending activities may be broad in scope or they may be limited to specified areas considered critical, such as housing, agriculture, fisheries and small business. In developing countries, development banks often follow commercial banks in the growth of the financial markets. They offer the same services provided by specialized banks and the securities markets in mature economies. They have a more important role in providing long term financing in a country with limited securities market, as in Bolivia. In most countries, development banks respresent 2-15% of the total assets of all domestic financial institutions. (David Gill, IFC, 'Development Banks and the Mobilization of Financial Resources", 1979, p. 2)

The role of development banks as a catalyst in modernizing the financial sector has varied considerably between countries. Some confine their activities to furnishing long-term loans and paying no attention to other financing areas. In other cases, their charter calls for specific participation in different aspects of the securities markets. For example, the National Development Bank in Sri Lanka is expected to stimulate the security markets by selling shares of client enterprises to the general public, with the objective of developing an active capital market. Also, the Bank may underwrite share issues of client enterprises or syndicate the funds needed for the successful issue of shares. (Annual Report, National Development Bank of Sri Lanka). Another development bank in Thailand made no contribution to the creation of a capital market, despite the fact that among its stated objectives was to "conduct its operations in such a manner as to assist in the growth of a capital market in Thailand and to improve facilities for marketing shares and securities". (The Industrial Finance Corporation of Thailand.) The Korea Development Finance Corporation (KDFC) was established in 1967 to assist in the development of private enterprise by furnishing medium and long-term industrial financing and equity participation, as well as technical and managerial consulting services. Not only did KDFC encourage the development of the Korean securities market, but also it played an important role in the creation of the country's commercial paper market, and encouraged leasing activities. The Private Development Bank of the Philippines participated in the development of that country's money market and formed securities trading subsidiaries. The Corporacion Financiera Colombiana (CFC) sought the development of underwriting activities.

Although many development banks have contributed to the modernization of the financial markets, there are several obstacles which were necessary to overcome. These included the preoccupation of their managements with the narrow area of long-term lending, their reluctance to buy equities, and their general unfamiliarity with the operations of a securities market. According to the World Bank, private development banks are finding it increasingly difficult to mobilize long-term resources and to maintain their financial positions. They are concentrating less on term lending and moving toward mixed financing strongly diluted with quick-turnover operations. Moreover, they are now combining project lending, often principally in foreign exchange, with commercial or money market financing. Their self interest in working with the business community and institutional investors have provided the private development finance companies with the incentive to play an active role in developing the capital markets.

(Quoted from Creating Capital Markets in Developing Countries, by Sidney Robbins, professor at Columbia University, in a report for AID)

VIII. COMPARISON WITH OTHER PROPOSALS

A. CARANA

In September 1989 Carana Corporation did a pre-feasability for a private Development Finance Company (DFI) in Bolivia, and wrote a project identification document (PID) for the DFI in February 1990. This was the result of recommendations from the Development Associates Study, done in March 1989, and the first mid-term evaluation of the Project by ISTI, finished in August 1988. USAID/Bolivia decided to put the new DFI on hold, since it did not create a permanent institutional structure for the Project.

The pre-feasibility study by Carana indicated that there was a strong possibility of creating a viable, self-sustaining private DFI in Bolivia, using concessionary loan funds, grant and technical assitance from USAID. However, the study pointed to legal, political and technical difficulties in transferring the Project's funds to the private DFI, and therefore recommended that USAID go forward with the private DFI as a new project, separate from the MTCF project.

The recommended PDB differs from Carana's DFI in several ways. The most important is that we feel the UCF/UCP system can be absorbed into the new PDB, in terms of personnel, physical assets, and learning experiences. Unlike Carana, we feel that the UCFs have developed good project identification, evaluation and monitoring skills. They are particularly respected by the ICIs in the less developed regions, where the ICIs depend on them for these services. (ISTI and CARANA consultants did not visit the less developed areas, so did not arrive at the same conclusion.). Also, the new PDB would be completely integrated with FINDES, which would help in attracting foreign and domestic investment. Carana limited its scope of activities to industry and agroindustry; we include other sectors as well (agriculture, mining). PDB will have a small business department specifically tailored to the needs of those borrowers, and will analyze the creation of a guarantee fund exclusively for small business. However, it will also lend to large projects. Carana said it would be focused on small and medium borrowers, but the DFI's average loan would have been $100,000, hardly small in Bolivian terms. (The FOCAS project has an average size loan of $30,000 when the largest loans are excluded, or $60,000 if they are included.) We feel the loans should be for up to ten years, Carana limited them to 3-5 years. We envision a larger shareholder base than Carana. We also will approach other donors (IFC, IIC) to obtain interest in the beginning; Carana limited its funding to USAID only. Carana's DFI would have concentrated lending in the central axis only, our proposed PDB will continue lending in the less developed regions as well.

There are some similarities with Carana's PID; however, which should be kept in mind for the next feasibility study, following on this report. Both studies recommended the creation of a new private, for profit development finance institution, instead of working with the banking system. The financial, institutional and technical constraints are the same in both studies. Carana estimated demand for term credit at

$16.5 million during 1990/91. Both proposals envisioned an initial capital base of $3 million, where ownership would be limited to no more than 5%, and a leverage of 5:1. Carana went so far as to identify potential investors, which hopefully can be contacted again.

B. Comparison with UCF Proposal (FINIRSA)

The main obstacle in the UCF proposal (FINIRSA) is that it does not coincide with the philosophy of the GOB; FINIRSA includes public sector participation, while the GOB has decided to elimate the state's participation in financial institutions. FINIRSA also includes the participation of private sector associations as investors, which would seem to be difficult, if not impossible, based on the statutes of the associations. Also, their capital contribution would be minimal since they have limited funds. They may not be objective as Directors, as they may support loans to their members, instead of basing their decisions on the overall financial condition of the new PDB. In other words, there would be a clear conflict of interest with associations as owners. FINIRSA also assumes that international organizations invest in the new entity, which is not very likely due to the state ownership.

The FOCAS project has been operating like a second tier bank, similar in function to the Development Department of the BCB. Besides operating on the margin of the financial system, it has been supported by the agreement between USAID and the Bolivian Planning Ministry, or with the implicit guaranty of the state, and with subsidized resources (interest rates at 4%), which permit the Project to sustain itself. In the future it is unlikely that this situation can continue, because the policy of the GOB is not to give guarantees, which would make it difficult to capture funds from international agencies. Also, the GOB stated that it will eliminate subsidies that actually exist in development credits. This will be managed in the future under a proposed auction system. Under this new system, the 4% that the UCFs/UCP receive, and the Libor rate that is rediscounted through the ICIs, would not exist, which could cause the system to be unviable.

FINIRSA insists on working with the private banking system as an intermediary in the channeling of resources. We believe that this was one of the major problems with the FOCAS project, due to the lack of ICIs in the less developed regions, the inability of many ICIs to evaluate projects, and their unreasonable collateral requirements.

What we propose instead is a private development bank, which would absorb the experience and capacities of the UCFs and the UCP, especially in terms of identification, evaluation, and monitoring of projects. This PDB would compete with other ICIs in capturing foreign development credit lines, to channel funds directly to the borrowers. It would offer specialized services for small businesses, combined with a strong technical assistance and investment promotion component. This new PDB would have ample regional and national coverage.

IX. TERMS OF REFERENCE FOR PHASE III

Below are suggested terms of reference for Phase III.

A. Feasibility Study

1. Legal framework (what steps are needed to incorporate a Bank)

2. Organizational structure (Staff, responsabilities, authority)

3. Financial proyections (key assumptions, sensitivity analysis, conclusions).

B. Other Issues to be Studied

1. GOB support
   - Privatization of financial system
   - Importance of competition
   - Need for a Private Development Bank
   - Auction System
   - Underwriting of stock (gradual transfer to Private Sector)

2. Private Sector Participation

   - Is the Private Sector really interested in the PDB?
   - Are there 200 shareholders willing to raise $ 3 MM?
   - Is it reasonable to expect a broadly based PDB?
   - active participation of a group of Shareholders at the Board level of the PDB, providing the necessary oversight and supervision of the Bank's performance.

3. Superintendency of Banks

   - Regulations measures (define them)
   - Approvals needed

4. Produce a multidonor proposal

   - Approach other donor agencies to assess interest
   - USAID should take the leadership role?

5. New Banking law

   - Is it feasible to introduce a chapter on Development Bank?

6. USAID Commitment
   - Is there a long term commitment from USAID to develop the PDB?
   - How does it fit in with the mission's financial sector strategy?

C. Staffing Requirements

1. Team Leader
   Must be familiar with the dynamics of the Bolivian banking sector, interest rate policies, and be an effective lobbyist for the PDB.

2. Bolivian lawyer
   Must be familiar with the banking law and incorporating a new financial institution.

3. Management Consultant
   Must have experienced restructuring organizations, reviewing personnel requirements and drawing up new job descriptions.

4. Financial Analyst
   Must have experience analyzing financial statements and projecting alternative financial scenarios for new financial institutions.

D. Timing Considerations

We feel that Phase III could be conducted in approximately 4-6 weeks, and that the mission should begin sometime in September. It is important that both USAID and the private sector approach Phase III with a long term committment.

APPENDIX A

Statement of Work (original)

Statement of Work for Phase I (Memo May 17, 1990)

Statement of Work for Phase II (Memo July 30, 1990)

58

ARTICLE I - TITLE

Second Mid-Term Evaluation of the Market Town Capital Formation Project
Project No. 511-0573

ARTICLE II - OBJECTIVE

The objective of this delivery order is to measure progress toward the attainment of the purpose and outputs of the project, and prepare plans for the institutionalization of the current UCP/UCFs system.

To achieve this purpose the evaluation should determine: a) the performance of the investment finance mechanisms, including norms and regulations; b) the performance of the current institutional structure; c) the achievements of the project purpose and outputs; and d) the options for the institutionalization of the system and a plan for the implementation of the best option.

ARTICLE III - STATEMENT OF WORK

The evaluation will be carried out in two phases.

Phase I

The contractor shall evaluate the performance of the current system and its achievements. Specifically, the contractor shall focus the investigation on the following questions:

a. <u>Findings and conclusions concerning the performance of the investment finance mechanisms</u>.

Is the system of evaluation, approval and disbursement for subprojects performing adequately? Are the norms, conditions, procedures and eligibility criteria set forth in the different implementing documents clearly defined (e.g. Regimen Operativo de Credito) and are they being met? Is the control and monitoring system, for both the banks and the FCUs/PCU, functioning well? Has the system achieved the required volume of lending to cover current and future operating costs? How is the automatic refinancing system performing? What lessons have been learned for the new institution?

b. <u>Findings and conclusions concerning the performance of the current institutional structure</u>.

What are the investment promotion activities being carried out by the FCUs/PCU? What other investment promotion activities could they carry out? To what extent do the FCUs complement the financing activities of the ICIs? Have the FCUs and ICIs helped put together finance packages?

What is the performance of the ICIs under the project? Why do the ICIs use the MTCF credit line instead of other refinancing credit lines? Are there still obstacles which impede a more active participation of the ICIs? Is the UCP effectively managing the portfolio? How effectively is the UCP coordinating activities with the ICIs, UCFs, USAID and PL-480? How important is the role of the organized private sector in the project? What has been the impact of its participation? Why has the private sector not actively participated in all the departments? How did the Regional Development Corporations and the national government support the achievement of the project goal? What lessons have been learned for the new institution?

c. <u>Findings and conclusions concerning the achievement of the project purpose and outputs</u>.

To what extent have project outputs been achieved? Explain the successes and the failures. To what extent have the subprojects chosen for financing contributed to the purpose and goal of the project? Compare ex-ante estimations of impacts with ex-post results. How can the project more effectively achieve the purpose and goal? What impacts has the project had on the regional economy? Has it really created employment, generated foreign exchange, added significant net value and contributed to the use of local goods and services? Has it contributed to increased competition in certain industries or sectors of the economy? Has it helped establish new enterprises? Has the project helped develop subprojects which would not have been developed without its assistance? Has it improved the technology or management of certain industries? Has it had other structural impacts? What impacts has the project had on the banking system? Has the project increased the ability of the banks to engage in long term lending? Has the project decreased the uncertainty and/or risks associated with long term lending? Has the project had an impact on the collateral required for long term lending? What is the quality of the portfolio? What is the performance of disbursements vis-a-vis projections? Is there a rational 1) geographical distribution (secondary vis-a-vis urban areas), 2) sectorial distribution and 3) investor equity participation? How did the project enhance the support of the government for private sector activities? What lessons have been learned for the new institution?

The original project was designed to promote investments in the secondary areas of Bolivia, and specifically excluded lending in urban centers. In January 1989, the project was amended to permit loans to firms located in the three principal urban centers of Bolivia - La Paz, Cochabamba, and Santa Cruz. These projects could only be funded if they had forward and backward linkages to the rural areas. Was this modification in the project purpose necessary in order to increase loan disbursements? Might there have been other mechanisms to increase loan disbursements, while still retaining the rural and semi-urban focus of the project? Would it be feasible and advisable to return to the original project purpose and restrict loans to the rural and semi-urban areas?

Phase II

The contractor will study the options for the institutionalization of the system and design a plan for the implementation of the best option. Specifically, the contractor should focus on the following questions:

a. Review of options for institutionalization.

What are the options for creating, from the system, a permanent institution? In what existing institutions could the program be placed? What are the advantages and disadvantages of the current system? What are the advantages and disadvantages of those options presented in the Development Associates and CARANA studies and the FCUs' proposal to establish Financiera?

b. Design and implementation plan for selected option.

How can this system become a permanent and self-financed institution? What would be the role of the private and public sectors? Design the organizational scheme of the new institution, present an action plan for establishing the institution, and develop financial projections.

The contractor is required to provide in a final report their findings, their conclusions and their recommendations for each phase.

ARTICLE IV - REPORTS

1. Format of the Report

The contractor should prepare a written report containing the following sections:

-Basic Project Identification Data Sheet;

-AID Evaluation Summary form;

-Table of Contents;

-Body of the Report. The report shall follow the format of the statement of work. It should include a description of the country context in which the project was developed and carried out, and provide the information (evidence and analysis) upon which the conclusions and recommendations are based. The length of the body of the report should not exceed 50 pages. Include details in appendices or annexes;

61

-The report should end with a full statement of conclusions and recommendations. Conclusions should be short and succinct, with the topic identified by a short subheading related to the questions posed in the Statement of Work. Recommendations should correspond to the conclusions; whenever possible, the recommendations should specify who, or what agency, should take the recommended actions;

-Appendices. These are to include at a minimum the following:

a) The evaluation Scope of Work;

b) The pertinent Logical Framework, together with a brief summary of the current status/attainment of modified outputs;

c) List of actions taken, and status of actions not yet taken but still considered valid by the evaluation team, based on the recommendations of the first evaluation of the project;

d) A description of the methodology used in the evaluation. Evaluators should recommend a monitoring and evaluation plan (review plan for other Private Sector Office projects for a model to be followed);

e) A bibliography of documents consulted;

f) A draft of the abstract for the AID Evaluation Summary;

g) Other relevant details related to the evaluation and a list of agencies consulted.

2. <u>Submission of Report</u>

The contractor shall submit two reports, one for each of the items of Phase I and Phase II of the Statement of Work. The contractor is required to present the draft report and make an oral presentation to USAID/Bolivia staff and host country counterparts of the draft report five days before the end of the work in each phase. After review by appropriate USAID staff and host country counterparts, all substantive comments and recommendations will be incorporated into the final reports. A clear and bound final version of both reports, in English and Spanish, with 20 copies in each language shall be submitted to Chief, Private Sector Office, USAID/Bolivia, within four weeks after terminating the work in Phase II.

<u>ARTICLE V - TECHNICAL DIRECTIONS</u>

The contractor shall work under the general policy guidance of the USAID/Bolivia Mission Director and/or his designee(s).

62

Technical directions during the performance of this delivery order will be provided by Project Officer pursuant to Section F.3 of the contract.

673

6. Have the guarantees of the commercial banks been reduced for FOCAS projects? Is there a difference between guarantees required by each bank? What incentives need to be introduced to have banks lower their guarantee requirements?

7. What is the level of past due loans in the FOCAS portfolio and the Corporation's portfolio? What type of monitoring system exists for problem loans? What are the guidelines for loan loss provisions and writedowns?

B. Supervision, Monitoring and Control

1. What are the norms and operating documents established by the UCP?

2. How do the UCFs monitor and reduce their risk in the event of a bank failure?

3. How do the UCFs monitor the subprojects? Is the methodology for analyzing subprojects established by UCP used by all of the UCFs?

4. What formal arrangements (legal or otherwise) should be made to bring all of the UCP/UCF system under the supervision of the Superintendency of Banks? Should it be under the supervision of the Central Bank?

5. Is there a need for an independent auditor at UCP?

C. Financial Sustainability

1. What volume of lending is necessary to cover current and future operating costs? Why has it been difficult for Oruro and Potosi to achieve financial sustainability?

2. How does the system support those regions until they are self supporting? Is there a relationship between the skills of the personnel in various UCFs and their ability to sustain themselves? What would be the best mechanism to share in the risk?

3. Is the size of each UCF and the UCP reasonable in terms of personnel, operating costs? What should they be if they increase the portfolio with additional donor funding?

4. Will the system be self supportive after AID funding terminates in July 1991?

MEMORANDUM

To: D. Jessee/M. Hoyos
USAID/Bolivia

From: MSI Evaluation Team (E. Pereira, J. Trigo, E. Evans)

Re: Revised Scope of work for Mid-term evaluation
MTCF/FOCAS Project

Date: May 17, 1990

We have revised the original scope of work in the following Sections I, II and III. This was based on information obtained at USAID/Bolivia, and during a strategic planning exercise with the managers of the UCFs and the Director of the UCP. We have also included our Evaluation Methodology in Section IV, and a Timeframe for completion of both Phases I and II in Section V. This scope of work only includes Phase I, however.

I. THE INVESTMENT FINANCE MECHANISM (E. Evans)

A. The Investment Finance Mechanism

1. What are the sources of funds for FOCAS, and what are the conditions of the loans/grants (USAID, PL480, Corporations) that will affect its future funding?

2. How has the financing mechanism improved over time with the changes in the original agreement?

3. Has the automatic refinancing mechanism increased disbursements in all regions? Is the FOCAS line disbursed more efficiently than other foreign lines channeled through the Central Bank? Has it introduced more risk in the loan portfolio?

4. Why was the program amended to included working capital loans? What percentage of loans were made for working capital only, and what percentage for fixed investment? Should the FOCAS line finance working capital? Were the conditions in the "Regimen de Credito" followed by banks making working capital loans?

5. What improvements have been made in the evaluation of projects? Does the evaluation methodology mitigate risk in the loan portfolio? What is he eligibility criteria?

II. THE INSTITUTIONAL SYSTEM (E. Pereira)

A. Overview of the existing system

1. How effectively is the UCP coordinating and supervising the component's activities and managing the portfolio?

2. What should be the relationship between UCP/UCF/ICI and donors in terms of responsibility, approvals, reporting, decision-making? Who has control over what?

3. What are the legal differences in terms of ownership, claim on DDC-FOCAS portfolio? Can the two be fully integrated?

4. What has been the role of the private sector?

5. Who is using the system? By regions?

B. Promotional Activities

1. What is generally understood when we talk about an investment promotion program?

2. What is the trade-off between sustainability and investment promotion?

3. Should the UCFs carry out investment promotion activities in the future? If yes, what investment promotion activities can they carry out?

4. Who are the beneficiaries of the investment promotion activities?

5. Are they presently promoting or could they promote new alternative activities?

6. Is there a relationship between promotional activities and volume of lending?

C. Financing Activities

1. How do the UCFs encourage more lending in ICIs?

2. What are the comparative advantages of the MTCF line vis-avis other refinancing lines?

3. Are there alternative sources of financing for the sub-borrowers?

4. How have the UCFs reached the smaller and secondary cities the ICIs haven't by themselves?

hh

5. Should we continue lending in the big cities: La Paz, Cochabamba, Sta Cruz?

III. ACHIEVEMENT OF THE PROJECT, PURPOSE AND OUTPUTS (J. Trigo)

A. Impacts on the Economy

1. How much direct and indirect employment was created, and what was the employment creation per unit of capital?
2. How much foreign exchange has been generated in the traditional and non traditional sectors?

3. What are the backward linkages generated by this project?

B. Impacts on the Financial Markets

1. Would long term credit be available to small and medium businesses and agroindustry producers if the FOCAS line was no longer available?

2. Is there a reasonable distribution of the FOCAS credit line by regions and economic sectors?

3. How does the current high interest rate environment hinder productive private sector investment, and the project in particular?

IV. TIME FRAME

A. Phase I (4 weeks) 5/14/90 to 6/9/90

1. Team Orientation and Strategic Planning Meetings (1 Week)

2. Conduct of Phase I (3 Weeks)

B. Phase II (4 weeks) 6/25/90 to 7/20/90 tentatively

1. Review of Phase I, Orientation and Information Meetings (1 week)

2. Conduct of Phase II (3 weeks)

V. EVALUATION METHODOLOGY

A. Clarify Scope of Work
B. Establish priority questions
C. Assign data collection tasks
D. Collect data
E. Analyze data
F. Develop findings, conclusions, recommendations
G. Debriefing and feedback
H. Write reports

Concurrence of: M. Zalles
D. Jessee
M. Hoyos

cc: USAID: R. Kramer, D. Jessee, M.Hoyos, L.Downing,
E.Kadunc, D.Carroll
UCP: M. Zalles
MSI: L. Cooley

MEMORANDUM

DATE: July 30,1990

TO: Miguel Hoyos, Private Sector Office, USAID/Bolivia

FROM: MSI Evaluation Team (J. Trigo, E. Evans) J. Trigo E. Evans

SUBJECT: Revised Scope of Work for Phase II of the Second Mid-Term evaluation of MTCF/FOCAS Project

Based on the decision made by the Mission that during Phase II of the FOCAS evaluation the MSI Evaluation Team should concentrate its efforts to analyze the options to institutionalize the current UCP/UCFs system, we propose the following revised scope of work:

Analyze the critical considerations for a permanent institutional structure of the UCP/UCFs system. What are the options for creating a permanent institution? What are the advantages and disadvantages of these options? Which, and why, is the most preferred option? Define the role of the new institution, its organizational scheme, the requirements, conditions and constraints to establish it, the participation of the private and public sectors and its relationship to other financing and/or investment promotion programs. Compared the preferred option with the proposals presented by CARANA and the UCFs. Suggest terms of reference to implement the selected option, pointing out the issues to be studied, expertise required and timing considerations.

Concurrence of: ______ Miguel Hoyos, USAID/Bolivia

______ Miguel Zalles, UCP

APPENDIX B

Project Data Sheet

AGENCY FOR INTERNATIONAL DEVELOPMENT

PROJECT DATA SHEET

1. TRANSACTION CODE: A (A = Add, C = Change, D = Delete) — Amendment Number: ____ — DOCUMENT CODE: 3

2. COUNTRY/ENTITY: Bolivia

3. PROJECT NUMBER: 511-0573

4. BUREAU/OFFICE: LAC 05

5. PROJECT TITLE (maximum 40 characters): Market Town Capital Formation

6. PROJECT ASSISTANCE COMPLETION DATE (PACD): MM 07 DD YY 91

7. ESTIMATED DATE OF OBLIGATION (Under "B." below, enter 1, 2, 3, or 4)
A. Initial FY 86 B. Quarter 4 C. Final FY 91

8. COSTS ($000 OR EQUIVALENT $1 =)

A. FUNDING SOURCE	First FY 86: B. FX	C. L/C	D. Total	Life of Project: E. FX	F. L/C	G. Total
AID Appropriated Total						
(Grant)	(2,776)	(150)	(2,926)	(3,256)	(244)	(3,500)
(Loan)	(7,154)	(-)	(7,154)	(15,000)	(-)	(15,000)
Other U.S. 1.						
Other U.S. 2.						
Host Country	-	1,400	1,400	-	6,900	6,900
Other Donor(s) (Private Sector)	-	3,300	3,300	-	16,500	16,500
TOTALS	9,930	4,850	14,780	18,256	23,644	41,900

9. SCHEDULE OF AID FUNDING ($000)

A. APPROPRIATION	B. PRIMARY PURPOSE CODE	C. PRIMARY TECH. CODE 1. Grant	C. 2. Loan	D. OBLIGATIONS TO DATE 1. Grant	D. 2. Loan	E. AMOUNT APPROVED THIS ACTION 1. Grant	E. 2. Loan	F. LIFE OF PROJECT 1. Grant	F. 2. Loan
(1) ARDN	100	190	190			2,206	3,750	3,500	15,000
(2)									
(3)									
(4)									
TOTALS						2,206	3,750	3,500	15,000

10. SECONDARY TECHNICAL CODES (maximum 6 codes of 3 positions each)

11. SECONDARY PURPOSE CODE

12. SPECIAL CONCERNS CODES (maximum 7 codes of 4 positions each)
A. Code
B. Amount

13. PROJECT PURPOSE (maximum 480 characters)

To increase the level of productive private sector investment in Bolivia's rural and semi-urban areas.

14. SCHEDULED EVALUATIONS
Interim MM YY 09 88 | MM YY | Final MM YY 05 91

15. SOURCE/ORIGIN OF GOODS AND SERVICES
Grant: 000 | Loan: 941 | Grant/Loan: Local | Other (Specify)

16. AMENDMENTS/NATURE OF CHANGE PROPOSED (This is page 1 of a ____ page PP Amendment)

The USAID Controller has reviewed the financing procedures described herein and hereby indicates his concurrence.

Steven G. Liapis, Controller

17. APPROVED BY
Signature
Title: David A. Cohen, Director, USAID/Bolivia
Date Signed MM DD YY: 07 21 86

18. DATE DOCUMENT RECEIVED IN AID/W, OR FOR AID/W DOCUMENTS, DATE OF DISTRIBUTION
MM DD YY

AID 1330-4 (8-79)

APPENDIX C

Logical Framework

72

ANNEX 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

(INSTRUCTION: THIS IS AN OPTIONAL FORM WHICH CAN BE USED AS AN AID TO ORGANIZING DATA FOR THE PAR REPORT. IT NEED NOT BE RETAINED OR SUBMITTED.)

Life of Project:
From FY 1986 to FY 1991
Total U.S. Funding $18,500,000
Date Prepared: June 15, 1986

Project Title & Number: MARKET TOWN CAPITAL FORMATION

PAGE 1

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Program or Sector Goal: The broader objective to which this project contributes: To achieve a higher standard of living through increased employment and greater production in Bolivia's rural and semi-urban areas.	**Measures of Goal Achievement:** In Bolivia's rural and semi-urban areas: . Employment statistics have improved (jobs have been created). . Business and farm output has increased. Levels of household consumption have risen. . Levels of business investment have risen.	. INE National statistics. . Local studies done by DDCs and regional banks. . Banking sector statistics.	**Assumptions for achieving goal targets:** . Political stability obtains in Bolivia. . Bolivia continues the economic improvement process begun in August 1985. . GOB policies on foreign exchange, private sector activites, exports and imports and currency reform remain positive. . No natural disasters of overwhelming proportion (like "El Niño") distort the development process.

73.

ANNEX 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY 1986 to FY 1991
Total U.S. Funding $18,500,000
Date Prepared: June 15, 1986

Project Title & Number: MARKET TOWN CAPITAL FORMATION

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Project Purpose: To increase the levels of productive private sector investment in Bolivia's rural and semi-urban areas.	**Conditions that will indicate purpose has been achieved: End of project status.** . Private sector investments have increased. . Intermediate Credit Institutions performing more effectively, and with larger development loan portfolios. . UCFs working well. . UCF Credit Fund established and functioning. . Variety of types of investors have taken new equity positions in private sector ventures. . Agricultural and agribusiness enterprises show greater production, higher productivity and/or better quality in their outputs.	. Local bank statistics, and DDC studies. . Participating ICI loan evaluations and follow up. . UCF subproject evaluation data. . Mid-term and EOP project evaluations.	**Assumptions for achieving purpose:** 1. Bolivia maintains political stability. 2. Economic stability is obtained and maintained in Bolivia. 3. GOB policies supporting the private sector continue.

ANNEX 1

AID 1020-28 (7-71)
SUPPLEMENT 1

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project:
From FY 1986 to FY 1991
Total U.S. Funding $18,500,000
Date Prepared: June 15, 1986

Project Title & Number: MARKET TOWN CAPITAL FORMATION

PAGE

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Outputs:	Magnitude of Outputs:		Assumptions for achieving outputs:
1. Investments which are beneficial both socio-economically and financially, totalling approximately $37.5 million, are undertaken.	1. $21 million in project loans made which finance investments worth $37.5 million.	. PCU, UCF, and ICI records.	1. There is continued, effective credit demand.
2. UCF Credit Fund is established.	2. One, integrated into new development finance institution, or operating under institutionalized PCU.	. Internal and external audits.	2. AID and GOB disburse loan funds promptly.
3. ICIs' rural lending operations have improved.	3. Up to 12.	. Mid-term and EOP evaluations.	3. The ICIs participate actively in the project.
4. All UCFs are fully operational.	4. 8.		4. Appropriate PCU and UCF staff and operating cost support are available.
			5. DDC and UCF relationships remain productive.
			6. UCF's and the PCU retain their semi-autonomous status.

ANNEX 1

PROJECT DES[illegible]N SUMMARY
LOGICAL F[illegible]AMEWORK

Life of Project:
From FY 1986 to FY 1991
Total U.S. Funding $18,500,000
Date Prepared: [illegible]

Project Title & Number [illegible]

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS		MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Inputs:	Implementation Target (Type and Quantity)			Assumptions for providing inputs:
	US$(000)	H.C.		
1. Investment Financing	14,500	23,000	. USAID accounting documents.	Funds are made available by PL-480 Title III and USAID and ICIs.
2. Technical Assistance/Training	1,725	-	. PL 480 Title III accounting documents.	
3. Project Support/Costs	1,455	400	. PCU and UCF reports.	
4. Evaluations/Audits	171	-	. Internal and external audits.	
5. Contingencies	649	-		
TOTAL	18,500	23,400		

APPENDIX D

List of Actions Taken

Amendment No. 6

USAID Letter to Planning Ministry (20 Octubre 1989)

Project Implementation Letter (December 28, 1989)

OUTPUTS OF THE FIRST FOUR YEARS OF PROJECT

Based on Amendment No. 6

1. Private sector investments

Private investments in productive sectors increased substantially in rural and semi urban areas, due to the near full utilization of the FOCAS credit line.

2. Self sufficient system which will finance and promote private sector investment

The system is not completely self sufficient, due to deficits in Potosi and Oruro, which will continue for some time.

3. Five improved and strengthened ICIs

No more than three ICIs have developed the capacity for channeling development credit throughout Bolivia.

4. The UCFs will have improved their capability to promote investments

The UCFs only have a limited capacity to promote investments. Investment promotion has not been an achievable objective, given problems with previous technical assistance, and trade offs required in implementation.

5. Three functioning priority market towns

There are only two market towns which have benfitted under this Project - Camargo and Riberalta.

78

Donación AID No.511-0573
AID Grant No.511-0573
Préstamo AID No 511-T-071
AID Loan No 511-T-071

ENMIENDA No.6
AMENDMENT No.6

CONVENIO DE PRESTAMO Y DONACION
LOAN AND GRANT AGREEMENT

ENTRE
BETWEEN

LA REPUBLICA DE BOLIVIA
THE REPUBLIC OF BOLIVIA

Y
AND

LOS ESTADOS UNIDOS DE AMERICA
THE UNITED STATES OF AMERICA

PROYECTO FORMACION DE CAPITALES EN AREAS SECUNDARIAS
MARKET TOWN CAPITAL FORMATION PROJECT

FECHA: 16 de febrero de 1989
DATE: February 16, 1989

ENMIENDA No.6

La República de Bolivia ("Bolivia") y los Estados Unidos de América, actuando por intermedio de la Agencia para el Desarrollo Internacional ("A.I.D."), suscribieron un Convenio de Proyecto denominado "Proyecto de Formación de Capitales en Areas Secundarias" en fecha 23 de julio de 1986 (el "Convenio"). Dicho Convenio fue enmendado el 4 de septiembre de 1986, el 28 de febrero de 1987, el 27 de mayo de 1987, el 25 de julio de 1986 y el 30 de septiembre de 1988.

Bolivia y A I.D. acuerdan además modificar dicho convenio como sigue:

1. La primera frase de la Sección 2 1 se modifica para que diga lo siguiente

> "El propósito del Proyecto, que se describe con mayor detalle en el Anexo 1, es incrementar el nivel de inversión productiva del sector privado en las regiones rurales y urbanas de Bolivia".

2. Se incluye una nueva Sección 8.6 al Convenio de Donación de Proyecto como sigue.

> "Sección 8.6. Violación de la Ley de EE UU.
>
> A.I.D. se reserva el derecho de retener a su propio criterio, cualquier desembolso que podria ser una violación a cualquier legislación, ley, o regulaciónes que gobierna a A.I.D.".

3. Se suprime en su totalidad el Anexo I, Sección I-A y se lo sustituye con lo siguiente:

AMENDMENT No.6

The Republic of Bolivia ("Bolivia") and the United States of America, acting through the Agency for International Development ("A I.D ") entered into a Project Agreement entitled "Market Town Capital Formation Project," dated July 23. 1986 ("Agreement"). Said Agreement was amended on September 4, 1986, February 28, 1987; May 27, 1987; July 25, 1986; and September 30, 1988

Bolivia and A.I.D. further agree to amend this agreement as follows.

1. The first sentence of Section 2.1. is amended to read as follows.

> "The purpose of the Project, which is further described in Annex 1, is to increase the level of productive private sector investment in Bolivia's rural and urban areas

2. A new Section 8.6 is hereby added to the Project Grant Agreement as follows:

> Section 8.6. Violation of U S Law.
>
> A.I.D. retains the right to withhold, at its own discretion, any disbursement which would be in violation of any legislation, law, or regulations governing A.I.D."

3. Annex I, Section I-A has been deleted in its entirety and the following substituted in lieu thereof

"El objetivo del Proyecto es lograr un mejor nivel de vida, mediante el aumento de fuentes de trabajo y producción, en Bolivia. El propósito del Proyecto es incrementar el nivel de las inversiones productivas del sector privado en las regiones rurales y urbanas de Bolivia. Al final del proyecto, es decir en la Fecha de Terminación del Convenio del Proyecto (23 de julio de 1991), deberán existir las siguientes condiciones (EOPs):

1. Las inversiones del sector privado en empresas productivas en toda Bolivia habrán aumentado considerablemente.

2 Las Instituciones Crediticias Intermedias (ICIs) se desempeñarán con mayor efectividad y sus carteras de préstamos para el desarrollo habrán aumentado sustancialmente.

3. Las Unidades Crediticias Financieras habrán desarrollado importantes actividades de promoción de inversiones.

4. Se habrá establecido y estará en funcionamiento un sistema autosuficiente para financiamiento y promoción de inversiones.

El Proyecto tendrá cuatro resultados principales:

1) Inversiones productivas y de servicios relacionados del sector privado por un total aproximado de $US32 millones, que incrementen la producción y el empleo en áreas rurales y semiurbanas.

"The goal of the Project is to achieve a higher standard of living, through increased employment and production, in Bolivia. The purpose of the project is to increase the level of productive private sector investment in Bolivia's rural and urban areas. At the end of the Project, that is by the Project Agreement Completion Date (July 23, 1991), the following conditions (EOPS) will exist:

1. Private sector investments in productive enterprises throughout Bolivia will have increased significantly.

2. Intermediate Credit Institutions (ICIs) will be performing more effectively and their development loan portfolios will have increased substantially.

3. The Unidades Crediticias Financieras will have developed important investment promotion activities.

4. A self-sufficient system for financing and promoting investments will be established and functioning.

The Project will have four major outputs:

1) Productive and services related private sector investments totalling approximately US$32 million to increase production and employment in rural and semi-urban areas.

2) Un sistema autosuficiente que financiará y promoverá inversiones del sector privado.

3) Mejoramiento y fortalecimiento de cinco ICIs para una mejor administración de sus programas de crédito de fomento en toda Bolivia.

4) Las Unidades Crediticias Financieras habrán mejorado su capacidad para promover inversiones.

5) Estarán en funcionamiento tres centros prioritarios de mercado como proyectos piloto.

Con excepción de lo que se enmienda expresamente mediante la presente, el Convenio permanece en plena vigencia y efecto.

EN TESTIMONIO DE LO CUAL, la República de Bolivia y los Estados Unidos de América, cada cual actuando por intermedio de su representante debidamente autorizado, suscriben la presente Enmienda No. 6 al Convenio de referencia, en sus nombres y en la fecha y año indicados más arriba.

2) A self-sufficient system which will finance and promote private sector investments.

3) Five improved and strengthened ICIs for better management of their development lending programs throughout Bolivia

4) The Unidades Crediticias Financieras will have improved their capability to promote investments.

5) Three functioning priority market town pilot projects.

Except as amended hereby, the Agreement remains in full force and effect.

IN WITHNESS WHEREOF, THE Republic of Bolivia and the United States of America, each acting through its duly authorized representative, have caused this Amendment No.6 to the Agreement to be signed in their name and delivered as of the day and year first above written.

REPUBLICA DE BOLIVIA
REPUBLIC OF BOLIVIA

Lic Fernando Romero Moreno
Ministro de Planeamiento y Coordinación
Minister of Planning and Coordination

ESTADOS UNIDOS DE AMERICA
UNITED STATES OF AMERICA

G. Reginald van Raalte
Director
USAID/Bolivia

595L-0896L

Fecha/Date: February 16, 1989

97

UNITED STATES AID MISSION to BOLIVIA
c/o American Embassy
La Paz, Bolivia

USAID - BOLIVIA
APO MIAMI 34032

Telephones: 350120, 350251
Casilla 673
La Paz, Bolivia

20 de octubre de 1989
PS-A-171-89

Señor
Lic. Enrique García Rodríguez
Ministro de Planeamiento y
Coordinación
Presente

Estimado señor Ministro:

Mediante la presente tengo a bien informarle que USAID/Bolivia ha concluido el informe de la primera fase del Estudio sobre la Institución Financiera de Desarrollo, realizado por la firma consultora CARANA Corp.

En base al análisis del informe presentado por la mencionada consultora, USAID/Bolivia tomó conocimiento de varios problemas fundamentales respecto al establecimiento y financiamiento de una Financiera privada. Además, creemos que aún existen problemas pendientes de solución respecto a las opciones de largo plazo para la institucionalización del Proyecto FOCAS. Por lo tanto, nos gustaría discutir las conclusiones del estudio de la Financiera, además de las opciones de institucionalización para el Proyecto FOCAS, tan pronto como así usted lo crea conveniente. Con este propósito, adjunto a la presente para su conocimiento una copia del resumen del informe presentado por los consultores.

Entretanto, y dada la importancia de utilizar el saldo de los recursos del Convenio de Préstamo 511-T-071 del Proyecto FOCAS para cumplir con los objetivos prioritarios de desarrollo que tiene el Gobierno, proponemos suspender temporalmente nuevos desembolsos para el financiamiento de inversiones bajo el mencionado proyecto. Esta recomendación no implica una paralización de las actividades del Proyecto FOCAS, las cuales pueden continuar mientras el Gobierno tome una decisión respecto a los problemas mencionados anteriormente. Con este propósito, estamos dispuestos a colaborar en las acciones que el Gobierno emprenderá en relación a la institucionalización del Proyecto FOCAS.

En espera de su respuesta, saludo a usted atentamente.

G. Reginald van Raalte
Director

..ITED STATES AID MISSION to BOLIVIA
c/o American Embassy
La Paz, Bolivia

PS. 4

USAID - BOLIVIA

Telephones: 350120, 350251
Casilla 673
La Paz, Bolivia

28 de diciembre de 1989

Señor
Lic. Enrique Garcia Rodriguez
Ministro de Planeamiento y
Coordinación
Presente

Señor
Gaston Martinic Reyes
Director
Unidad de Coordinación de Proyectos
Presente

Estimados señores:

Ref: Préstamo AID No. 511-T-071
Donación AID No. 511-0573
Proyecto Formación de Capital
en Areas Secundarias (FOCAS)
Carta de Implementación No. 71

El propósito de la presente Carta de Implementación es dar respuesta a su carta No. 5800, de fecha 30 de noviembre de 1989. En esta carta se solicita que USAID/Bolivia reanude desembolsos bajo el proyecto de referencia para financiar subproyectos aprobados por las UCFs. También se solicita que se lleve a cabo una evaluación y se tome una determinación respecto a las medidas a ser adoptadas para institucionalizar el actual sistema UCP/UCFs.

Mediante la presente, USAID/Bolivia conviene reanudar desembolsos y que el proyecto FOCAS no emita más Certificados de Elegibilidad para

December 28, 1989

Mr. Enrique Garcia Rodriguez
Minister of Planning and
Coordination
La Paz

Mr. Gastón Martinic Reyes
Director
Projects Coordination Unit
La Paz

Gentlemen:

Ref: AID Loan No. 511-T-071
AID Grant No. 511-0573
Market Town Capital
Formation Project
Implementation Letter No. 71

The purpose of this Implementation Letter is to respond to letter No. 5800, dated November 30, 1989. In this letter, it is requested that USAID/Bolivia resume disbursements under the referenced project to finance subprojects approved by the UCFs. It is also requested that an evaluation be carried out and that a determination be made as to the measures to be taken to institutionalize the current UCP/UCFs system.

USAID/Bolivia, hereby, agrees to resume disbursements and that the FOCAS Project not issue any more Certificates of Eligibility for new nuevos subproyectos dado el elevado número ya emitido. También recomendamos que el Proyecto FOCAS reserve US$3 millones de los fondos de préstamo ($US1,9 millones de fondos de AID y $US1,1 millones de fondos de PL-480). Estos fondos no serán desembolsados hasta después de la conclusión de la evaluación, y que sus recomendaciones incluyendo aquellas concernientes a la institucionalización del fondo, sean implementadas.

También estamos de acuerdo en llevar a cabo una evaluación para determinar el desempeño del actual sistema y los ajustes que sean necesarios. Esta evaluación también debería estudiar las opciones para institucionalizar el fondo. Este trabajo será estrechamente coordinado con la UCP, las UCFs y el sector privado.

Aprovecho la oportunidad para informarle que de acuerdo a las recomendaciones del Sr. Jorge Urquidi Barrau, Subsecretario de Inversiones Públicas y Cooperación Internacional, estamos coordinando las acciones necesarias para llenar las vacancias de la UCP por medio de competencia abierta, siguiendo los procedimientos establecidos en el proyecto. Entre las posiciones a ser llenadas está la del Director del Proyecto FOCAS. Esta nueva posición consolida la del Director de la UCP y la del Jefe de FOCAS, debido a la transferencia del Proyecto Organizaciones Agrícolas Privadas al Ministerio de Asuntos Campesinos y Agropecuarios. USAID/Bolivia se reserva el derecho de aprobar los candidatos seleccionados para cada posición, quienes deben cumplir con los requerimientos minimos establecidos para cada posición.

subprojects given the already large number issued. We recommend also that the FOCAS Project reserve US$3 million in subproject loan funds (US$1.9 million in funds from AID and US$1.1 million in funds from PL-480). These funds will not be disbursed until after the evaluation is completed, and its recommendations, including those concerning institutionalization of the fund, are implemented.

We also concur in carrying out an evaluation to determine the performance of the current system and any adjustments which are required. This evaluation should also study the options for institutionalization of the fund. This work will be closely coordinated with the UCP, the UCFs, and the private sector.

We take this opportunity to inform you that in agreement with the recommendations of Mr. Jorge Urquidi Barrau, Subsecretary of Public Investments and International Cooperation, we are coordinating the actions needed to fill the vacancies in the UCP through open competition, following the procedures established for the project. Among the positions being filled is that of the Director of the FOCAS Project. This new position consolidates that of the UCP Director and the FOCAS Chief, due to the transfer of the Private Agricultural Organizations Project to the Ministry of Campesino Affairs and Agriculture. USAID/Bolivia reserves the right to approve the candidates selected for each position, each of whom must meet the minimum requirements established for each position.

Es nuestro deseo de que la implementación de todas estas actividades permitirán continuar la labor del Proyecto FOCAS en una forma ordenada para asi alcanzar el objetivo y el propósito del proyecto.

Sin otro particular, saludo a usted atentamente.

We hope that the implementation of all these actions will permit the FOCAS Project to continue with its activities in an orderly manner to achieve the project goal and purpose.

Sincerely,

F. Wayne Tate

F. Wayne Tate
Director a.i.

3501/35021

.91

APPENDIX E

METHODOLOGY FOR THE MISSION

Phase I

A. Clarify Scope of Work

B. Establish Priority Questions (Memo dated May 17 to USAID/Bolivia)

C. Assign data collection tasks

E. Evans	- Investment Finance Mechanism	
	- Financial Sustainability	
E. Pereira	- Institutional Framework	
	- Project Background and Objectives	
J. Trigo	- Socioeconomic Impact	
	Bolivian Economy and Financial Market Overview	

D. Collect Data

E. Analyze Data

F. Develop findings, conclusions, and recommendations

G. Debriefing and feedback (Memo dated June 8 to USAID/Bolivia)

H. Write Reports

METHODOLOGY FOR ASSESSING THE SOCIOECONOMIC IMPACTS

The quantitative measurement of the impact has been realized by taking into account the information presented by the UCF's along with a simplified method of measuring the macroeconomic effects contained in the document completed by PREALC, titled "Impacto Económico de los Proyectos Públicos". The qualitative analysis is the culmination of samples taken of the project nationwide, the samples being completed by visiting consultants. The department of Pando is not included.

Application of the methodology involves three phases:

(i) measurement of the direct and indirect effects of investment on the product. This effect is measured by the increase in demand and the net foreign exchange generated by the project in the investment and operation phase, and the indirect impact on industries or other economically active sectors which provide national input to the financed project.

(ii) measurement of the increase in employment associated with the increase in the product. This step is completed through the assessment of the employment coefficients and modifications over time due to increments in productivity.

(iii) measurement of the net foreign exchange generated by the project in both the execution phase and the operation phase.

MONITORING AND EVALUATION

The FOCAS Project does not have within its institutional structure a program of monitoring and evaluation. This is due in part to the absence of an internal auditing department which would conduct an expost evaluation based on pre-established guidelines. Also, there have been no goals or objectives established on an annual basis that the Project was supposed to complete. Therefore, the Board of Directors could not compare the planned with the actual results. This has been even more difficult due to the high degree of autonomy of each of the UCFs, and the UCP does not have direct authority.

APPENDIX F

BIBLIOGRAPHY

Project Documents

USAID Market Town Capital Formation Project Paper

Loan and Grant Agreement July 23, 1986

Amendment No. 6 to Loan and Grant Agreement - February 16, 1989

UCP/UCF Operating Documents

FOCAS - Informe de Actividades - Oct. 1, 1986 - Sept. 30, 1989

Information about types of projects, level of investment, and social impact

Propuesta para la Constitucion de la Financiera de Inversiones Regionales S.A.M., Septiembre 1988

Complementacion a la Propuesta para la Constitucion de la Financiera Nacional de Inversiones Regionales (FINIRSA),
Abril 1988

Regimen de Credito, Marzo 27, 1989

Regimen Financiero, May 16, 1989

(Propuesta) Fondo de Credito de las UCFs - Regimen de Credito

(Propuesta) Fondo de Credito de las UCFs - Regimen Financiero

(Propuesta) Carta de Entendimiento para Implementar Proyectos con Recursos del Programa Formacion de Capital en Areas Secundaries y Establecer el Fondo de Credito de las UCFs.

Plan Consolidado de Inversiones, Julio/89 a Junio 90

Guia para la Elaboracion de Informes de Evaluacion

Programa de Seguimiento y Control de Proyectos (UCF Chuq.)

FONDESA (UCF Chuquisaca), Memoria Anual 1986

Miscellaneous Reports

PL480 - Flow Diagram of Activities

Legal Opinion from Mostajo & Gutierrez, May 14, 1990 on Supervision of FOCAS by Superintendency of Banks

Development Associates - Study of Institutional Options, May 1989

ISTI - Final Evaluation of Corporations Project and Mid Term Evaluation of MTCF Project, September 1988

Carana Corporation - Bolivian Development Finance Institute, February 1990

Balance Sheets for 1989 of each UCF

Superintendencia de Bancos

- Boletines Informativos, Dec. 1989, Feb. and March 1990

Banco Central de Bolivia - Gerencia de Desarrollo

- Movimiento Crediticio de Lineas Refinanciados para el sector Privado
- Carta Informativa No. 8, Marzo 1990
- Boletin Estadistico No. 264

Ministerio de Planificacion

- Evaluacion de los Impactos de Proyectos de Inversion Publica

APPENDIX G

EVALUATION ABSTRACT

The Market Town Capital Formation Project (FOCAS) was designed to increase the level of productive private sector investment in Bolivia's rural and semi-urban areas. This would increase production, create employment and generate economic growth. Although there were seven market towns initially identified, only two, Riberalta and Camargo, received financing under the project. This geographic restriction resulted in a project substantially behind schedule in the first three years. An earlier evaluation conducted by ISTI in 1988 (subsequently rejected by USAID Bolivia due to lack of objectivity) recommended that the markets and uses for the credit be modified to increase disbursements, as the project did not have a large enough portfolio to sustain itself based on interest. As a result, the project was amended in February 1989 to include the cities of Cochabamba, Santa Cruz and La Paz, and also to allow for working capital lending. This mid-term evaluation covers the period from July 1986 through June 1990. The evaluators visited eight regions of the country to meet the UCFs, obtain the private sector and the government's view, and visit several projects. There is one year remaining in the project. As a result of the amendment, all of the funds have been committed. The major findings and conclusions are:

Conclusions

The Project has achieved:

- The highest socioeconomic impact in terms of creating employment, increasing production and encouraging non-traditional exports in the less developed regions.
- Employment generation in the small and medium businesses, and export-oriented projects, in particular.
- Full disbursement of available funds one year before PACD.
- Better regional distribution that other Central Bank credit lines.
- Improvement of the capabilities of the UCFs.

The Project:

- Did not directly address the constraints to increasing capital formation in secondary market towns. Instead, the amendment changed the project to emphasize sustainability.
- Has channeled funds to some large projects which generate little employment.
- Has lent working capital for medium and large projects which could have obtained financing from commercial banks.
- Has not achieved its objective to be decentralized. Some of the functions overlap, such as project evaluation.
- Has not fostered the high level of cooperation needed with the ICIs, in terms of reducing/being more flexible on collateral requirements, or to lend their own funds,
- Was not flexible enough to accommodate different terms, and also to anticipate inevitable rescheduling.

Recommendations for the last year of the Project

* Emphasize lending to small and medium projects, and export oriented projects, in less developed regions of the country.

* Carry out pending administrative matters to the project, such as: reschedule problem loans, write down the DDC portfolio, consolidate accounting systems, coordinate efforts with the Superintendency of Banks, and redistribute portfolio to less developed regions.

* Improve the participation of ICIs by strengthening their development departments in project evaluation and supervision, by encouraging decentralization of decision-making, and by requiring more flexibility on guarantees.

* The private sector should have a majority participation on the Board of Directors of the UCFs to encourage transparency.

* Provide technical assistance for investment promotion, marketing and economic studies.

* All project evaluations and credit analysis should be done by the ICIs.

* Before PACD, each UCF should decide whether it wants to become a legitimate financial institution (under supervision), or an investment promotion unit.

Recommendations for Creating a Permanent Institutional Structure

* There is general consensus that new financial intermediaries are needed to introduce competition to the banking system.

* There is a need for a private development bank (PDB) to address the unmet demand for long term credit in Bolivia, especially with the closing of State banks.

* The GOB does not intend to be an owner in the financial sector, therefore the proposed PDB would be private, for profit, with a wide shareholder base.

* The PDB would initially have three core departments: project financing (for medium and large businesses), foreign trade, and small business. The PDB would be multisectorial.

* The UCP/UCF system could be absorbed into the small business department of the new PDB. This would include absorbing the personnel, loan portfolio, fixed assets, and learning experiences as much as possible.

* The PDB would be complemented by a separate project, an investment promotion program called FINDES, which would conduct marketing studies and help attract foreign investment.

Lessons Learned

- There should not be a multiplicity of objectives, such as supporting secondary areas vs. financial sustainability, or financial intermediation vs. investment promotion, which cause confusion and require tradeoffs in implementation.

- AID should ensure any type of financial institution it creates be subject to adequate supervision and control (by the Superintendency of Banks, and subject to regular internal audits), to contribute to institutionalization after PACD.

- The fee structure for UCFs throughout the country should be more flexible to accommodate different stages of development and risk. Also, investment financing projects will always need to have clear guidelines for rescheduling.

- Rash decisions to suspend project funds may undermine the Project and create disrespect for AID's work in the financial sector.

APPPENDIX H

LIST OF PERSONS, AGENCIES CONTACTED

Region/Name/Project	Organization	Position
LA PAZ		
US GOVERNMENT		
van Raalte, R.	USAID	Director
Kramer, Robert	USAID	Deputy Director
Jessee, David	USAID	PSO/Acting Chief
Rosenberg, Rich	USAID	PSO/Chief (8/90)
Hoyos, Miguel	USAID	FOCAS Project Officer
Davison, John	USAID	Controller
Kadune, Ed	USAID	Chief, PD&I Office
McIntyre, D.	USAID	Chief, ARD Office
Tate, Wayne	USAID	Chief, DPO Office
BOLIVIAN GOVERNMENT		
Boada, Raul	Central Bank	President
Knaudt, Susana	Central Bank	Manager, Devel. Dept.
Barbery, Rosendo	Super. of Banks	Asst. Superintendent
Rosales, Ramon	Super. of Banks	Advisor
Blanco, David	Finance Ministry	Minister
Garcia, Enrique	Planning Ministry	Minister
Urquidi, Jorge	Planning Ministry	Subsecretary
Brockman, Carlos	PL480	Executive Secretary
Noda, Jorge	PL480	Financial Manager
UCP		
Zalles, Miguel	UCP	Director
Beltran, Arturo	UCP	Financial Manager
Camberos, Antonio	UCP	Manager,Promotions
Kreidler, Lita	UCP	Asst.Man., Promotions
Antenzana, Nelson	UCP	Accountant
Aliaga, Javier	UCP	Project Evaluator
PRIVATE SECTOR		
Calvo, Carlos	CEPB (Priv.Sect.)	Priv.Sect. Confed. President
Nogales, Johnny	CEPB	Executive Secretary
Zalles, Amparo	CEPB	Economist

INTL. ORGANIZATIONS		
Mendoza, Fernando	World Bank	Representative
Shaw, William	World Bank	Macroeconomist
Ardiles, Luisa	World Bank	Consultant
Dorfman, Mark	World Bank	Consultant
Albergucci, Francisco	IDB	Representative
Castaños, Arturo	CAF	Representative
ICIS		
Calvo, Fernando	Banco Nacional	General Manager
Alvarez, Eduardo	Banco Nacional	Manager, La Paz
Gutierrez, Jaime	Banco Inversion	Vice President
Ibarnegaray, Jaime	Banco Inversion	Manager, Dev. Depart.
Blanco, Enrique	BHN Multibanco	Manager, Dev. Depart.
Lema, Mario	BHN Multibanco	Vice President
Hinojosa, Guido	Banco de La Paz	President
Peñaranda, Rafael	Banco de La Paz	Manager, Dev. Depart.
Unzueta, Emilio	Banco Mercantil	Vice President
Arias, Jose	Banco Boliv. Amer.	Exec. Vice President
Ortega, Ramiro	Banco Boliv. Amer.	Commercial Vice Pres.
Medrano, Omar	Banco Boliv. Amer.	Assistant Vice Pres.
Sanjinez, Edgardo	UCF La Paz	Manager
Dávalos, Waldo	UCF La Paz	Project Evaluator
Projects		
"Muebles Equus"	Furniture	
"Textiles Modas Express"	Textiles	
BENI		
Ruiz, Gonzalo	UCF Beni	Manager
Cuellar, Oscar	UCF Beni	Project Evaluator
Davalos, Luis	Banco Big Beni	Manager
Projects		
"Ben. Castana Bezerra"	Brazil Nut	
"Ben. Castana Agrinbol"	Brazil Nut	
"Ben. Castana Hecker"	Brazil Nut	
"Irobi Transferencia de Embriones"	Cattle Breeding	
"Lecheria Nueva Esperanza"	Milk Processing	

COCHABAMBA		
Prudencio, Marcelo	UCF Cochabamba	Manager
Rico Toro, Faustino	Corporation	President
Polo, Jose	Private Sector	General Manager
La Fuente, Jaime	Fed. Emp. Privados	Second Vice President
Gainsborg, Jose	Fed. Emp. Privados	Representative
Gamarra, German	Fed. Emp. Privados	Economic Advisor
Projects		
"El Tumbal"	Agroindustry	
"Asarti"	Sweaters	
"Flores Canedo"	Flowers	
SANTA CRUZ		
Velasco, Jaime	UCF Santa Cruz	Manager
Paz, Roberto	UCF Santa Cruz	Legal Councel
Vargas, René	UCF Santa Cruz	Asst. Manager
Cabrera, Jorge	Small Industry	President
Savedra, Luis	Banco Santa Cruz	President
Arias, Jorge	Banco de la Union	General Manager
Fajerstain, Jaime	Banco de la Union	Asst.Man,Dev.Depart.
Davis, Mauricio	Banco de La Paz	Manager
Projects		
"Refresco Cabrera"	Agroindustry	
"Terminal Carga Pailon"	Transportation	
"Inabol Ltda."	Textiles	
"Jihusa"	Industry	
"Indusrias Camba"	Agroindustry	
"Matadero Frigorifico"	Meat processing	
SUCRE		
Aguirre, José Luis	UCF Chuquisaca	Manager
Gardilcic, Mirko	UCF Chuquisaca	Technical Manager
Lopez, Alvaro	UCF Chuquisaca	Financial Manager
Santa Cruz, Marcelo	UCF Chuiq. Board	Private Sect. Rep.
Projects in Sucre		
"Prelavado Lana Oveja"	Wool washing	
"Proces. Polietileno"	Plastic bag production	
"El Paraiso"	Domestic Plants	
"IPAL"	Food Processing	

91

Projects in Camargo

"La Torre"	Fruit, Vegetables	
"Agroindustria Colorado"	Fruit, Wine, Agroindustry	
"Buena Vista"	Fruit, Vegetables	

ORURO

Calderón, José	UCF Oruro	Manager
Paz, Tito	UCF Oruro	Project Evaluator

Projects in Oruro

"Laminadora Oruro"	Steel Processing	
"Ceramica Roja"	Housing material	
"Carpinteria Collado"	Carpentry	
"Curtiembre Iquimbol"	Leather Processing	
"Fabrica Tejidos Sendotex"	Textiles	

POTOSI

Buhezo, Jaime	CODEPOT	President
Decormis, Juan M.	UCF Potosí	Manager
Cornejo, Ruth	UCF Potosi	Project Evaluator
Ayala, Ramiro	UCF Potosi	Accountant
Rios, Armando	Banco de La Paz	Manager
Aguirre, Ramon	Banco Nacional	Manager
Romay, Johnny	Mining Association	Admin. Manager
Subieta, Roberto	Fed. Empres. Priv.	Executive Secretary

Projects

"Estuquera Cayara"	Lime Production	
"Prod. Porcinos"	Pig Farming	
"Hostal Claudia"	Hotel	
"Panif. Guadalupe"	Bread Bakery	

TARIJA

Lea Plaza, Mario	CODETAR	President
Galarza, Iván	UCF Tarija	Manager
Moreno, Carlos	UCF Tarija	Administrator
Borda, Enrique	UCF Tarija	Technical Evaluator
Castillo, Lucio	UCF Tarija	Economic Evaluator
Oropeza, Mario	UCF Tarija	Lawyer
Castellanos, Milton	Fed. Empres. Priv.	President
Michel C., Franse	Agroindustry Assoc.	President
Ruiz, Jaime	Agroindustry Assoc.	Manager
Paz B., Fernando	Banco. Nacional	Manager
Herbas, Mario	Banco Mercantil	Manager

Projects

"Curtiembre Guadalquivir"	Leather Processing
"Carpinteria Castanon"	Carpentry
"Proces. Productos Bandy"	Food Processing
"Confecciones Manfredo"	Textiles

WASHINGTON, D.C.

Cooley, Larry	MSI	President
Bunce, Dwight	MSI	Senior Associate, Former Advisor FOCAS

APPENDIX I - Case Studies

Box 4.2 Lending program for small enterprises in Ecuador

In 1980, Ecuador's Corporación Financiera Nacional, the country's largest government-owned development finance institution, established a fund—Fondo de Fomento para la Pequeña Industria y la Artesanía (FOPINAR)—to refinance loans from local financial institutions to small enterprises. The fund is autonomous and operates from a head office in Quito as well as from regional branches. Its financing has come principally from multilateral institutions via the government, which bears the foreign exchange risk. At the end of 1988, FOPINAR had approved the refinancing of 7,467 loans averaging $14,000. Enterprises outside the main urban centers have received 48 percent of the loans (by value).

There are now some forty participating financial intermediaries. The government-owned Banco de Fomento Nacional (BFN), primarily an agricultural bank, accounts for 45 percent of the loans to about 75 percent of the borrowers. Private development finance institutions and commercial banks account for the rest. (The four most active banks account for around 23 percent of total lending, and other banks and finance institutions each account for between 1 and 3 percent.) To participate in the program, the institutions must meet criteria regarding the quality of their FOPINAR portfolio, their overall debt-to-equity ratio, and their standing with the central bank and the superintendency of banks. In order to encourage the participating institutions to become more independent, the program requires them to provide 10 percent of project costs from their own resources. Terms and conditions have been designed to provide FOPINAR and the institutions with adequate spreads (currently 2.5 percent and 5.0-6.0 percent respectively) and to keep interest rates to borrowers positive in real terms. The latter goal has not been fully achieved, mainly because of the very high inflation of the past year and the lack of an automatic procedure for adjusting interest rates.

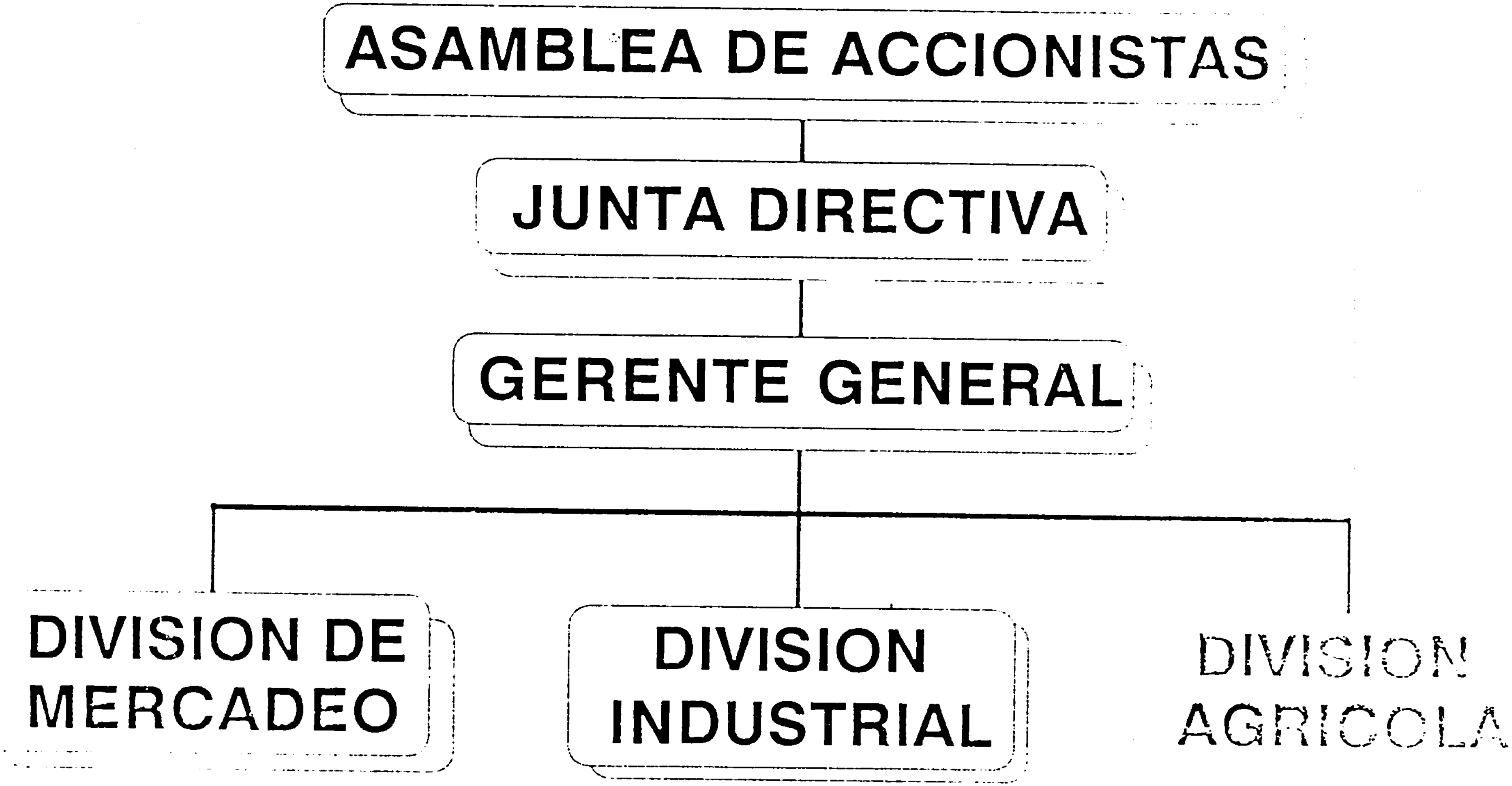
Collection has been quite good. Arrears on the FOPINAR portion of the discounted loans of the private development finance institutions and commercial banks have averaged less than 3 percent. In June 1988 arrears represented about 11 percent of their overall portfolios.

FOPINAR's independence has allowed it to respond flexibly to changing conditions. FOPINAR actively promoted the program and set terms that were sufficiently generous to attract the financial institutions. It has helped to train the institutions' staff, and they and FOPINAR have accorded a high priority to supervising the loans. Automatic debiting of the institutions for amounts due to FOPINAR gives them an incentive to judge their lending carefully.

Source: World Development Report "Financial Systems and Development", 1989. The World Bank.

CINDE

COALICION COSTARRICENSE DE INICIATIVAS PARA EL DESARROLLO



PROGRAMA DE PROMOCION DE INVERSIONES Y EXPORTACIONES (P.I.E.)

METAS:

* GENERAR NUEVOS EMPLEOS

* AUMENTAR LAS EXPORTACIONES NO TRADICIONALES

* FOMENTAR LAS INVERSIONES EXTRANJERAS

CINDE

SERVICIOS PARA EL INVERSIONISTA:

PRESENTACIONES EN EL EXTERIOR

VISITAS AL PAIS (ITINERARIOS)

INFORMACION

INVESTIGACION

SEGUIMIENTO

TRAMITES

CINDE

SERVPIE

CINDE

AÑOS

85 86 87 88 89 90 91

PROMOCION DE INVERSIONES EXTRANJERAS

CONTRATACION SENCILLA

CONTRATACION COMPLEJA

RECONVERSION INDUSTRIAL SECTOR LOCAL

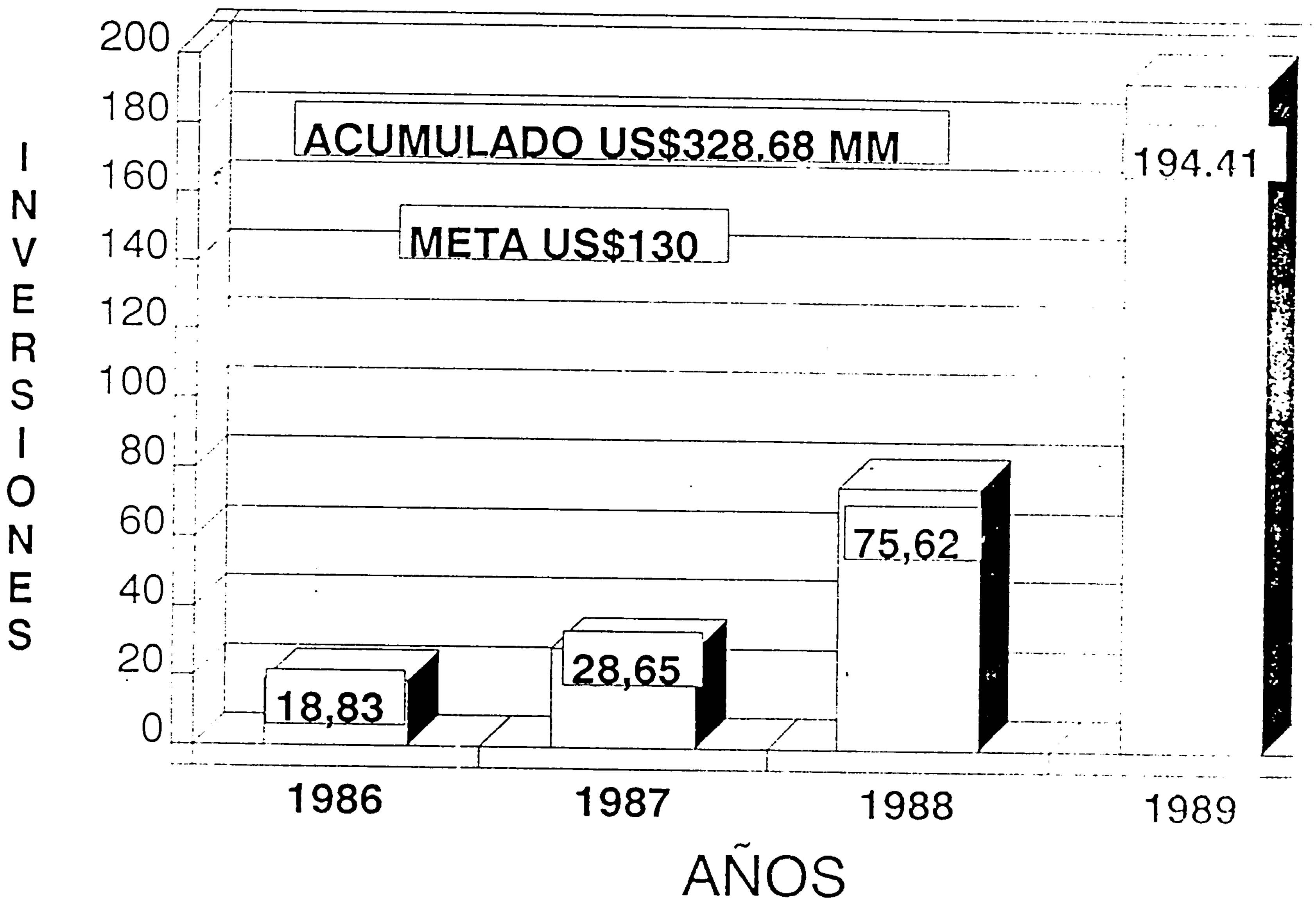
PROMOCION COINVERSIONES

EVOLUCION DE SERVICIOS

104

EVOLSERV

CINDE/PIE
RESULTADOS INVERSIONES



105

APPENDIX J

FINDES - Organizational Charts

ORGANIZATIONAL CHART
FINDES

STAGE 1

GENERAL ASSEMBLY OF SUPPORTERS

BOARD OF DIRECTORS
EXECUTIVE DIRECTOR
(C.E.O.)

GENERAL MANAGER
(C.O.O.)

SECRETARY

INFORMATION SERVICES

EXTERNAL PROMOTION SUPERVISOR

SECRETARY

LOCAL PROMOTION SUPERVISOR

SECRETARY

SUPPORT SERVICES SUPERVISOR

SECRETARY

PROMOTER OFFICE # 1

PROMOTER OFFICE # 2

SECRETARY

SECRETARY

MARKETING OFFICIAL

SECTOR SPECIALIST

SECTOR SPECIALIST

SECTOR SPECIALIST

SECRETARY

CONTRACTING OFFICIAL

OFFICIAL #1

OFFICIAL #2

ASSISTANT

ASSISTANT

ASSISTANT

ASSISTANT

SECRETARY

ORGANIZATIONAL CHART
FINDES

STAGE 2

GENERAL ASSEMBLY OF SUPPORTERS

BOARD OF DIRECTORS
EXECUTIVE DIRECTOR
(C.E.O.)

GENERAL MANAGER
(C.O.O.)

SECRETARY

INFORMATION SERVICES

EXTERNAL PROMOTION MANAGER

SECRETARY

LOCAL PROMOTION MANAGER

SUPPORT SERVICES MANAGER

SECRETARY

SECRETARY

PROMOTER OFFICE # 1

PROMOTER OFFICE # 2

MARKETING OFFICIAL

OFFICIAL #1

OFFICIAL #2

SECTOR SPECIALIST

SECRETARY

SECRETARY

ASSISTANT

ASSISTANT

ASSISTANT

SECTOR SPECIALIST

SECRETARY

PROMOTER OFFICE # 3

PROMOTER OFFICE # 4

REGIONAL PROMOTER #1

SECRETARY

SECTOR SPECIALIST

SECRETARY

SECRETARY

SECRETARY

OFFICIAL #3

OFFICIAL #4

CONTRACTING OFFICIAL

REGIONAL PROMOTER #2

ASSISTANT

ASSISTANT

ASSISTANT

SOUTH AMERICAN EXPORT PROMOTER

SECRETARY

SECRETARY