CLASSIFICATION:

AGENCY FOR INTERNATIONAL DEVELOPMENT

PROGRAM ASSISTANCE APPROVAL DOCUMENT (PAAD)

1. PAAD Number: Amendment to PAAD 517-K-046 K-039 A
2. Country: Dominican Republic
3. Category: Cash Transfer
4. Date: September 23, 1983
5. To: Acting AA/LAC, Marshall D. Brown
6. OYB Change Number:
7. From: LAC/DR, Dwight B. Johnson
8. OYB Increase: None
   To be taken from: Economic Support Funds (ESF)
9. Approval Requested for Commitment of: $ 8,000,000
10. Appropriation Budget Plan Code: LESA83-35517-KL31 72-1131037
11. Type Funding: [X] Loan [ ] Grant
12. Local Currency Arrangement: [ ] Informal [X] Formal [ ] None
13. Estimated Delivery Period: FY 1983
14. Transaction Eligibility Date:
15. Commodities Financed: N/A

16. Permitted Source	17. Estimated Source
U.S. only	U.S. $8,000,000
Limited F.W.	Industrialized Countries
Free World	Local
Cash $8,000,000	Other

18. Summary Description

This is an amendment to increase funding for the Private Enterprise Sector Dev, Program (Project #517-0171, Loan #517-K-039) by $8,000,000 to $49,000,000. Additional funds are being requested to implement the following strategy:

(1) A.I.D. to provide additional immediate BOP relief to the Dominican economy by the provision of a $8 million cash transfer to the Central Bank. The foreign exchange will be made available from the loan subject to a convenant by the GODR that in the succeeding 12 months, it will allocate at least an equivalent amount of foreign exchange to the private sector for the importation of essential raw materials, intermediate goods, and capital goods from the U.S. for private sector industry and agriculture. The Central Bank will document imports of eligible commodities by the private sector and provide the mission with a quarterly report of these transactions. All necessary supporting documents will be maintained by the Central Bank for mission review.

(2) The GODR to provide as counterpart funding, the peso equivalent of $8 million to be held in special accounts. In accordance with the mission development strategy elaborated in the FY 1985 CDSS, this counterpart fund will be used to finance high priority private sector developent needs. The GODR has requested that counterpart funds be utilized to provide assistance to two general areas: (a) RD pesos three million to support private sector export expansion including the development of free zone facilities; and (b) RD pesos five million in support of a productive infrastructure principally to accelerate execution of IDB, IBRD and AID projects, which are necessary for private sector investment.

The dollar loan will be repaid in 25 years with a 10 year grace period. Interest will be paid at the rate of 2 percent during the grace period and 3 percent thereafter.

19. Clearances	Date
LAC/DP, D. Erbe DJS for	23 Sept 83
GC/LAC, R. Meighan	9/28/83
LAC/CAR, J. Holtaway	9/28
M/FM, C. Christensen	9/29
ARA/ESP, R. Bash	9/28
LAC/DR, W. Stickel S. Smith	9/28
DAA/LAC, I. A. Levy	9/28

20. Action: [X] APPROVED [ ] DISAPPROVED

Authorized Signature: Marshall Brown — Date: 9/29/83

Marshall D. Brown

Title: Acting AA/LAC

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E.O. 12356: N/A
SUBJECT: PROGRAM ASSISTANCE APPROVAL DOCUMENT (PAAD) - AMENDMENT TO PROJECT NO. 517-0203

1. SUMMARY. THIS CABLE CONSTITUTES THE PAAD TO AMEND THE ONGOING PRIVATE ENTERPRISE SECTOR DEVELOPMENT PROGRAM (PROJECT NUMBER 517-0203, LOAN NUMBER 517-K-039). THIS AMENDMENT WILL ADD DOLS. 8.0 MILLION TO THE ONGOING ECONOMIC SUPPORT FUND (ESF) LOAN. MISSION REQUESTS AID/W AUTHORIZATION TO OBLIGATE THIS AMENDMENT PRIOR TO SEPTEMBER 30. END SUMMARY.

2. RECOMMENDATION: USAID/DOMINICAN REPUBLIC RECOMMENDS AUTHORIZATION OF A DOLS 8.0 MILLION INCREASE TO THE ONGOING PRIVATE ENTERPRISE SECTOR DEVELOPMENT PROGRAM. THIS INCREASE WILL RAISE THE EXISTING ESF LOAN TO A TOTAL OF DOLS. 49 MILLION. THE DOLLAR LOAN WILL BE REPAID IN 25 YEARS WITH A 10-YEAR GRACE PERIOD. THE INTEREST WILL BE 2 PERCENT DURING THE GRACE PERIOD AND 3 PERCENT THEREAFTER.

3. BORROWER: THE BORROWER WILL BE THE GOVERNMENT OF THE DOMINICAN REPUBLIC (GODR). THE TECHNICAL SECRETARIAT OF THE PRESIDENCY (STP) WILL BE THE OFFICIAL GODR PROJECT REPRESENTATIVE.

4. PROGRAM SUMMARY:
A. DURING RECENT YEARS THE DOMINICAN ECONOMY HAS SUFFERED SERIOUSLY FROM DEPRESSED INTERNATIONAL PRICES FOR ITS MAJOR PRODUCTS, SHORTAGES OF FOREIGN EXCHANGE AND CONSTRICTED IMPORTS, REDUCED REVENUES, SCARCITY OF CREDIT AND INVESTMENT, GROWING PUBLIC SECTOR DEFICITS, AND A POLICY FRAMEWORK WHICH HAS EMPHASIZED IMPORT SUBSTITUTION AND DEPENDENCE UPON EXPORTS OF TRADITIONAL AGRICULATURAL AND MINERAL COMMODITIES.

B. IN RESPONSE TO THIS SEVERE ECONOMIC SITUATION, THE GOVERNMENT OF PRESIDENT JORGE BLANCO, WHO ASSUMED OFFICE IN AUGUST 1982, IMMEDIATELY FORMULATED BOTH SHORT-AND MEDIUM-TERM STRATEGIES AIMED AT ECONOMIC RECOVERY. THESE STRATEGIES WERE CONSISTENT WITH RECOMMENDATIONS PRESENTED TO THE GODR BY THE WORLD BANK IN JUNE 1982 CALLING FOR A NARROWING OF THE CENTRAL GOVERNMENT'S FISCAL DEFICIT, A SPURRING OF THE SAGGING DOMINICAN PRIVATE SECTOR, AND PROMOTION OF NON-TRADITIONAL EXPORTS TO IMPROVE THE COUNTRY'S FOREIGN EXCHANGE POSITION. ALTHOUGH THE GODR HAS BEGUN PLANNING AND IMPLEMENTATION TO ACHIEVE THESE OBJECTIVES, IT WILL TAKE TIME FOR THESE REMEDIAL ACTIONS TO HAVE A SIGNIFICANT POSITIVE IMPACT.

C. THE GODR HAS DEMONSTRATED THAT IT IS DETERMINED TO CONFRONT THE CURRENT ECONOMIC CRISIS. IN ADDITION TO ITS ANNOUNCEMENT AND IMPLEMENTATION OF A SERIES OF ECONOMIC REFORMS, THE GODR REACHED AGREEMENT IN JANUARY 1983 WITH THE IMF FOR AN EXTENDED FUND FACILITY (EFF), TOTALING DOLS. 450 MILLION OVER 3 YEARS BEGINNING IN 1983. IT WAS AGAINST THIS BACKDROP THAT THE USG AND THE GODR EXECUTED ON SEPTEMBER 30, 1982 A LOAN AGREEMENT TO PROVIDE DOLS. 41.0 MILLION IN

IMMEDIATE BALANCE-OF-PAYMENT (BOP) SUPPORT AND TO EASE THE STRAIN OF THE AUSTERITY MEASURES THE GODR WAS COMMITTED TO TAKE.

D. DURING THE FIRST HALF OF 1983 THE GODR HAS SATISFIED ALL IMF CONDITIONS FOR THE EFF. PARTY DUE TO THE GODR EFFORT TO COMPLY WITH THE IMF AGREEMENT, THE BOP SITUATION IMPROVED SUBSTANTIALLY DURING THE JANUARY-JUNE 1983 PERIOD. THE OVERALL BOP DEFICIT IN 1983 IS NOW ESTIMATED TO BE DOLS. 89 MILLION AS COMPARED TO THE DISMAL LEVEL OF DOLS. 317 MILLION IN 1982. THIS IMPROVEMENT, HOWEVER, IS NOT DUE TO AN INCREASE IN EXPORT EARNINGS BUT PRIMARILY DUE TO THE RESCHEDULING OF MORE THAN DOLS. 600 MILLION IN SHORT-TERM COMMERCIAL BANK ARREARAGES. THE COMMERCIAL RESCHEDULING AGREEMENT IS TO BE SIGNED ON SEPTEMBER 15, 1983. MEANWHILE, THE GODR HAS PROPOSED FORMALLY TO THE GOVERNMENT OF FRANCE THE RENEGOTIATION OF ITS OFFICIAL DEBT THROUGH THE PARIS CLUB MECHANISM. IF COMPLETED BEFORE YEAR END, THIS ACTION WILL RELIEVE THE GODR OF ABOUT DOL. 81 MILLION IN OFFICIAL DEBT SERVICE IN 1983. THE REDUCTION IN THE OVERALL BOP DEFICIT, HOWEVER, IS NOT AN INDICATION OF IMPROVEMENT IN THE ECONOMY BUT RATHER A MANIFESTATION OF DEPRESSED ECONOMIC ACTIVITY. CONTINUED BOP ASSISTANCE IS CLEARLY INDICATED BY THE FACT THAT THE NET INTERNATIONAL RESERVES HAVE DECLINED STEADILY TO MINUS DOLS. 855 MILLION AS OF MARCH 1983 INDICATING A SEVERE SHORTAGE OF FOREIGN EXCHANGE AND LIMITED ESSENTIAL IMPORTS TO THE COUNTRY.

E. THE STRATEGY PROPOSED HEREIN IS FOR:

1) THE USG TO PROVIDE ADDITIONAL IMMEDIATE BOP RELIEF TO THE DOMINICAN ECONOMY BY THE PROVISION OF A DOLS 8 MILLION CASH TRANSFER TO THE CENTRAL BANK. THE FOREIGN EXCHANGE WILL BE MADE AVAILABLE FROM THE LOAN SUBJECT TO A COVENANT BY THE GODR THAT IN THE SUCCEEDING TWELVE MONTHS IT WILL ALLOCATE AT LEAST AN EQUIVALENT AMOUNT OF FOREIGN EXCHANGE TO THE PRIVATE SECTOR FOR THE IMPORTATION OF ESSENTIAL RAW MATERIALS, INTERMEDIATE GOODS, AND CAPITAL GOODS FROM THE U.S. FOR PRIVATE SECTOR INDUSTRY AND AGRICULTURE. THE CENTRAL BANK WILL DOCUMENT IMPORTS OF ELIGIBLE COMMODITIES BY THE PRIVATE SECTOR AND PROVIDE THE MISSION WITH A QUARTERLY REPORT OF THESE TRANSACTIONS. ALL NECESSARY SUPPORTING DOCUMENTS WILL BE MAINTAINED BY THE CENTRAL BANK FOR MISSION REVIEW.

2) THE GODR TO PROVIDE, AS COUNTERPART FUNDING, THE PESO EQUIVALENT OF DOLS. 8 MILLION TO BE HELD IN SPECIAL ACCOUNTS. IN ACCORDANCE WITH THE MISSION DEVELOPMENT STRATEGY ELABORATED IN THE FY 1985 CDSS, THIS COUNTERPART FUND WILL BE USED TO FINANCE HIGH PRIORITY PRIVATE SECTOR DEVELOPMENT NEEDS. THE GODR HAS REQUESTED THAT COUNTERPART FUNDS BE UTILIZED TO PRIVDE ASSISTANCE TO TWO GENERAL AREAS: (A) RD PESOS 3 MILLION TO SUPPORT PRIVATE SECTOR EXPORT EXPANSION INCLUDING THE DEVELOPMENT OF FREE ZONE FACILITIES; AND (B) RD PESOS 5 MILLION IN SUPPORT OF A PRODUCTIVE INFRASTRUCTURE PRINCIPALLY TO ACCELERATE EXECUTION OF IDB, IBRD AND AID PROJECTS, WHICH ARE NECESSARY FOR PRIVATE SECTOR INVESTMENT.

5. DESCRIPTION OF ECONOMIC CONDITIONS - UPDATE:

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A. DURING 1983, THE DOMINICAN ECONOMY APPEARS TO HAVE HALTED ITS DOWNSLIDE WHICH BEGAN WITH THE NEAR-DOUBLING OF PETROLEUM PRICE IN 1978, TWO HURRICANE DISASTERS IN 1979, AND THE PRECIPITOUS DROP OF WORLD SUGAR PRICES IN 1981. DURING THE FIRST HALF OF 1983, SUGAR PRICES HAVE RECOVERED SLIGHTLY AS HAVE PRICES OF GOLD, SILVER, AND FERRONICKEL. A SUBSTANTIAL INCREASE IN TOURISM EARNINGS IS FORECAST FOR 1983. REAL GDP GROWTH FOR 1983 IS ESTIMATED IN THE RANGE OF 2-3 PERCENT, WHICH COMPARES FAVORABLY AGAINST ZERO GROWTH IN 1982. THE PRELIMINARY ESTIMATES INDICATE, HOWEVER, THE PRODUCTIVE SECTORS -- AGRICULTURE AND INDUSTRY -- HAVE NOT SHOWN ANY APPRECIABLE IMPROVEMENTS DURING THE FIRST HALF OF 1983. IN AN OPEN ECONOMY SUCH AS THIS ONE, IT IS UNREALISTIC TO EXPECT REAL GROWTH IN PRODUCTION TO OCCUR WITHOUT INCREASES IN IMPORTS OF RAW MATERIALS, INTERMEDIATE INPUTS AND CAPITAL. VARIOUS IMPORT STATISTICS SHOW A REDUCED 1983 IMPORT LEVEL, IN CURRENT PRICES, FROM THE DEPRESSED 1982 LEVEL. AS LONG AS IMPORTS ARE RECESSED AT THE 1982 LEVEL, NO REAL ECONOMIC GROWTH IS LIKELY TO TAKE PLACE IN THE DOMINICAN ECONOMY.

B. THE SINGLE MOST IMPORTANT EVENT SO FAR IN 1983 HAS BEEN THE IMF AGREEMENT FOR AN EXTENDED FUND FACILITY SIGNED IN JANUARY. UNDER THE AGREEMENT, THE GODR IS PERMITTED TO PURCHASE ABOUT DOLS. 450 MILLION OVER 1983-1985, APPROXIMATELY DOLS. 150 MILLION EACH YEAR, WITH QUARTERLY IMF CONSULTATIONS. THE IMF AGREEMENT CONTAINS THE USUAL PERFORMANCE CRITERIA, SPECIFIED ONE YEAR AT A TIME, RELATED TO EXPANSION OF NET DOMESTIC CREDIT OF THE CENTRAL BANK AND RESERVE BANK, NET DOMESTIC ASSETS OF THE CENTRAL BANK, NET REDUCTION IN EXTERNAL PAYMENTS ARREARS, CENTRAL BANK NET INTERNATIONAL RESERVES, AS WELL AS LIMITS ON THE CONTRACTING OF NEW EXTERNAL LOANS BY THE PUBLIC SECTOR, A DOLS 100 MILLION REDUCTION IN CENTRAL BANK EXTERNAL PAYMENT ARREARAGES, AND A DOLS. 85 MILLION TRANSFER OF OFFICIAL IMPORTS IN 1983TO THE PARALLEL EXCHANGE MARKET. THE IMF ARRANGEMENT DID NOT REQUIRE DEVALUATION OF THE OFFICIAL EXCHANGE RATE, BUT ENCOURAGED LEGALIZATION AND UTILIZATION OF THE PARALLEL EXCHANGE MARKET. IT WAS HYPOTHESIZED THAT A POLICY OF BROADENING THE SCOPE OF THE PARALLEL FOREIGN EXCHANGE MARKET WOULD FACILITATE UNIFICATION OF THE EXCHANGE MARKET AT SOME FUTURE TIME AT A REALISTIC RATE.

C. WITH THE IMF AGREEMENT IN HAND, THE JORGE BLANCO ADMINISTRATION LAUNCHED ITS NEGOTIATIONS WITH COMMERCIAL BANKS TO RESCHEDULE ARREARAGE PAYMENTS. ALTHOUGH THE NEGOTIATIONS WERE DELAYED CONSIDERABLY DUE TO DIFFERENCES AMONG THE CREDITOR BANKS OVER TERMS, THE BANKS AND THE GODR REACHED AGREEMENT IN LATE AUGUST TO RESCHEDULE REPAYMENTS OF MORE THAN DOLS. 600 MILLION IN 1982/83 COMMERCIAL ARREARAGES TO FIVE YEARS WITH A ONE YEAR GRACE. THE IMF AGREEMENT AND THE COMMERCIAL RESCHEDULING AND PROSPECTIVE PARIS CLUB RESCHEDULING WILL RELIEVE PRESSURE ON THE BALANCE OF PAYMENTS SIGNIFICANTLY BUT TEMPORARILY.

D. THE SLOW ECONOMIC GROWTH RATE DURING THE PAST FEW

YEARS HAS AGGRAVATED THE ALREADY HIGH UNEMPLOYMENT SITUATION. SOME REPORTS CLAIM THE UNEMPLOYMENT RATE TO EXCEED 30 PERCENT OF THE AVAILABLE WORKFORCE. HOWEVER, THE CONSERVATIVE MONETARY POLICY AND PRICE CONTROL MEASURES PURSUED BY THE GODR HAVE LIMITED THE CONSUMER PRICE INFLATION IN 1983 TO ABOUT A 7 PERCENT ANNUAL RATE AND THE NET DEPRECIATION OF THE PESO TO UNDER 10 PERCENT. PERHAPS THE MOST REMARKABLE OUTCOME OF THE JORGE BLANCO'S ADMINISTRATION MUST BE ITS ALL OUT EFFORT TO INCREASE THE EFFICIENCY OF THE PUBLIC SECTOR ENTERPRISE OPERATIONS. THE PRESIDENT SCRUTINIZED THE FINANCIAL OPERATION OF CEA, CDE, INESPRE, AND THE CORDE ENTERPRISES AND REPORTED THAT THEIR DEFICITS HAD BEEN REDUCED BETWEEN 44 TO 74 PERCENT DURING THE JANUARY-JUNE 1983 PERIOD, COMPARED TO THOSE DURING THE SAME PERIOD IN 1982. THE DEFICIT OF THE CENTRAL GOVERNMENT HAS ALSO BEEN REPORTED TO DECLINE FROM RD PESOS 145 MILLION IN THE FIRST HALF OF 1982 TO RD PESOS 85 MILLION DURING THE SAME PERIOD IN 1983 -- A REDUCTION OF 39 PERCENT. THIS REMARKABLE OUTCOME IS PRIMARILY DUE TO THE STEPPED UP EFFORT IN TAX COLLECTION INITIATED BY THE JORGE BLANCO ADMINISTRATION.

E. IN SUM, THE COMBINATION OF THE IMF AGREEMENT, THE RESCHEDULING OF THE COMMERCIAL AND OFFICIAL DEBT AND THE DETERMINED EFFORT BY THE GODR TO IMPROVE PUBLIC SECTOR EFFICIENCY SEEM TO HAVE STALLED OR EVEN HALTED THE ECONOMIC SLIDE WHICH HAS HAMPERED THE DOMINICAN ECONOMY FOR THE PAST FEW YEARS. HOWEVER, THE REAL ECONOMIC SECTOR HAS NOT YET INCREASED PRODUCTION AND EXPORTS IN RESPONSE. PERHAPS, THE MORE RELEVANT QUESTION TO ASK IS QUOTE WHY WOULD PRODUCTION AND INVESTMENT INCREASE UNQUOTE. FOR THE IMF ARRANGEMENT IS ESSENTIALLY A STABILIZATION PROGRAM. THE IMF CONDITIONS, WHICH LIMIT NET DOMESTIC CREDITS, NET DOMESTIC ASSETS OF THE CENTRAL BANK, NET EXTERNAL PAYMENT, ARREARS, NET INTERNATIONAL RESERVES OF THE CENTRAL BANK AND PLACE CEILINGS ON FOREIGN BORROWING BY THE PUBLIC SECTOR, CONSTRAIN THE GODR FROM ADOPTING AN EXPANSIONARY ECONOMIC POLICY FOR THE DURATION OF THE AGREEMENT. WITHOUT THE INITIATION OF EXPANSIONARY POLICY MEASURES, IT IS UNLIKELY THAT A NEW WAVE OF INVESTMENT AND PRODUCTION WILL BE FORTHCOMING. IN ADDITION, THE COMMERCIAL DEBT RESCHEDULING PROVIDES ONLY A ONE YEAR GRACE PERIOD (1984). THUS, THE GODR MUST FIND WAYS OF INCREASING ITS EARNINGS IN THE SHORT TO MEDIUM RUN TO MEET THE NEW DEBT REPAYMENTS AND EXPAND THE ECONOMY.

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F. TO INCREASE ITS REVENUES AND FX POSITION, THREE OPTIONS APPEAR OPEN TO THE GODR POLICY MAKERS:

1) INCREASE NON-TRADITIONAL EXPORTS OF GOODS AND SERVICES BY AT LEAST DOLS 150 MILLION A YEAR OVER THE 1985-89 PERIOD TO COVER THE UPCOMING ARREARAGE REPAYMENT. HOWEVER, IT IS UNREALISTIC TO EXPECT NON-TRADITIONAL EXPORTS TO INCREASE AT THIS RATE. IT WILL TAKE AT LEAST FOUR TO FIVE YEARS TO CHANGE THE STRUCTURE OF THE ECONOMY FROM ITS IMPORT SUBSTITUTION TO EXPORT EXPANSION MODE. AS LONG AS THE CURRENT IMPORT SUBSTITUTION EMPHASIS IS MAINTAINED, NO DRASTIC INCREASE IN NON-TRADITIONAL EXPORTS WILL LIKELY TAKE PLACE.

2) HOPE FOR CHANGES IN THE TERMS OF TRADE IN FAVOR OF DOMINICAN EXPORT COMMODITIES TO INCREASE THE COUNTRY'S BOP AND REVENUE POSITION. THE WORLD PRICES OF SUGAR, COFFEE, COCOA, TOBACCO, GOLD, SILVER, NICKEL, ETC., MAY RISE IN THE FUTURE THEREBY EASING THE FOREIGN EXCHANGE PRESSURE FOR THE TIME BEING. DUE TO THE PROJECTED REDUCTION OF CORN CROPS THIS YEAR IN THE U.S., IT MIGHT HAPPEN THAT SUGAR SUBSTITUTES WILL NO LONGER BE COMPETITIVE AND SUGAR PRICES ACTUALLY MAY GO UP SUBSTANTIALLY. UNFORTUNATELY, WITH THIS OPTION THERE IS NOTHING THAT THE GODR CAN DO. IN ADDITION, EVEN IF THE TERMS OF TRADE IMPROVE FOR NOW, IT IS LIKELY TO BE ONLY A TRANSIENT PHENOMENON.

3) INCREASE FOREIGN INVESTMENT AND LONG-TERM SOFT LOANS TO MAKE UP FOR THE FX SHORTFALL. THIS OPTION WOULD INCREASE FOREIGN EXCHANGE AVAILABILITY WHICH CAN BE USED TO STIMULATE THE ECONOMY THROUGH INVESTMENT, PRODUCTION, AND EXPORTS WITHOUT THE BURDEN OF IMMEDIATE REPAYMENT. WHILE THE GODR CAN HOPE FOR SOME IMPROVEMENT IN PRICES OF ITS PRINCIPAL EXPORTS AND SOME INCREASES IN ITS EXPORTS IN THE SHORT RUN, INCREASED FOREIGN INVESTMENT AND LONG-TERM SOFT LOANS APPEAR THE MOST REALISTIC OPTION OPEN TO THE GODR POLICY MAKERS. FOREIGN INVESTMENT HAS THE ADVANTAGE OF PROVIDING INVESTMENT CAPITAL, MARKETING KNOW-HOW AS WELL AS PRODUCTION TECHNOLOGY. THE INTERNATIONAL DONOR COMMUNITY ALSO SHOULD PROVIDE THE BOP ASSISTANCE FOR THE NEXT FOUR TO FIVE YEARS TO INCREASE IMPORTS AND EXPORTS.

6. BALANCE OF PAYMENTS UPDATE. (ALSO SEE ANNEX 1):

A. THE LATEST CENTRAL BANK PROJECTION FOR THE 1983 BOP SHOWS SLIGHT IMPROVEMENT IN BOTH TRADE BALANCE AND NET SERVICES. THE TRADE DEFICIT FOR 1983 IS PROJECTED AT DOLS 458 MILLION, DOWN FROM THE 1982 DEFICIT OF DOLS. 490 MILLION. THIS RECOVERY IS BASED ON A COMBINATION OF A PROJECTED SMALL INCREASE IN EXPORTS AND REDUCED IMPORTS. THE DEFICIT IN THE INVISIBLE BALANCE IS ALSO PROJECTED TO DECLINE SLIGHTLY FROM DOLS. 157 MILLION IN 1982 TO DOLS. 127 MILLION IN 1983, MAINLY DUE TO RISING TOURISM EARNINGS. AS A RESULT, THE CURRENT ACCOUNT DEFICIT IS PROJECTED AT DOLS. 370 MILLION IN 1983, A REDUCTION OF DOLS. 72 MILLION FROM THE 1982 DEFICIT LEVEL. ALTHOUGH THIS IS STILL A HIGH DEFICIT, IT IS THE SMALLEST CURRENT ACCOUNT DEFICIT SINCE 1979. THE CAPITAL ACCOUNT ALSO PROJECTS SOME IMPROVEMENTS. NET PRIVATE CAPITAL INFLOW IS

ESTIMATED AT MINUS DOLS 6 MILLION COMPARED TO THE ESTIMATED NET OUTFLOW OF DOLS. 121 MILLION DURING LAST YEAR. THE IMF AGREEMENT AND THE COMMERCIAL DEBT RESCHEDULING SEEM TO HAVE HAD POSITIVE IMPACT ON CREDIT AVAILABILITY. IN ADDITION, THE NET OFFICIAL CAPITAL INFLOW IS PROJECTED AT A SOMEWHAT OPTIMISTIC LEVEL OF DOLS. 269 MILLION, SOME DOLS. 61 MILLION HIGHER THAN LAST YEAR'S LEVEL. THE OVERALL BOP DEFICIT FOR 1983 IS ESTIMATED AT DOLS. 89 MILLION, WHICH IS FAR LESS THAN THE DOLS. 337 MILLION DEFICIT ESTIMATED FOR 1982.

B. WE MUST HASTEN TO ADD A WORD OF CAUTION. ALTHOUGH THE CENTRAL BANK PROJECTS AN IMPROVED BOP PICTURE FOR 1983, THE FIGURES INDICATE THAT THERE HAS NOT BEEN REAL PROGRESS IN EXTERNAL TRADE ON TWO ACCOUNTS: (1) THE OVERALL BOP IS STILL NEGATIVE. THAT MEANS, THE DOMINICAN ECONOMY MUST REDUCE ITS INTERNATIONAL RESERVES WHICH ARE ALREADY AT MINUS DOLS 855 MILLION; AND (2) THE IMPROVEMENT IS ENTIRELY SUPERFICIAL AND MAY BE TEMPORARY BECAUSE THE BOP IMPROVEMENT IS LARGELY BASED ON THE EXTENDED REPAYMENT SCHEDULE OF THE SHORT-TERM COMMERCIAL ARREARS. UNDER THE NEW REPAYMENT SCHEDULE, THE DOMINICAN ECONOMY HAS ONE YEAR (1984) TO REVITALIZE ITS EXPORT SECTOR TO EARN ADDITIONAL FOREIGN EXCHANGE SUFFICIENT TO COVER THE ADDITIONAL SERVICES OF ABOUT DOLS. 150 MILLION PER ANNUM BEGINNING IN 1985. SINCE THE 1983 BOP ACCOUNT FAILS TO SHOW ANY APPRECIABLE INCREASE IN EXPORT EARNINGS, PROSPECTS FOR A RAPID INCREASE IN EXPORTS IN 1985 ARE AT BEST UNCERTAIN. FURTHERMORE, THE LEVEL OF IMPORTS IS DEPRESSED AT DOLS. 1,250 MILLION, WHICH IS, IN CURRENT PRICES, SLIGHTLY LESS THAN THE DEPRESSED 1982 IMPORT LEVEL AND SOME 14 PERCENT BELOW THE 1980 IMPORT LEVEL. IT IS UNLIKELY THAT EXPORT ACTIVITIES AND EXPORTS WILL INCREASE WITHOUT A SIGNIFICANT RISE IN IMPORT ACTIVITIES AND IMPORTS.

C. THE BOP DEFICITS OF 1978-1982 WERE SUBSTANTIALLY FINANCED BY THE ACCUMULATION OF EXTERNAL PAYMENTS ARREARS AND THE REDUCTION IN THE NET INTERNATIONAL RESERVES OF THE BANKING SYSTEM. THE INTERNATIONAL ASSETS AND LIABILITIES OF THE ENTIRE BANKING SYSTEM SHOW AS OF MARCH 1983 A NEGATIVE INTERNATIONAL RESERVE OF DOLS. 855.3 MILLION, AS COMPARED TO A POSITIVE INTERNATIONAL RESERVE OF DOLS. 19.4 MILLION AT THE END OF 1977. THIS DRAMATIC DETERIORATION IN INTERNATIONAL RESERVES MUST BE REVERSED SOON IF THE EXTERNAL TRADE SECTOR IS TO BE RESTORED TO A MORE NORMAL SITUATION. IN ADDITION, MEDIUM-AND LONG-TERM EXTERNAL DEBTS REGISTERED WITH THE CENTRAL BANK HAVE INCREASED DURING 1982 TO DOLS. 1.75 BILLION FROM DOLS. 1.60 BILLION. THE AMORTIZATION OF MEDIUM-AND LONG-TERM DEBTS ALONE AMOUNTED TO DOLS. 161 MILLION IN 1982. THE SHORT-TERM DEBT AMORTIZATION WAS EVEN HIGHER AT DOLS. 255 MILLION. ALTHOUGH MUCH OF THESE AMORTIZATION PAYMENTS WERE FINANCED THROUGH ADDITIONAL LOANS, A CONTINUED ACCUMULATION OF EXTERNAL DEBTS CLEARLY COMPOUNDS THE COUNTRY'S EXTERNAL TRADE PROBLEMS.

D. THE DOMINICAN REPUBLIC NEEDS A RAPID INCREASE IN EXPORTS TO PROVIDE FOREIGN EXCHANGE FOR THE REPAYMENT OF PAST ARREARS AS WELL AS TO INCREASE IMPORTS FOR FURTHER EXPORTS. HOWEVER, UNDER THE IMF AGREEMENT, BORROWING BY THE CENTRAL BANK AND THE AUTONOMOUS AGENCIES IS CONSTRAINED BY THE LIMITATION IMPOSED ON THE NET INTERNATIONAL RESERVE (PERTAINING TO LIABILITIES OF MATURITY LESTLTHAN THREE YEARS). IN ORDER TO INITIATE THE NECESSARY EXPORT PROMOTION, WHICH IS A MEDIUM TO LONG-TERM PROBLEM, THE GODR MUST CONVERT ITS SHORT-TERM HIGH COST COMMERCIAL ARREARS TO A MANAGEABLE LONG-TERM LOAN PACKAGE. THE CURRENTLY NEGOTIATED RESCHEDULING OF THE DEBT IS ONLY A STOP GAP MEASURE WHICH WILL NOT CONTRIBUTE MUCH TO THE LONG-TERM SOLUTION OF DOMINICAN REPUBLIC'S BOP PROBLEMS. IMMEDIATE BOP ASSISTANCE IS URGENTLY NEEDED TO INCREASE IMPORTS OF RAW MATERIALS AND CAPITAL GOODS FOR THE PURPOSE OF INCREASING INVESTMENT, PRODUCTIVITY, EMPLOYMENT, AND EXPORT EARNINGS.

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E. RELATED TO THIS IS THE CURRENT EXCHANGE RATE POLICY THAT PROVIDES LITTLE FINANCIAL INCENTIVE TO EXPORTERS. THE GODR IS UNDER INCREASING PRESSURE TO ELIMINATE THE FOREIGN EXCHANGE SURRENDERING REQUIREMENT AS SOON AS POSSIBLE. IN ADDITION, THE GODR IS BEING ENCOURAGED TO ACCEPT THE IBRD/SAL AS A MEANS OF EASING THE CURRENT FOREIGN EXCHANGE BOTTLENECK AS WELL AS TO EMBARK ON THE STRUCTURAL CHANGE THAT IS NECESSARY TO BRING ABOUT THE EXPORT EXPANSION (THE IBRD DELEGATION IS SCHEDULED TO ARRIVE TOWARD THE END OF SEPTEMBER 1983 TO BEGIN NEGOTIATIONS). IN THIS CONNECTION, THE CBI LEGISLATION AND THE ALMOST CERTAIN DESIGNATION OF DOMINICAN REPUBLIC AS A CBI BENEFICIARY COUNTRY WILL PROVIDE A STRONG INCENTIVE FOR EXPORTS OF DOMINICAN PRODUCTS AS WELL AS FOR FOREIGN INVESTMENT.

7. PUBLIC FINANCE SITUATION UPDATE: THE DOMINICAN PUBLIC SECTOR, THE CENTRAL AND LOCAL GOVERNMENT, AND THE PUBLIC SECTOR ENTERPRISES, HAVE HAD LITTLE FINANCIAL DISCIPLINE IN THE PAST. PUBLIC SECTOR WAGES AND EMPLOYMENT GREW SHARPLY DURING 1978-1980 AND, AS A RESULT, CENTRAL GOVERNMENT CURRENT EXPENDITURES GREW BY 25 PERCENT PER ANNUM DURING THIS PERIOD. ON THE REVENUE SIDE, RECEIPTS BARELY KEPT PACE WITH INFLATION MAINLY DUE TO TAX EXEMPTIONS GRANTED TO RISING PETROLEUM AND FOOD IMPORTS. BY MID-1980, A FISCAL CRISIS EMERGED AS PRESIDENT GUZMAN INSTRUCTED BUDGET OFFICIALS TO HOLD FISCAL EXPENDITURES IN LINE WITH REVENUES VIRTUALLY ON A MONTH-TO-MONTH BASIS. IN 1982, THE CENTRAL GOVERNMENT CURRENT ACCOUNT DEFICIT REGISTERED THE PEAK OF RD PESOS 217 MILLION, WHEN THE NEW JORGE BLANCO ADMINISTRATION DECIDED TO RAISE THE INTERNAL EFFICIENCY OF THE PUBLIC SECTOR OPERATIONS. THE 1983 GOVERNMENT BUDGET FOR CURRENT EXPENDITURES WAS SET AT RD PESOS 720 MILLION, A 7.5 PERCENT REDUCTION FROM THE 1982 LEVEL. THE PRESIDENT HIMSELF SCRUTINIZED GOVERNMENT EXPENDITURES TO REDUCE UNNECESSARY EXPENSES. IN ADDITION, TAX ORGANIZATIONS WERE INSTRUCTED TO IMPROVE ENFORCEMENT OF TAX COLLECTION. A LARGE NUMBER OF UNNECESSARY AND LUXURY IMPORTS ARE PROHIBITED. AS A RESULT, IN SPITE OF THE RECESSED ECONOMIC SITUATION AND THE LOW LEVEL OF IMPORTS, CURRENT REVENUES HAVE INCREASED SUBSTANTIALLY DURING THE FIRST HALF OF 1983. THE 1983 JANUARY/JUNE CURRENT REVENUES EXCEEDED RD PESOS 434 MILLION, SOME RD PESOS 96 MILLION MORE THAN THE SAME PERIOD FOR 1982. ALTHOUGH CURRENT EXPENDITURES INCREASED AT A FASTER RATE THAN ANTICIPATED, THE CURRENT ACCOUNT FOR THE FIRST SIX MONTHS OF 1983 REGISTERED A SURPLUS OF RD PESOS 23 MILLION. THE OVERALL CENTRAL GOVERNMENT DEFICIT ALSO SHOWED A REDUCTION FROM RD PESOS 140 MILLION DURING THE FIRST SIX MONTHS OF 1982 TO ONLY RD PESOS 35 MILLION DURING THE SAME PERIOD OF 1983. ALTHOUGH DATA ARE NOT AVAILABLE ON THE FINANCIAL SITUATION OF PUBLIC SECTOR ENTERPRISES, THE PRESIDENT HAS REPORTED IN HIS LATEST SPEECH THAT DEFICITS OF CEA, CDE, INESPRE, AND CORDE HAVE BEEN REDUCED SUBSTANTIALLY FROM THE PREVIOUS YEAR LEVEL. IT HAS BEEN ALSO REPORTED THAT THE PUBLIC SECTOR ENTERPRISES HAVE REDUCED THEIR DEFICITS BETWEEN 44 PERCENT AND 74 PERCENT. SINCE THERE HAS BEEN NO MAJOR TAX CHANGES INSTITUTED THIS YEAR (EXCEPT THE 10

PERCENT IMPORT SURCHARGE), THE IMPROVEMENT IN TAX COLLECTION MUST BE ATTRIBUTED TO BETTER ENFORCEMENT OF EXISTING TAX LAWS. THIS IS A REMARKABLE TURNAROUND IN VIEW THAT THE FIRST QUARTER FIGURES INDICATED THAT THE 1983 DEFICIT COULD EXCEED THE PROJECTED LEVEL OF RD PESOS 212 MILLION. ALTHOUGH IT IS TOO EARLY TO JUDGE THE PUBLIC SECTOR DEFICIT SITUATION FOR 1983, THE NEW ADMINISTRATION SEEMS TO HAVE A HANDLE ON THE PUBLIC SECTOR FINANCIAL DISARRAY.

8. SELF-HELP MEASURES UPDATE:

A. THE ACHIEVEMENT OF THE JORGE BLANCO ADMINISTRATION ON ECONOMIC MATTERS IS INDEED IMPRESSIVE. ITS MAJOR ACCOMPLISHMENT HAS BEEN THE IMF AGREEMENT AND THE RESCHEDULING OF REPAYMENTS OF COMMERCIAL ARREARS. IN ADDITION, THE GODR HAS REQUESTED A PARIS CLUB MEETING FOR RESCHEDULING OF BILATERAL DEBTS WITH THE UNITED STATES AND SPAIN AND SEVERAL OTHER CREDITORS. THE REVISION OF FOREIGN INVESTMENT LAW 861 WAS DESIGNED TO ENCOURAGE FOREIGN INVESTMENT. UNDER THE AMENDMENT, FOREIGN INVESTORS ARE ALLOWED TO REGISTER INVESTMENT CAPITAL IN FOREIGN CURRENCIES, AND YEARLY PROFIT REMITTANCES HAVE BEEN INCREASED TO 25 PERCENT OF THE REGISTERED CAPITAL. THE LAW ALSO LIBERALIZED DOMSTIC INVESTMENT USING SURPLUS PROFITS. IN CONNECTION WITH THIS NEW LAW, THE FOREIGN INVESTMENT COMMISSION WAS CREATED TO ENCOURAGE FOREIGN INVESTMENT AND EXPORTS.

B. THE NEW ADMINISTRATION ALSO REVISED LAW 299 ON INDUSTRIAL INCENTIVES AND PROTECTION TO EXTEND THE BENEFIT OF IMPORTATION OF RAW MATERIALS AND CAPITAL GOODS WITH EXONERATIONS TO ALL PRODUCERS. A NEW 6 PERCENT VALUE ADDED TAX WILL GO INTO EFFECT IN NOVEMBER. THE GODR IS PREPARING THE OPERATIONAL PROCEDURES TO IMPLEMENT THE NEW TAX LAW. THE CENTRAL BANK IS IN THE PROCESS OF CONVERTING THE EXCHANGE HOUSES INTO FORMAL FOREIGN EXCHANGE BANKS, MOTIVATED IN PART TO STABILIZE THE EVER RISING PARALLEL MARKET EXCHANGE RATE (CURRENTLY RD PESOS 1.50 EQUALS US DOLS.1.00) AND IN PART TO INSTITUTIONALIZE THIS IMPORTANT FINANCIAL MARKET. FOR THIS PURPOSE, COMMERCIAL BANKS WERE PERMITTED TO OPERATE FREELY IN THE PARALLEL MARKET. TO MAKE THIS TRADITIONAL EXPORTS -- SUGAR, COCOA, COFFEE, TOBACCO -- MORE FINANCIALLY VIABLE, THE MONETARY BOARD AUTHORIZED ISSUANCE OF FREELY NEGOTIABLE FOREGN EXCHANGE CERTIFICATES FOR UP TO 20 PERCENT OF THE FIRMS' EXPORTS. THE TRADITIONAL EXPORTERS CAN USE THESE CERTIFICATES EITHER FOR IMPORTATION THROUGH THE CENTRAL BANK OR FOR EXCHANGE AT THE PARALLEL MARKET.

9. STATUS OF THE ONGOING PROGRAM:

A. THE PRIVATE ENTERPRISE SECTOR DEVELOPMENT PROGRAM IS NOW APPROXIMATELY ONE YEAR INTO IMPLEMENTATION. IN GENERAL THE PROGRAM IS PROGRESSING WELL. ALL OF THE DOLS. 41 MILLION WAS DISBURSED. REPORTS RECEIVED FROM THE CENTRAL BANK INDICATE THAT AS OF MARCH 31, 1983, DOLS. 20.4 MILLION OF ELIGIBLE GOODS HAVE BEEN IMPORTED UNDER THE PROGRAM FROM THE US FOR PRIVATE SECTOR INDUSTRY AND AGRICULTURE. AN INFORMAL REVIEW OF THE REPORTS BEING PREPARED BY THE CENTRAL BANK FOR SUBSEQUENT REPORTING PERIODS INDICATES THAT THE GODR WILL BE ABLE TO FULLY COMPLY WITH THE COVENANT IN THE LOAN AGREEMENT REGARDING THE IMPORTATION OF DOLS 41 MILLION OF GOODS FROM THE US BY THE COUNTRY'S PRIVATE SECTOR.

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INFO AALA-01 LACO-02 LADP-03 LADR-01 FVA-01 PPCE-01 PPEM-01
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ES-01 COM-02 OMB-02 OPIC-10 TRSY-05 RELO-01 MAST-01
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B. THE GODR'S COUNTERPART TO THE PROGRAM, THE PESO EQUIVALENT OF DOLS. 41.0 MILLION, WAS DEPOSITED IN A SPECIAL ACCOUNT IN THE CENTRAL BANK FOR USE IN SUPPORT OF SELECTED PRIVATE SECTOR ACTIVITIES. THE DETAILED PROCEDURES FOR THE PROGRAMMING AND USE OF THE GODR COUNTERPART HAVE BEEN ESTABLISHED. THE OVERALL DISTRIBUTION FOR THE USES OF THESE PESOS IS:

	RD PESOS
AGROINDUSTRY AND EXPORT CREDIT ACTIVITY	23 MILLION
PRODUCTIVE INFRASTRUCTURE FUND	10 MILLION
INSTITUTIONAL SUPPORT AND DEVELOPMENT	8 MILLION
TOTAL	41 MILLION

THE FOLLOWING IS A DISCUSSION OF THE STATUS OF THESE ACTIVITIES.

1. AGROINDUSTRY AND EXPORT CREDIT ACTIVITY:

A) OF THE RD PESOS 23 MILLION ORIGINALLY BUDGETED FOR THIS ACTIVITY, APPROXIMATELY RD PESOS 8.4 MILLION (36.5 PERCENT) HAS BEEN DISBURSED BY THE CENTRAL BANK FOR APPROVED SUBLOANS, RD PESOS 2.0 MILLION (8.7 PERCENT) IN SUBLOAND APPLICATIONS HAS BEEN APPROVED BY THE PRIVATE FINANCIAL INSTITUTIONS (PFI'S) AND IS BEING REVIEWED BY THE CENTRAL BANK, AND APPROXIMATELY RD PESOS 10.4 MILLION (45.2 PERCENT) IN SUBLOAND APPLICATIONS IS UNDER REVIEW BY THE PFI'S. RD PESOS 500,000 HAS BEEN SET ASIDE FOR STUDIES TO FACILITATE LENDING TO COOPERATIVES. THE DETAILED SCOPE OF WORK FOR THESE STUDIES IS BEING DISCUSSED AS WELL AS THE PLANS FOR THE USE OF THE REMAINING RD PESOS 1.7 MILLION (7.4 PERCENT) OF SUBLENDING FUNDS. IT IS EXPECTED THAT ALL PROGRAMED FUNDS UNDER THIS ACTIVITY WILL BE FULLY DISBURSED DURING THE NEXT QUARTER.

B) OF THE APPROXIMATELY RD PESOS 20.8 MILLION IN SUBLOANS EITHER DISBURSED OR UNDER REVIEW, 52.7 PERCENT IS IN SUPPORT OF AGROINDUSTRIAL PROJECTS FOR EXPORT, 2.2 PERCENT IS IN SUPPORT OF AGROINDUSTRIAL PROJECTS FOR LOCAL CONSUMPTION, AND 45.1 PERCENT IS IN SUPPORT OF NON-AGROINDUSTRIAL EXPORT PROJECTS.

2. PRODUCTIVE INFRASTRUCTURE FUND:

A) ALL OF THE RD PESOS 10.0 MILLION PROGRAMED UNDER THIS ACTIVITY WAS DISBURSED RAPIDLY. THESE FUNDS WERE DESPERATELY NEEDED TO ACCELERATE ONGOING GODR INVESTMENTS FINANCED BY INTERNATIONAL LENDING INSTITUTIONS WHERE LACK OF LOCAL CURRENCY COUNTERPART HAD RESULTED IN WORK STOPAGES OF CRITICAL PROJECTS WHICH WOULD FACILITATE EXPANSION OF PRIVATE

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SECTOR PRODUCTION. IN ADDITION, THE PESOS DISBURSED UNDER THIS ACTIVITY HAVE RESULTED IN THE FREEING UP OF APPROXIMATELY DOLS. 25 MILLION AVAILABLE FOR DISBURSEMENT UNDER EXISTING IDB, IBRD AND AID LOAN AGREEMENTS. THIS ACTIVITY HAS BEEN SUCCESSFUL IN PERMITTING THE COMPLETION OF THE PRINCIPAL HIGHWAY BETWEEN AZUA AND BARAHONA AND THE REHABILITATION AND MAINTENANCE OF APPROXIMATELY 540 KMS. OF RURAL ROADS, ALL IMPORTANT FOR AGRICULTURAL PRODUCTION. IN ADDITION, THIS ACTIVITY HAS: MADE AVAILABLE APPROXIMATELY RD PESOS 3.45 MILLION IN CREDIT TO SMALL FARMERS THROUGH THE IBRD COCOA AND COFFEE LOAN; PROVIDED FUNDS TO SUPPORT ACTIVITIES TO INCREASE SMALL FARMER PRODUCTION AND PRODUCTIVITY UNDER THE IDB INTEGRATED AGRICULTURAL DEVELOPMENT PROJECT (PIDAGRO III); AND PROVIDED RESOURCES TO CONTINUE A MAJOR IDB ASENTAMIENTO DEVELOPMENT PROJECT INCLUDING THE CONSTRUCTION OF 13.6 KMS. OF IRRIGATION CANALS AND 7 AGRICULTURAL INPUT STORES.

3. INSTITUTIONAL SUPPORT AND DEVELOPMENT:

A) PRIVATE SECTOR DEVELOPMENT STUDIES. UNDER THIS ACTIVITY, RD PESOS 1.0 MILLION WAS ALLOCATED TO FINANCE A SERIES OF KEY STUDIES NEEDED TO SUPPORT THE DEVELOPMENT OF IMPORTANT DOMINICAN PRIVATE SECTOR INITIATIVES. FIVE STUDY ACTIVITIES HAVE BEEN IDENTIFIED BY THE GODR AND AGREED TO BY AID. EACH ACTIVITY WILL BE MANAGED BY A DIFFERENT GODR INSTITUTION AND WILL FOCUS ON A DIFFERENT ASPECTS OF THE PRIVATE SECTOR DEVELOPMENT PROBLEM. THE AREAS OF STUDY INCLUDE: FOREIGN INVESTMENT DEVELOPMENT; INDUSTRIALIZATION OF THE PRIVATE SECTOR; PRIVATE SECTOR DEVELOPMENT OF THE SOUTHEAST; FREE ZONE DEVELOPMENT; AND SPECIFIC PRIVATE SECTOR PROJECT FEASIBILITY STUDIES. TO DATE RD PESOS 300,000 HAS BEEN DISBURSED. THE REMAINING FUNDS HAVE BEEN ALLOCATED AND SHOULD BE DISBURSED WITHIN THE NEXT 6 MONTHS.

B) DEVELOPMENT OF A MANAGEMENT TRAINING INSTITUTE: UNDER THIS ACTIVITY, RD PESOS 3.0 MILLION WAS PROGRAMED TO COMPLEMENT A DOLS. 5.0 MILLION AID GRANT FOR THE GRADUATE MANAGEMENT TRAINING PROJECT (NO. 517-0157). THE RD PESOS 3.0 MILLION IS BEING USED TO SUPPORT THE CONSTRUCTION AND EQUIPPING OF THE NEEDED EDUCATIONAL FACILITIES AT THE UNIVERSIDAD CATOLICA MADRE Y MAESTRA (UCMM). CONSTRUCTION IS NOW UNDERWAY AND IS EXPECTED TO BE COMPLETED WITHIN THE NEXT 12 MONTHS.

C) SUPPORT FOR PRIVATE VOLUNTARY ORGANIZATIONS (PVO'S): UNDER THIS ACTIVITY, RD PESOS 4.0 MILLION WAS PROGRAMED TO SUPPORT A SERIES OF IMPORTANT PVO ACTIVITIES IN THE DOMINICAN REPUBLIC. 12 PVO SUBPROJECT PROPOSALS WERE DEVELOPED AND REVIEWED AND APPROVED BY A JOINT AID-GODR COMMITTEE. THE PVO PROJECTS CLOSELY COMPLEMENT OTHER MISSION FUNDED ACTIVITIES AND INVOLVE PVOS WITH SUBSTANTIAL EXPERIENCE IN THE DOMINICAN REPUBLIC. THE SUBPROJECTS FOCUS ON IMPROVING THE PRODUCTION OF THE LOWER INCOME GROUPS IN RURAL AND URBAN AREAS. EACH PVO HAS EXECUTED A FORMAL AGREEMENT WITH STP FOR CARRYING OUT THE PROJECT. NINE OF THE SUBPROJECTS WERE DISBURSED AS LOANS TO THE PVOS AND 3 WERE DISBURSED AS DONATIONS. TO DATE RD PESOS 1.3 MILLION HAS BEEN DISBURSED NOR THE PVO PROJECTS.

10. PROGRAM DESCRIPTION:

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A. GENERAL: THE ADDITIONAL FUNDS TO BE MADE AVAILABLE UNDER THIS AMENDMENT WILL BE DISBURSED IN ACCORDANCE WITH THE FY 83 CDSS AND THE CBI ASSISTANCE STRATEGY OUTLINED ON PAGES 14-15 OF THE ORIGINAL PAAD. THESE ADDITIONAL RESOURCES WILL FURTHER ASSIST THE DOMINICAN REPUBLIC IN CARRYING OUT THEIR RECOVERY PROGRAMS IN A MANNER WHICH PRESERVES THE BASIC TENANTS OF A DEMOCRATIC SOCIETY AND A FREE MARKET ECONOMY. THE FY 83 CDSS STRATEGY IS DESIGNED FROM THE CBI. IT TAKES AS A FUNDAMENTAL ASSUMPTION THAT THE PRIVATE SECTOR'S ROLE IN THE DEVELOPMENT OF THE DOMINICAN ECONOMY MUST BE STRENGTHENED. HELPING THE PUBLIC AND PRIVATE SECTORS TO UNDERSTAND THE NEED FOR A SIGNIFICANT SHIFT FROM IMPORT SUBSTITUTION TO AN EXPORT-ORIENTED PROMOTION BASE, WITH THEIR ASSISTING IN THE CREATION OF A BETTER ENVIRONMENT IN WHICH TO WORK, IS THE MISSION'S HIGHEST PRIORITY. THE RATIONALE FOR A CASH TRANSFER DISCUSSED ON PAGES 15-16 OF THE ORIGINAL PAAD IS STILL VALID. IN ADDITION, THE COVENANTS CONTAINED WITHIN THE EXISTING LOAN AGREEMENT CONCERNING THE USE OF THE US DOLLAR RESOURCES WILL STILL APPLY.

B. USES OF LOCAL CURRENCY COUNTERPART: THE PROCEDURES FOR THE USE OF THE LOCAL CURRENCY COUNTERPART FOLLOWED FOR THE DOLS. 41 MILLION HAVE WORKED WELL AND WILL BE FOLLOWED FOR THE LOCAL CURRENCY UNDER THE AMENDMENT. WITHIN APPROXIMATELY 30 DAYS AFTER THE DISBURSEMENT OF THE DOLS 8 MILLION, THE GODR'S LOCAL CURRENCY COUNTERPART WILL BE DEPOSITED IN A SPECIAL ACCOUNT IN THE CENTRAL BANK FOR THE USES AGREED TO UNDER THE PROGRAM. THE CENTRAL BANK WILL INFORM THE TECHNICAL SECRETARIAT OF THE PRESIDENCY (STP) OF THE DEPOSIT OF ALL PROCEEDS AND WILL ADVISE AID. THIS COUNTERPART WILL BE PROGRAMED JOINTLY BY THE GODR AND AID FOR HIGH PRIORITY PRIVATE SECTOR DEVELOPMENT NEEDS. STP WILL COORDINATE THE GODR PLANNING AND PROGRAMMING ACTIVITIES. PRIOR TO THE DISBURSEMENT OF THE PROCEEDS, STP WILL SUBMIT, FOR AID APPROVAL, A DETAILED IMPLEMENTATION PLAN FOR EACH PROJECT ACTIVITY. UNDER THE LOCAL CURRENCY FUNDED ACTIVITIES, TWO AREAS OF FINANCING HAVE BEEN IDENTIFIED BY THE GODR AS THEIR PRIORITY USES FOR THESE ADDITIONAL FUNDS. SPECIFIC ALLOCATIONS WILL BE THE SUBJECT OF FURTHER NEGOTIATIONS; HOWEVER, GODR PLANS AND PRIORITIES INVOLVE THE FOLLOWING:

1) PRODUCTIVE INFRASTRUCTURE (10 PESOS 5 MILLION): AS PREVIOUSLY DISCUSSED, THE 50 PESOS 10 MILLION ORIGINALLY ALLOCATED UNDER THE ESF PROGRAM AS COUNTERPART TO KEY INTERNATIONALLY FUNDED PROJECTS IS NOW FULLY DISBURSED. THERE STILL EXISTS, HOWEVER, A SUBSTANTIAL NEED TO PROVIDE COUNTERPART RESOURCES TO SUPPORT OTHER PROJECTS WHICH ARE CRITICAL TO THE EXPANSION OF THE DOMINICAN PRIVATE SECTOR. THE GODR ESTIMATES THAT THERE EXISTS AN IMMEDIATE NEED FOR APPROXIMATELY RD PESOS 77 MILLION TO SUPPORT VARIOUS PROJECTS FUNDED BY IBRD, IDB AND AID. ACCORDINGLY, IT IS EXPECTED THAT RD PESOS 5 MILLION PROVIDED UNDER THIS AMENDMENT WILL BE UTILIZED FOR THE PRODUCTIVE INFRASTRUCTURE TO SUPPORT A KEY HIGHWAY PROJECT FUNDED BY IBRD AND RURAL ROADS PROJECTS FUNDED

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BY IDB AND AID. THESE COUNTERPART FUNDS SHOULD FREE UP APPROXIMATELY DOLS. 12.5 MILLION AVAILABLE FOR DISBURSEMENT UNDER IBRD, IDB AND AID LOAN PROJECTS. STP WILL DEVELOP A LISTING OF PRIORITY PRODUCTIVE INFRASTRUCTURE PROJECTS TO BE FUNDED UNDER THE AMENDMENT FOR AID APPROVAL. ANY CHANGES IN THIS LISTING WILL REQUIRE AID CONCURRENCE. STP WILL SUBMIT QUARTERLY REPORTS TO AID ON THE DISBURSEMENT AND USAGE OF THESE FUNDS.

2) FREE ZONE DEVELOPMENT (RD PESOS 2 MILLION)

A) THE GODR AND THE PRIVATE SECTOR HAVE CREATED VARIOUS FREE ZONE AREAS IN DIFFERENT PARTS OF THE COUNTRY TO STIMULATE INDUSTRIAL DEVELOPMENT. FOUR FREE ZONES ARE CURRENTLY IN EXISTENCE. ONE OF THESE, THE PUERTO PLATA FREE ZONE, OFFERS CONSIDERABLE OPPORTUNITY AND POTENTIAL IN THE SHORT-TERM FOR INCREASING EMPLOYMENT AND FOREIGN EXCHANGE. THE PUERTO PLATA FREE ZONE AREA IS A RELATIVELY LARGE SITE WITH BASIC INFRASTRUCTURE IN PLACE TO SUPPORT FOUR LARGE INDUSTRIAL BUILDINGS. THE SITE IS WELL LOCATED IN PUERTO PLATA WHERE THERE IS AN INTERNATIONAL AIRPORT, A LARGE PORT ON THE ATLANTIC OCEAN, GOOD ROADS, CUSTOMS FACILITIES, ACCESS TO PUBLIC UTILITIES, AND A LARGE SOURCE OF UNEMPLOYED TRAINABLE LABOR. THE EXISTING FREE ZONE FACILITIES ARE CURRENTLY FULLY EMPLOYED AND ACCORDING TO SENIOR GODR OFFICIALS THERE ARE OVER FIFTY-FIVE APPLICATIONS OUTSTANDING FOR INDUSTRIAL SITES AT THE PUERTO PLATA FREE ZONE.

B) THE GODR IS THEREFORE CONTEMPLATING USING UP TO RD PESOS 3 MILLION TO BE MADE AVAILABLE UNDER THIS AMENDMENT TO EXPAND THE PUERTO PLATA FREE ZONE FACILITIES. THIS PROJECT WILL APPROXIMATELY DOUBLE THE EXISTING CAPACITY OF THE PUERTO PLATA FREE ZONE FACILITIES THROUGH THE CONSTRUCTION OF ADDITIONAL BUILDINGS. THIS PROJECT WILL BE CARRIED OUT BY THE DOMINICAN FREE ZONE CORPORATION WHICH COMES WITHIN THE ADMINISTRATIVE STRUCTURE OF THE GODR SECRETARIAT OF INDUSTRY AND COMMERCE. THE COUNTERPART FUNDS WILL BE PROVIDED UNDER THE PRIVATE SECTOR DEVELOPMENT FUND THROUGH FIDE OR ANOTHER APPROPRIATE DISBURSEMENT MECHANISM.

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C. FINANCIAL SUMMARY.

1. THE FOLLOWING IS THE REVISED FINANCIAL PLAN FOR THE AMENDED PROGRAM:

MAJOR OUTPUTS:	ALL YEARS (MILLIONS) UNIT COST
AID-FINANCED:	
1. BALANCE-OF-PAYMENT SUPPORT (PRIVATE SECTOR IMPORTS FROM US)	XXX DOLS. 49.0
GODR-FINANCED:	
1. SUB-LOANS FROM PRIVATE SECTOR DEV. FUND	XXX RD PESOS 26.0
2. PROJECTS SUPPORT UNDER INFRASTRUCTURE DEV. FUND	XXX RD PESOS 15.0
3. INSTITUTIONAL DEV. AND SUPPORT	XXX RD PESOS 8.0

D. NEGOTIATING STATUS. REPRESENTATIVES OF GODR HAVE BEEN WORKING CLOSELY WITH THE MISSION STAFF ON ALL ASPECTS OF THE PAAD AMENDMENT. THERE ARE NO REMAINING ISSUES WHICH WILL REQUIRE SUBSTANTIVE NEGOTIATION. THE MISSION AND THE GODR INTEND TO OBLIGATE THE LOAN AMENDMENT BEFORE THE END OF FY 83. ONCE THE PAAD IS APPROVED, THE AMENDMENT TO THE PROJECT AGREEMENT WILL BE PREPARED (WITH THE ASSISTANCE OF THE RLA) AND NEGOTIATED WITH THE GODR (PRINCIPALLY SEPC). THE AMENDMENT WILL THEN BE REVIEWED AND APPROVED BY THE LEGAL ADVISOR TO THE PRESIDENT AND SIGNED ON SEPTEMBER 30, 1983. NO UNUSUAL DELAYS ARE EXPECTED IN THIS PROCESS.

ANNEX 1
DOMINICAN REPUBLIC

BALANCE OF PAYMENTS

(MILLIONS OF DR PESOS)

	1981	1982	(PROJECTED) 1983
TRADE BALANCE	-263.7	-489.6	-458.0
EXPORTS	1,188.0	767.7	792.0
IMPORTS	1,451.7	1,257.3	1,250.0
(PETROLEUM)	(497.4)	(445.5)	(444.4)
NET SERVICES	-335.2	-15.1	-127.0
TOURISM	78.5	175.1	252.0
INTEREST	-293.1	-254.1	-289.3
OTHER	-120.6	-82.3	-90.8
BALANCE OF GOODS AND SERVICES	-598.9	-640.9	-585.0
UNREQUITED TRANSFER	193.0	205.0	215.0
CURRENT ACCOUNT BALANCE	-405.9	-441.9	-378.8
CAPITAL ACCOUNT	244.7	107.0	283.2
NET PRIVATE CAPITAL	56.3	-121.4	-5.9
FOREIGN INVESTMENT	79.4	-1.4	26.0
LOANS	-33.5	-46.4	-46.5
OTHERS	18.1	-73.6	14.6
NET OFFICIAL CAPITAL	188.4	228.4	289.1
ERRORS AND OMISSIONS	-14.7	2.1	2.4
OVERALL BALANCE	146.5	337.8	89.2
(MINUS EQUALS INCREASE)			

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12/20/83
10:00 a.m.

DAEC: DOMINICAN REPUBLIC PAAD

Irwin Loop	LAC/DR
Susan Merrell	LAC/DR
Wendy Sickel	LAC/DR
Robert W. Adler	LAC/DP
Pauline Johnson	GC/LAC
Douglas P. Browne	LAC/DP
BRUNO KOSHELUK	LAC/CAR (DESK)

RECORD COPY

SEP 29 9 20 AM '82

EXECUTIVE SECRETARIAT

ACTION MEMORANDUM FOR THE ADMINISTRATOR

SEP 27 1982

THRU : ES

THRU : AA/PPC, John Bolton

FROM : AA/LAC, Otto J. Reich

SUBJECT: Program Assistance Approval Document (PAAD) - Dominican Republic

Problem: To authorize a $41.0 million loan from the Economic Support Fund (ESF) Supplemental to the Government of the Dominican Republic (GODR).

Background: In recent years the Dominican economy has been adversely affected by three major events which have precipitated the current severe foreign exchange and fiscal crisis. They are: (1) Hurricane David in late 1979 that caused extensive damage to the country's infrastructure; (2) the 1979 doubling of world oil prices that raised the import bill of petroleum products from 29 percent of total export earnings in 1978 to 42 percent in 1981; and (3) the world economic recession of 1981-1982 that has caused serious deterioration in the Dominican economy primarily due to depressed international prices for its major exports.

In response to a desperate economic situation, the newly-elected government of President Jorge Blanco, who assumed office in August 1982, immediately formulated both short- and long-term strategies aimed at economic recovery. These strategies are consistent with recommendations presented to the GODR by the World Bank in June 1982 calling for a narrowing of the central government's fiscal deficit, a spurring of the sagging Dominican private sector, and promotion of non-traditional exports to improve the country's foreign exchange position. Nevertheless, it will take time for these remedial actions to have a significant positive impact and, in the short run, there is concern that current difficulties could steadily impose worsening economic hardships on the Dominican people and cause severe structural damages to the economy.

The new administration will not only have to face the country's economic difficulties and undertake a series of difficult and far-reaching measures, but will also have to convince the Dominicans that its economic problems are being addressed effectively, that short-term austerity measures will pay off in the longer term, and that sacrifices will be shared equitably within the society. This is an extremely difficult task for the new government, and the reaction of the country is unknown. Nevertheless, the GODR has demonstrated that it is determined to confront the current economic crisis. In addition to its announcement and implementation of a series of economic reforms, the GODR is in the process of negotiating an IMF agreement. It is anticipated that this agreement will be reached by the end of the calendar year. It is against this backdrop that the U.S. offers assistance to ease the strain of the austerity measures the GODR is committed to take and to provide immediate balance-of-payments support.

Discussion: The attached PAAD proposes to provide a $41.0 million loan from ESF to the GODR through a cash transfer to the Dominican Central Bank. The cash transfer approach is considered the most appropriate because of the

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immediate need for disbursement of dollars to provide balance-of-payments support and, specifically, to respond to demands for foreign exchange by the private sector. Foreign exchange will be made available from the loan subject to a covenant that in the succeeding twelve months the GODR will allocate at least an equivalent amount of foreign exchange to the private sector for the importation of raw materials, and intermediate and capital goods from the United States.

Within approximately a month of disbursement of the loan, the local currency generated from the program will be deposited in a special account in the Central Bank for uses agreed to by the GODR and the U.S. under the assistance program. The GODR has identified three areas of financing which respond to high priority private sector development needs. Although specific allocations of local currency generations will be subject to further negotiations between the GODR and the Mission, and subsequent presentation to A.I.D./W for approval, GODR plans and priorities include the following: (1) capitalization of a credit facility within the Central Bank to increase the volume of credit to the private sector for expansion of agribusinesses and export activities ($25.0 million); (2) capitalization of a productive infrastructure fund to accelerate on-going GODR investments financed by AID, the IDB and the IBRD where lack of local currency counterpart has resulted in work stoppage of projects deemed critical to expanded private sector productivity ($10.0 million); and (3) private sector training and technical assistance, and financial support for private voluntary organizations ($6.0 million).

The LAC Bureau's Development Assistance Executive Committee (DAEC) reviewed the PAAD and recommended approval on September 24, 1982, subject to certain revisions. Principal revisions are: (1) the inclusion of a covenant and side letter indicating that the CBI funds, including local currency generated, should not be used in a manner which will cause serious injury to the production, marketing or pricing of U.S. agricultural commodities or products; (2) the inclusion of a requirement that a least 80 percent of the credit funds be directed at small and medium export and agribusiness activities; (3) institutionalization of measures within the GODR to ensure that special emphasis be placed upon lending to cooperatives, including setting aside a portion of funds for feasibility studies which will identify cooperative projects for financing under this program; (4) an increase in assistance for private voluntary organizations; and (5) the inclusion of a general covenant that mutual agreement between the GODR and A.I.D. is to be reached on the programming of all local currency generated under the cash transfer.

Justification to Congress: Since funds were appropriated by the U.S. Congress for the Dominican Republic in the Caribbean Basin Initiative FY 1982 Supplemental, no further notification of Congress is required.

Recommendation: That you sign the attached PAAD facesheet authorizing $41.0 million for the Dominican Republic.

Attachment: Dominican Republic PAAD

LAC/DR:KPeake:rjw:9/27/82:X29484

Clearances:

PPC:PDPR:JEriksson
GC:CLvanOrman CLvO 28Sep

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CLASSIFICATION:

AID 1120-1 (8-66)

PAAD.

DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT

PROGRAM ASSISTANCE APPROVAL DOCUMENT

1. PAAD NO.: 517-K-039
2. COUNTRY: Dominican Republic
3. CATEGORY: Cash Transfer
4. DATE: September 17, 1982
5. TO: M. Peter McPherson, Administrator
6. OYB CHANGE NO.:
7. FROM: Otto J. Reich, AA/LAC
8. OYB INCREASE
TO BE TAKEN FROM: Economic Support Funds (ESF)
9. APPROVAL REQUESTED FOR COMMITMENT OF: $ 41,000,000
10. APPROPRIATION - ALLOTMENT
11. TYPE FUNDING: [X] LOAN [ ] GRANT
12. LOCAL CURRENCY ARRANGEMENT: [ ] INFORMAL [X] FORMAL [ ] NONE
13. ESTIMATED DELIVERY PERIOD: FY 83
14. TRANSACTION ELIGIBILITY DATE: Date of approval
15. COMMODITIES FINANCED: N/A

16. PERMITTED SOURCE	17. ESTIMATED SOURCE
U.S. only:	U.S.: $41,000,000
Limited F.W.:	Industrialized Countries:
Free World:	Local:
Cash: $41,000,000	Other:

18. SUMMARY DESCRIPTION

The program proposes to: a) provide immediate balance-of-payment relief to the Dominican economy by provision of a $41 million cash transfer to the Central Bank; b) utilize these funds to pay for imported inputs of necessary U.S. goods and services for the private sector; c) provide, as counterpart funding, the peso equivalent of $41 million to be held in special accounts and aimed, with U.S. concurrence, at high priority private sector development needs in three areas: (i) $25 million for financing private sector export promotion and agribusiness projects; (ii) $6 million for training programs and institutional strengthening of organizations involved in private sector development; and (iii) $10 million to assist GODR investment in productive infrastructure necessary for expansion of private sector activities.

The GODR will agree to allocate foreign exchange to the private sector for the importation of spare parts, capital goods and industrial and agricultural inputs from the U.S. in an amount at least equivalent to the loan over a one-year period. Covenants will be included in the loan agreement which will require, inter alia, (1) use of A.I.D. assistance in a manner which will not cause injury, or the threat thereof, to the production, marketing, or pricing of U.S. agricultural commodities or products; and (2) the implementation of the provisions of Section 203(a) of the draft authorization markup for the FY 1982 supplemental which prescribes requirements relating to the use of funds. Details regarding the

(see continuation on next shee

19. CLEARANCES	DATE
REG/DP	9/22
REG/GC	9-27
AA/PPC	9-28/82
M/FM	9-27-82
GC:CLvanOrman	28 Sept
ARA/ECP:CAllen	9/27
LAC/DR:ILevy	9.27

20. ACTION
[X] APPROVED [ ] DISAPPROVED
AUTHORIZED SIGNATURE: Frank B. Kimball — DATE: 9/29/82
Counselor to the Agency
TITLE

CLASSIFICATION:

18. Continuation of Summary Description

implementation of these covenants will be spelled out in a separate side letter.

The dollar loan will be repaid in 25 years with a 10-year grace period. The interest will be 2% during the grace period and 3% thereafter.

be obligated until the IMF and GODR have reached agreement on the targets for the second year of their Extended Fund Facility (EFF) Agreement. Evidence that this agreement has been reached should be submitted by the GODR, with the endorsement of the IMF. Upon approval by AID/W, the Mission will then be authorized to obligate these funds.

The loan is for a 25-year term with a 10-year grace period. Interest is set at 2 percent during the grace period and 3 percent thereafter. The implementing agency is the Technical Secretariat of the Presidency.

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Clearances:
LAC/CAP:BKoeheleff
LAC/DP:DBroome
GC/LAC:FLeihgan
LAC/DP:LArmstrong
LAC/DP:CLechuro
LAC/DP:ILevy
H/PM:CCristensen LMD/SQuiers (phone)
ARA/ECP:CAllen
DAA/LAC:MSBrown
PPC/PDPR:JHrikason
GC:CLyanOrman