

PD-006-009 (2)

527-80-1101  
4201

UNCLASSIFIED

5278011

UNITED STATES INTERNATIONAL DEVELOPMENT COOPERATION AGENCY  
AGENCY FOR INTERNATIONAL DEVELOPMENT  
Washington, D. C. 20523

PERU

PROJECT PAPER

UPGRADING LOW-INCOME SETTLEMENTS

AID/LAC/P-059

Project Number 527-HG-011

UNCLASSIFIED

AGENCY FOR INTERNATIONAL DEVELOPMENT  <b>PROJECT PAPER FACESHEET</b>	1. TRANSACTION CODE <input type="checkbox"/> A ADD <input type="checkbox"/> C CHANGE <input type="checkbox"/> D DELETE	PP 2. DOCUMENT CODE 3

3. COUNTRY ENTITY 1 PERU	4. DOCUMENT REVISION NUMBER <input type="checkbox"/>
-----------------------------	---

5. PROJECT NUMBER (7 digits) [ 527-HG-011 ]	6. BUREAU, OFFICE A SYMBOL LA B CODE [ 05 ]	7. PROJECT TITLE (Maximum 40 characters) [ Upgrading Low-Income Settlements ]
--	--	--

8. ESTIMATED FY OF PROJECT COMPLETION FY [ 83 ]	9. ESTIMATED DATE OF OBLIGATION A. INITIAL FY [ 81 ] B. QUARTER <input type="checkbox"/> C. FINAL FY [ 81 ] Enter 1, 2, 3 or 4
--	--

A. FUNDING SOURCE	FIRST FY			LIFE OF PROJECT		
	B. FX	C. L. C.	D. TOTAL	E. FX	F. L. C.	G. TOTAL
AID APPROPRIATED TOTAL						
GRANT						
LOAN						
OTHER U.S. Housing Guaranty			20,000			20,000
2. IIPUP Grant			100			100
HOST COUNTRY ECV			2,223			2,223
OTHER DONORIS: Down Payments			1,171			1,171
TOTALS			23,494			23,494

A. APPROPRIATION	B. PRIMARY PURPOSE CODE	PRIMARY TECH. CODE	E. 1ST FY 81		H. 2ND FY 82		K. 3RD FY 83	
			C. GRANT	D. LOAN	GRANT	J. LOAN	L. GRANT	M. LOAN
1. HG	720	866		6,000		10,000		4,000
2. IIPUP		100						
3. (FY 1981)								
TOTALS				6,000		10,000		

A. APPROPRIATION	N. 4TH FY		O. 5TH FY		LIFE OF PROJECT		12. IN-DEPTH EVALUATION SCHEDULED
	D. GRANT	P. LOAN	R. GRANT	S. LOAN	T. GRANT	U. LOAN	
HG						20,000	MM YY 1   2   8   3
2. IIPUP Grant (FY 1980)						100	
TOTALS						20,100	

13. DATA CHANGE INDICATOR. WERE CHANGES MADE IN THE PID FACESHEET DATA BLOCKS 12, 13, 14 OR 15 OR IN PRP FACESHEET DATA BLOCK 12? IF YES, ATTACH CHANGED PID FACESHEET.

14. ORIGINATING OFFICE CLEARANCE  
 NO  
 YES

15. DATE DOCUMENT RECEIVED IN AID/W OR FOR AID/W DOCUMENTS, DATE OF DISTRIBUTION	16. DATE SIGNED
SIGNATURE Leonard Yaeger	DATE SIGNED MM DD YY 0   9   0   1   8   0
TITLE Director USAID/Lima	MM DD YY

UNITED STATES INTERNATIONAL DEVELOPMENT COOPERATION AGENCY  
AGENCY FOR INTERNATIONAL DEVELOPMENT  
WASHINGTON D C 20523

ASSISTANT  
ADMINISTRATOR

GUARANTY AUTHORIZATION

PROJECT 527-HG-011

Provided From: Housing Guaranty Authority

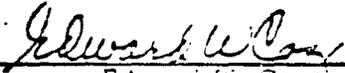
For Housing Bank of Peru

Pursuant to the authority vested in the Assistant Administrator, Bureau for Latin America and the Caribbean, by the Foreign Assistance Act of 1961, as amended (FAA), and the delegations of authority issued thereunder, I hereby authorize the issuance of guaranties pursuant to Section 222 of the FAA of not to exceed twenty million dollars (\$20,000,000) in face amount, assuring against losses (of not to exceed one hundred percent (100%) of loan investment and interest) with respect to loans by eligible U.S. investors (Investor) acceptable to A.I.D. made to finance basic services for upgrading low-income settlements in Peru.

These guaranties shall be subject to the following terms and conditions:

1. Term of Guaranties: The loans shall extend for a period of up to thirty years (30) from the date of disbursement and may include a grace period of up to ten years on repayment of principal. The guaranties of the loans shall extend for a period beginning with disbursement of the loans and shall continue until such time as the Investor has been paid in full pursuant to the terms of the loans.
2. Interest Rate: The rate of interest payable to the Investor pursuant to the loans shall not exceed the allowable rate of interest prescribed pursuant to Section 223(f) of the FAA and shall be consistent with rates of interest generally available for similar types of loans made in the long term U.S. capital markets.
3. Government of Peru Guaranty: The Government of Peru shall provide for a full faith and credit guaranty to indemnify A.I.D. against all losses arising by virtue of A.I.D.'s guaranties to the Investor or from non-payment of the guaranty fee.
4. Fee: The fee of the United States shall be payable in dollars and shall be one-half percent (1/2%) per annum of the outstanding guarantied amount of the loans plus a fixed amount equal to one percent (1%) of the amount of the loans authorized or any part thereof, to be paid as A.I.D. may determine upon disbursements of the loans.

5. Other Terms and Conditions: The guaranties shall be subject to such other terms and conditions as A.I.D. may deem necessary.

  
\_\_\_\_\_  
Edward W. Coy  
Acting Assistant Administrator  
Bureau for Latin America and the Caribbean

9-25-80

Clearances:

DS/H:DMcVoy	_____	Date	9/27/80
DS/H:MSorock	MS	Date	9/22/80
GC/H:BDavis	BD	Date	9/22/80
FM/LD:EWilson	_____	Date	_____
LAC/SA:WRhodes	_____	Date	_____
LAC/DR:MBrown	MS	Date	_____
GC/LAC:BVeret	BV/LW	Date	7/21/80

GC/H:BBDAVIS:prj:09/15/80

P E R U  
UPGRADING LOW-INCOME SETTLEMENTS  
PROJECT PAPER

TABLE OF CONTENTS

	Page
I. <u>SUMMARY AND RECOMMENDATION</u> .....	1
A. Recommendation.....	1
B. Description of the Project.....	1
C. Summary of Findings.....	2
1. Outputs	
2. Inputs	
3. Economic and financial findings	
4. Environmental considerations	
5. Policy Issues	
D. Project Issues.....	4
1. Project strategy	
2. Absorptive capacity	
3. Sub-project components	
4. Effective demand and affordability	
5. GOP financial commitment to cover foreign exchange losses	
II. <u>PROJECT DESCRIPTION</u> .....	12
A. Background.....	12
1. Overview	
2. Shelter constraints	
3. Mission Strategy	
4. Target group	
5. Relation to GOP priorities	
6. History of proposed project	
B. Detailed Project Description.....	14
1. The project	
2. Project objective	
3. Participating institutions	
4. Project outputs	
5. Project inputs	
III. <u>PROJECT ANALYSIS</u> .....	16
A. Economic Analysis.....	16
1. The current economic situation	
2. GOP capacity to repay	
3. Economic benefits	
B. Financial Analysis.....	19
1. Effective demand for project items	
2. Cost Recovery	
3. Summary financial plan	

C.	Administrative Feasibility.....	22
1.	Summary assessment	
2.	BVP	
3.	Utility concessionaires	
4.	The Savings and Loan System	
5.	Neighborhood councils	
D.	Social Analysis.....	28
1.	The social landscape	
2.	Organizational context	
3.	Institutional relationships	
4.	Motivation	
5.	Obstacles	
6.	Communication strategies	
7.	Spread effects	
8.	Social consequences and benefit incidence	
9.	Changes in power and participation	
E.	Technical Feasibility.....	34
1.	Technical considerations	
2.	Construction aspects	
3.	Environmental Considerations	
F.	Technical Assistance.....	38
G.	Other Donors.....	39
IV.	<u>IMPLEMENTATION</u> .....	40
A.	Implementation.....	40
B.	Evaluation.....	41
C.	Covenant and Negotiating Status.....	42

#### ANNEXES

A.	Draft Authorization
B.	GOP Letter of Application
C.	Statutory Checklist
D.	Logical Framework
E.	PID Issues Cable
F.	Social Soundness Analysis
G.	Initial Environmental Examination and BVP Environmental Checklist
H.	Current Economic Setting: Mission Analysis
I.	Median Household Incomes
J.	Affordability of Sub-projects
K.	FONAVI: A National Housing Fund for Peru
L.	BVP Financial Position
M.	Illustrative Cost Estimates for Public Utility Projects
N.	Flow Chart for Implementation of a Service Program
O.	USAID/Peru's Urban Strategy (FY 80 - FY 84)

## ABBREVIATIONS AND ACRONYMS

BVP	National Housing Bank
ElectroPeru	Electricity Company of Peru
ElectroLima	Electricity Company of Lima
ESAL	Sanitary Company of Lima
ESAR	Sanitary Company of Arequipa
DGOS	MOHC Department of Sanitation
MOHC	Ministry of Housing and Construction
SINAMOS	National System of Social Mobilization

## UPGRADING LOW-INCOME SETTLEMENTS

### I. SUMMARY AND RECOMMENDATION

#### A. Recommendation

Based upon a review of the proposal set forth in this paper, it is recommended that the subject guaranty be approved as follows:

Amount of Guaranty: US\$20.0 million to the Banco de la Vivienda del Peru (BVP: National Housing Bank), the Borrower, for upgrading low-income urban settlements.

Term: The loan will be for a term of up to 30 years with a grace period of up to 10 years for the payment of principal to be negotiated with the investor.

Interest Rate: The interest rate payable to the U.S. investor shall not exceed the allowable rate of interest prescribed by the AID Administrator pursuant to Section 223(1) of the FAA, and shall be consistent with rates of interest generally available for similar type loans.

#### B. Description of the Project

The goal of the project is to increase the supply of basic services affordable by low-income families. The project purpose is to assist the GOP to continue to finance a minimum level of basic infrastructure and community facilities in low-income settlements in Lima and in other rapidly growing urban centers. To this end, the project will continue to address the major deficit of basic services of the target group, low-income urban families living in pueblos juvenes and similar settlements, by financing:

- a. affordable packages of water, sewerage, and electricity services,
- b. ancillary community facilities, and
- c. home improvements.

Half of the HG funds would be used in cities outside the Lima Metropolitan Area.

The project is part of the Mission's Urban Strategy (FY80-FY83), which includes the proposed project, and is consistent with the CDSS.

BVP would be the Borrower for the project. BVP is a state-owned, semi-autonomous institution created in 1962. In 1969 it received authority to mobilize funds domestically, through the issuance of mutual development bonds, and to extend credits for housing and construction. This included financing to housing cooperatives, public and private developers, lending for urban renewal and redevelopment projects in poor areas, and lending for experimental projects.

The BVP has extensive experience with AID-financed housing programs. Starting in 1962 with a \$7.5 million AID seed capital loan for initiating the S&L system in Peru, BVP has subsequently administered and/or implemented \$82 million of AID-funded shelter programs. It also administers AID DG and DL funds. In the present loan, BVP will provide the S&L's \$2,137,000 of HG funds for on-lending for home improvements.

ElectroPeru, ElectroLima, and the Electric Company of Arequipa as participating agencies in the case of electrification programs in pueblos jóvenes and similar settlements, would be responsible for carrying out the construction of the electricity infrastructure projects. Upon completion of the projects, the utility company would collect on behalf of the BVP from the individual households a single monthly payment covering authorization of the secondary network and the household connections as well as the charge for electricity consumption.

ElectroPeru is an autonomous public institution controlling all electrical production in the country either directly or through ownership of a majority of the stock of the associated electric companies. It has been quite effective in working with the BVP.

ESAL, the Sanitary Company of Arequipa (ESAR), and the Sanitary Works Department of the Ministry of Housing (Dirección General de Obras Sanitarias DGOS) will be responsible for civil works construction in water supply and sewerage sub-projects. The utility concessionaire would collect the monthly payments on behalf of the BVP from the individual household. Repayments would cover the capital costs as well as the cost of water consumed. ESAL and ESAR are autonomous public entities responsible for all water and sewerage projects in their respective jurisdictions. DGOS has responsibility in secondary cities. Their technical staffs are competent and enjoy a growing experience of extending service to the target group.

A formal socio-political structure exists in all pueblos jóvenes and similar settlements in Peru's cities. The GOP, first through the National System of Social Mobilization (SINAMOS) and more recently through the Ministry of Housing and Construction (MOHC), has supported and strengthened the development of formal mechanisms to facilitate communication and participation.<sup>1/</sup> The community organizations make it possible for their residents to deal with the government and other institutions.

An important feature of this project is the active participation of the communities served, both in the design and construction of the individual components. This participation not only should reduce the cost of the proposed works and thus increase the number of people who can afford the programs, but it also has an important social effect in promoting community cohesion.

### C. Summary of Findings

On the basis of infrastructure service projects presently being carried out with AID assistance, the Mission is confident that the BVP, the utility concessionaires, the private construction industry, and the community organizations in the pueblos jóvenes and similar areas all have sufficient technical and managerial capacity to participate in the program in an effective manner.

<sup>1/</sup> SINAMOS was deactivated in 1978 and its functions transferred to the MOHC. See Annex F ("Social Soundness Analysis") for a description of the role played by SINAMOS.

1. Outputs. The actual sub-project mix of water, sewerage infrastructure, electricity, home improvements, and community facilities will vary with each sub-project depending upon the preferences and ability to pay of each borrower. Nevertheless, depending on the wishes of each community and home improvement loan borrower, it would be possible to finance some 31,500 solutions plus \$750,000 of community programs. (See Section III-B-3, "Summary Financial Plan.")

water	11,000
sewerage	7,600
electricity	2,700
home improvements	4,200

This calculation assumes that \$2.5 million of project resources will be for home improvements; and that the remaining 90% will be allocated in the proportions of 40:20:40 respectively for water, sewerage, and electricity in Lima and 45:45:10 in the Provinces.

2. Inputs. The outputs would be financed by a total of \$23,394,000 as follows:

down payments (5%)	\$ 1,171,000
HG funds (90% of balance)	20,000,000
BVP funds (10% of balance)	<u>2,223,000</u>
Estimated First Round Total:	\$23,394,000

The reflows and earnings will be relent to reproduce the project in the second and subsequent rounds.

3. Economic and Financial Findings. Based in large part on an extremely good external account performance in 1979, Peru is beginning to come out of its most severe recession, 1977-79, since World War II. The new government, which was elected in May 1980 and is scheduled to take office in July, will have to focus on policies promoting economic recovery; but barring unforeseen and very adverse movements in the terms of trade or gross economic mismanagement, GDP growth on the order of 6.5% a year should be possible through 1985. The long-term prognosis is favorable. The GOP easily will be able to service the proposed loan.

The effective demand will far exceed project resources. A rapid commitment of project resources is expected and project funds should be committed within 2 years. The proposed project will pose no financial difficulties for the BVP. Section III-C ("Administrative Feasibility") concludes that the experience and capability of the participating entities will ensure smooth project implementation.<sup>1/</sup>

4. Technical Findings and Environmental Considerations. The technical analysis provides reassurance that there are no effective constraints in the construction industry, in the supply of materials, nor in the technical capability of participating entities.

<sup>1/</sup> Section III-D ("Social Analysis") does caution that the neighborhood councils, in particular, may need technical assistance in some cases if they are to fulfill successfully their expected role.

4. Environmental Considerations. Annex G examines and deals with the project's environmental issues. The Initial Environmental Examination sets forth the critical concerns associated with this HG. During the preparation of the Project Paper, it became evident that the foreseeable positive impacts of the proposed action should markedly outweigh the foreseeable negative impacts. Therefore, from the environmental standpoint, the program should be authorized. By its nature a program which brings services to those who totally or partially lack them should be a major improvement to the environment.

There are, nevertheless, some potential negative impacts associated with the upgrading of services. Program development should include detailed environmental considerations as to infrastructure delivery capabilities and the hazards of the natural setting. Appropriate planning can be employed to minimize potential negative impacts.

An environmental checklist was developed with the BVP to ensure that sub-projects are environmentally sound (see Annex G). It will be used to determine which pueblos jovenes and similar low-income areas are to receive upgrading assistance. The selection process will be on a project-by-project basis within the context of the strategy of the MOHC for upgrading these areas. The checklist will make certain that site selection will be restricted to those areas which are not environmentally sensitive or disaster-prone. Potable water, sewerage, and electricity will be supplied only in those situations where they can be readily supplied once the on-site infrastructure work is accomplished. The environmental checklist developed under the previous program should be applied now; and project development should be monitored by selected site visits.

5. Policy issues. The project recognizes that Peru does not have a satisfactory set of shelter sector policies. It suggests the types of position background studies which should be begun now so that the new government will have a basis for considering the issues. Technical assistance could be provided to assist these analyses as needed.

D. Project Issues

The major issues raised by the DAEC review of the PID (Annex E) concerned:

1. Project Strategy. The severe economic crisis and recession in the past few years have compelled the Mission to concentrate its shelter sector activities on emergency efforts to deliver basic infrastructure services to the target group. There are signs that the economic situation now has bottomed out and that conditions are beginning to improve.

It is anticipated that many of the shelter issues posited in the FY-80 PID guidance cable (e.g., the erosion of the financial base of the housing system; insufficient GOP budgetary allocations to the sector; and the use of a tax, FONAVI, to keep the construction industry alive) will be resolved

with increases in urban sector real incomes which will accompany improvements in the overall economic condition of the country. The Mission believes that very little in the way of addressing long-term development issues can be accomplished without this recovery.

Section II-A-2 summarizes the reasons for the current lack of effective demand for housing. The Mission will continue to discourage the financing of low-cost housing projects until real incomes permit the purchase of dwelling units on a cost recovery basis. In the meantime, the Mission will encourage the GOP to continue financing basic communal services that are affordable to the target group as well as providing credit for self-help construction and/or improvement of dwellings.

The subsidies presently being provided to the housing finance system can be divided into three categories: (a) budgetary allocations to the MOHC and occasional capitalization of the Housing Bank, (b) emergency subsidies to keep the housing finance system intact during a period when loan portfolio earnings are substantially lower than deposit (liability) payments, and (c) the GOP payment to the BVP for losses on external credits arising from exchange devaluation. In total, these GOP allotments subsidies amount to approximately \$153.3 million for 1980.

The need for emergency subsidy to the S&L system has arisen from successive differential increases in interest rates on the credits and deposit liabilities of Peru's financial intermediaries. Interest rates have been increased with the aim of eventually creating "real interest rates", i.e., rates of interest higher than the rate of inflation. Since S&L borrowers' incomes have not risen as rapidly as the rate of inflation, the GOP decided to permit only a partial upward adjustment of interest rates on old loans (from 13 to 18 percent) while allowing deposit rates to rise to over 30 percent p.a. and to compensate S&L and the BVP for the de facto negative real interest rates on their loan portfolios. This compensatory subsidy is provided to the S&L's and to the BVP with institution-specific credit lines (bearing 9% p.a. interest) granted by the Central Bank which can be used solely for purchasing public credit bonds (bearing 37% p.a.). In 1980 (and as compensation for the 1979 portfolio losses) the S&L's will receive S/.1,187 million and the Housing Bank will receive S/.1,070 million (approximately \$4.2 million and \$3.8 million respectively).

The GOP subsidy to the BVP for foreign exchange losses is calculated by comparing the scheduled debt service with the actual (present) quantity of soles needed for debt service. Devaluation increases the sole obligation. For the period 1975-1979 the BVP was compensated S/.1,067 million for losses on exchange devaluation (approximately \$6.9 million). It is expected that the exchange devaluation loss for 1980 will amount to \$2.8 million. Even if the sole were not further devaluated, the exchange devaluation loss would continue for several years. For example, by December 1979 a monthly payment in soles equivalent to \$100 prior to September 1975 was equivalent to only \$15.69. The Mission estimates that the service of external loan obligations of the BVP originating prior to 1976 will require subsidy of at least 80%. We estimate the magnitude of that annual subsidy in the \$4-5 million range for 1981-1985.

Despite the budget austerity program of the Central Government, Peru's contribution to the shelter sector has been on the rise. In addition to the subsidies to S&L's and BVP, the Central Government has allocated \$49.8 million in CY-79 and \$142.5 million in CY-80 for shelter related activities.

The Mission will, in negotiating a \$15 million 527-HG-010 loan, begin to encourage the new government to organize itself for a major review of its urban growth plans and programs so as to change from emergency-type programs to longer range development programs. The Mission is optimistic about the opportunity to work with the new government in developing ways to more effectively deliver basic services to the poor. Urban development policy will be a crucial area for the new government and for foreign assistance donors. Both AID and the World Bank support the convening of the Peru Consultative Group as soon as possible. This body should encourage the GOP to develop a more comprehensive urban development policy, including the definition of investment programs to which aid donors can rapidly respond.

The PID guidance cable suggested that the Mission begin the information gathering phase of a policy review with the military government so as to pave the way for the formal review of the sector to be undertaken by the new government. This was not possible because the MOHC and the BVP undertook a series of emergency measures designed to leave a good impression with the public. All senior management attention was focussed on implementing these activities (e.g., FONAVI).

By the end of June 1980, the Mission revised its urban strategy and indicated that it was not sure when it could begin to work with the government in organizing a major review of its urban growth plans and programs. The Mission did, however, mention that it would begin to articulate its interest in the GOP undertaking a policy review when negotiating this loan (011). (See Conditions Precedent, pp. 42-43).

The new government assumed power on July 28, 1980. Shortly before Belaunde's inauguration, the Mission began to meet regularly with key representatives of the urban sector. At the request of the principal advisor to the Minister of Housing, the Mission prepared a brief statement on USAID/Peru's urban programs and expressed our interest in knowing how the GOP would deal with such questions as:

- (a) Continuing support for Basic Services
- (b) Lowering Standards
- (c) Strengthening the Management of the Sector
- (d) Interest Rate Subsidies
- (e) Targeting Resources to the Target Group

The Mission stressed that the outcome of a policy review would set the stage for a well coordinated international donor's assistance program for the urban sector. In a follow up briefing paper prepared for President Belaunde and related to the Director of the International Development and Cooperation Agency visit to Peru, USAID/Peru reiterated the importance of Peru undertaking an in-depth review of its shelter and urban development policies.

By mid August, the Mission had negotiated a limited scope agreement with the MOHC and the National Planning Institute that will provide planning staff support to a multisectorial commission that has been created to upgrade, in an integrated fashion, the pueblos jovenes of Lima. It is anticipated that this planning exercise will help articulate a series of policy issues that will have to be addressed by the new government and which will feed into the proposed policy review exercise requested by AID.

In recent conversations with the BVP related to the conditions on this loan, the President expressed his firm belief that the GOP would be, in the next six to eight months, involved in an in-depth review of the policies of the sector and that BVP would be involved in that review process. For the moment, he mentioned, the leaders of the sector were still in the process of recruiting their staffs and familiarizing themselves with the myriad of new institutions that have been created since their ouster in 1968.

Finally, the Mission has been involved in a variety of meetings with the World Bank Representative and his urban missions to Peru. Although the Bank has not as yet articulated its urban strategy, it has indicated that it will want to support programs similar to those being undertaken by USAID/Peru. To avoid duplication of effort or cross purposes in policy guidance provided to the urban sector, USAID/Peru and IBRD have agreed to work closely together in encouraging the GOP to develop a more comprehensive urban development policy.

The Mission will be working on a complementary list of issues to be discussed with the new government once the IBRD has completed its next round of visits to Peru in early September, 1980.

The above touches on the Mission's efforts to apprise the leadership of the sector of our interest in seeing Peru take a hard look at policy issues. The Mission also has attempted to identify some of the issues that should be considered; has indicated its interest in providing technical assistance in the policy review exercise; and has provided some limited support to date for reviewing the need to reduce standards and to start an integrated planning and development effort in pueblos jovenes. The results of a recent DS/UD construction study and a related employment-generation study also will be helpful in developing the policy review.

The "Consejo Nacional de Vivienda y Construcción" (National Housing and Construction Council) is an advisory group for the Ministry of Housing which will be in charge of preparing the "National Shelter Sector Policy".

Up to now several committees have been formed to study specific shelter sector areas e.g., Shelter Urban Development, Public Services (Electricity, Water and Sewer), Construction, Legal Dispositions, Administration. They are presently analyzing the situation and formulating recommendations. The initial work of these committees should be ready in approximately 90 days.

To kick off the policy review exercise, USAID and the GOP have agreed on the desirability of utilizing HG loan resources to undertake the standards study referred to above. The Mission also has agreed on the importance of Peru developing an integrated planning approach for its pueblos jovenes and both have set aside resources to undertake the required study. The Mission feels that other issues signalled to the GOP by the Mission will be reviewed by the new managers of the sector, particularly after the re-staffing of the sector has been completed.

There is also the World Bank urban strategy review and articulation of issues that hopefully will begin to establish IBRD interest in the sector. It will also have to identify the kinds of TA which it will be willing to provide the GOP in the policy review.

Given AID's desire to support the policy development exercise, but recognizing the need for the GOP and IBRD to have more time to develop their preliminary policy review strategies, the Mission proposes to set aside up to 1% of the HG loan (\$200,000) funds to finance (both US and Peruvian) costs related to the policy review study. The specific cost components of this support would accompany BVP's proposed involvement in the GOP's policy review exercise and would be submitted within six months after the signing of the loan agreement (see Conditions Precedent, p.42).

While seeking ways to support GOP initiatives that increase the number of persons who have access to basic services, the Mission also will be encouraging the GOP to consider several related long-term policy issues:

a. Reducing Standards. As a condition precedent to this loan, the Mission will request that the BVP, with appropriate GOP entities, conduct a study and make recommendations on construction standards and costs to ensure that the lowest cost appropriate technology is being employed in GOP-supported shelter programs. The intent of a redefinition of standards is to permit a greater participation of lower income people in the GOP's shelter related programs.

b. Solving the Deficit. Despite the budget austerity program of the Central Government, Peru's contribution beyond subsidies to the shelter sector has been on the rise. The Central Government allocated \$49.8 million in CY-79 and \$142.5 million in CY-80 for shelter-related services. The Mission will work with the GOP to determine the extent to which this support can be utilized to meet present and projected shelter-related deficits. Beyond budget allocation to the sector, what can the GOP do to resolve the existing and projected deficits?

c. Exchange Rate Costs. The Mission will consult with the BVP to determine the projected level of GOP budget support required to service exchange rate losses associated with external loans to the shelter sector. Given the existing and proposed level of HG inputs over the planning period as well as the proposed level of IBRD urban loans, will the GOP be willing and able to continue to cover exchange rate losses?

2. Absorptive Capacity. The DAEC queried whether the BVP, and especially the utility companies, have the managerial and administrative capacity to use efficiently the contemplated increased volume of HG resources. The BVP can accommodate a greatly increased financial volume with present staff; and the expected volume of basic infrastructure services, including the proposed HG financing, is well below the past peak volume of operations by the utility companies and by the construction industry. (See Section III-C, "Administrative Feasibility".) Recent evaluations of the Bank's perfor-

mance in implementing HG projects have identified a series of problems that need to be addressed by the Bank. These include: the need to develop an outreach capability to deal directly with the specific needs of the target group (see Conditions Precedent 2 a); the need to improve coordination among project implementers (see Conditions Precedent 2-b); and the need to strengthen the cost recovery procedures of the Bank (see Mission Implementation Letters on prior HGs). The Bank has acknowledged these problems and presently is implementing organizational operational changes to deal with these problems.

3. Sub-project Components. The DAEC asked for a justification for including community social infrastructure and home improvement loans in the project. The shortage of community facilities can be traced to the inability thus far of the GOP to respond to the need on equity grounds to provide them. In the present circumstances--a lack of both policy and funds--the GOP does not provide community facilities in sufficient measure. The communities must finance the capital costs or continue to do without the facilities.<sup>1/</sup>

The HG can finance community facilities and for the first time this HG loan to Peru has \$750,000 earmarked for such financing. The rationale behind the earmarking is the desire to mount a pilot effort through the BVP and to be responsive to the needs expressed by community groups.

The \$750,000 figure would provide facilities to approximately 40 communities, with each facility costing approximately \$18,000. The \$20 million HG will mean the mounting of some 40 projects. Based upon current construction costs, the average cost for a community center health post, day-care center, etc. is \$18,000, taking into account the special features needed depending upon the type of facility contemplated.

Communities that had developed projects with SINAMOS often had community facilities planned for which they could not obtain financing. The community groups began to develop their own plans for facilities since it became apparent that their projects were not getting priority at the Ministries. The Ministries might have wanted to construct such facilities but their budgets did not permit these projects to go forward.

There is a tradition in Peru of private sector involvement in the provision of community facilities. Fe y Alegria, for example, a church-sponsored program, assists the pueblos juvenes in constructing vocational schools. These are subsequently staffed by Ministry of Education paid personnel.

It is anticipated that the arrangements for each facility will vary depending upon community and government resources, availability of trained personnel, and supplies. This will enable substantial experimentation within the parameters of the pilot effort.

<sup>1/</sup> Within the low-income communities, the ability of each individual household to finance its portion of the community services varies from 0-100%. For the very poorest households, AID has a food-for-work program (administered by CARE) which will provide some facilities. A \$973,000 OPG will enable CARE to increase its administrative capacity and to supervise the distribution of about \$10 million of PL460 Title II commodities to workers. The proposed \$750,000 is an additional pilot approach.

a. For social infrastructure, a condition precedent for any sub-project will be that a statement in writing be obtained from the appropriate Ministry that the Ministry will staff and maintain the facility if the social infrastructure is not a self-financing operation. The investment costs will be prorated among the beneficiaries in the community and the BVP will retain the flexibility to schedule repayments to the ability to pay of individual households. This sort of arrangement would be applicable, for example, for schools and health clinics.

Some facilities, such as recreation facilities (soccer fields, recreation halls), will be maintained by the community.

The financing for the operation and maintenance of commercial facilities (bus depots, public markets) will be agreed to on a case-by-case basis. The bus company would normally be expected to maintain depots. For public markets, the licensing/supervisory agency in each municipality would be expected to devise charges for the use of the markets which would cover maintenance. If the market is for a cooperative group, the cooperative would be responsible for maintenance.

Coordination in each case will be the responsibility of the BVP as borrower; and arrangements will be subject to AID approval on a case-by-case basis.

In the few cases in which the BVP has lent for community facilities until now, the BVP has charged a higher interest rate than for loans for basic infrastructure services. The BVP says that its intention under the loan is to use the same line of credit (and interest rate) for both infrastructure and for community facilities. How much can be budgeted for community services within any given sub-project will depend on the size of the project to which the cost of the community facilities will be added. In each case, the joint unit cost per beneficiary must be affordable by the beneficiary group.

b. Home improvement loans under the 009 pilot project have only recently been made by S&L associations outside of Lima and money should begin shortly to move in the Lima Metropolitan Area as well. The first HG to include a home improvement loan component was 527-HG-009. In the past the BVP had showed an interest in such a program but had been unable to develop adequate procedures to on-lend the funds. Funds were always reprogrammed to other activities.

Under the first tranche of 527-HG-009, \$750,000 was earmarked for home improvement lending, utilizing the savings and loan system. The Foundation for Cooperative Housing, utilizing an Operational Program Grant (OPG), fielded a resident technician to work on the home improvement loan program with the BVP and the savings and loan system.

An evaluation of 527-HG-009 (I) shows that as of April 30, 1980, only 53 loans had been made to program beneficiaries. This showing did not meet the expectations of the project planners, who had expected that funds would be disbursed more quickly. The lack of initial success can be attributed to the following factors:

- . The small amount of resources allocated to the program.
- . The degree of effort required to do the necessary feasibility studies and to produce program guidelines.
- . The fact that the program's acceptance was uncertain and its potential unforeseen.

Corrective measures have been taken to ensure the adequate functioning of the home improvement program. The OPG has been extended for a total of 36 months. The BVP has appointed a full-time, experienced employee to work with the program. A series of complex guidelines adopted in November, 1978, was simplified and reissued in June, 1979. As of June 1980, seven of Peru's seventeen savings and loan associations are participating in the program and all of the funds from the first and second tranches of this HG are committed. The demand for funds by the savings and loan associations exceeds the funds destined for the program and additional monies are being programmed for home improvement loans in future HGs.

Since the evaluation was completed in April 1980, an additional 35 loans have been made to project beneficiaries. On June 25, 1980, the BVP announced the commitment of one billion soles (approximately \$3.3 million) to the home improvement loan program.

While project experience to date does not provide extensive experience with a home improvement lending operation, the early results are quite promising. It is anticipated that fuller experience will continue to be favorable and will support the recommendation that \$2.5 million of total project funds be made available for home improvement loans employing the same BVP-S&L mechanism. If, contrary to expectations, the demand for home improvements loans should prove to be inadequate, the funds allocated for home improvements will be used pro rata for other project activities.

4. Effective Demand. Section III-B ("Financial Analysis") examines the demand for basic infrastructure services among the target group in Lima and in other cities. It demonstrates that the effective demand for the project services will far exceed project resources. The project would provide infrastructure services to some 31,500 households in pueblos jovenes and similar communities.

5. GOP Financial Commitment. The Implementation Agreement for the proposed loan will stipulate that the GOP will reimburse the BVP for any foreign exchange loss incurred in servicing the loan. It is estimated that the GOP presently is providing an annual subsidy of \$2.5 million to cover exchange rate losses on the HG program. The GOP has compensated the BVP for foreign exchange losses in the past and will agree to do so for the present loan.<sup>1/</sup> The BVP, for its part, will use its own resources to finance 10% of the loan amounts. This will provide \$2.2 million of the \$23.4 million program.

<sup>1/</sup> The rationale for this is that the GOP, not the BVP, uses the foreign exchange received from the HG loan; and any foreign exchange losses are due to GOP general economic and exchange rate policy, not to BVP shelter sector activities.

## II. PROJECT DESCRIPTION

### A. Background

1. Overview. Starting in the 1950's, the population from Peru's rural areas and small towns started to move into economically active urban centers. Lima and the coastal cities received the brunt of these population flows. The physical and social service infrastructure of these cities was seriously overextended by the transplanted rural poor.

During the 1961-1972 intercensal period, Peru's total population grew at a rate of 2.9% per annum, rural population at 0.7% p.a., and urban population at 5.6% p.a. The official GOP hypothesis regarding future population growth projects total and urban population as follows: for 1980, 17.8 million (12.0 million urban); for 1990, 23.3 million (17.2 million urban); for 2000, 29.8 million (23.4 million urban). Thus, population in urban areas (over 2,000 people) will nearly double in the next two decades and will approximate 78.5% of total population as compared with 26.9% in 1940; 40.1% in 1961; 53.0% in 1972, and an estimated 67.4% in 1980.

The past pattern of urbanization is changing. In the 1940-1964 period the growth rate of Lima was 20% higher than that of total urban population and higher than that of most other medium-sized cities. Although Lima is still the primate city of Peru, medium-size cities are now growing at a faster rate than Lima.

Shelter and related service deficits have built up rapidly. Despite certain improvements in the public and private shelter delivery system in both quality and quantity, it is still being overwhelmed by the absolute numbers. 1977 housing deficit studies estimated that 72% of all housing units lacked piped water, 78% were without sewerage infrastructure, and 65% did not have electricity. In Lima, 75% of the population lives in pueblos jóvenes and inner city slums.

While not facing the sheer numbers impacting on Lima, a recent study by Compania Peruana de Investigacion de Mercado, S.A. (CPIM) shows that the same phenomenon is being repeated in all of the major cities of Peru. The percentage of city population living in pueblos jóvenes was found to be: Arequipa, 39%; Chiclayo, 44.8%; Chimbote, 65.8%; Iquitos, 55.9%; Piura, 51%; Tacna, 45.7%; and Trujillo, 52.9%.

2. Shelter Constraints. The major constraints to providing minimum shelter and related infrastructure to the growing urban lower-income segments of Peru are:

a. Effective housing demand has been drastically reduced by high interest rates, inflated construction costs, and falling real income. As a result, shelter and related service deficits are huge and are increasing.

b. The housing finance institutions are being decapitalized by high inflation rates. In the absence of a maintenance-of-value system, housing portfolios collect payments on past loans which are inadequate to finance equivalent replacement shelter. The government currently is supporting the S&Ls with approximately \$4.2 million annually in subsidies to compensate in part for this impact. It also is providing \$3.8 million annually to the BVP to deal with this problem.

- c. Rent controls undermine the will to increase and maintain the stock of rental housing.
- d. The GOP has yet to develop a meaningful strategy for its inner city slums (in contrast to pueblos jovenes).

3. Mission Strategy. The overall goal of AID's Urban Strategy in Peru is to improve the quality of life for the target group through programs that improve the delivery of shelter related services in the broadest sense. (Annex O is an undated urban strategy for USAID/Peru.) The Mission does not anticipate new urban initiatives until the newly elected GOP has had some time to examine its options. When the new government determines its shelter sector policy and the financial situation of the government has improved, the HG infrastructure projects can be adopted as models that can be replicated by both the public and private urban finance institutions.

Through its Integrated Regiona' Development project, the Mission will encourage the GOP to continue the trend toward decentralized planning and improved project preparation capability of regional planning institutions; establish a mechanism for financing productive market town and rural infrastructure in the sierra and high jungle; and serve as a pilot effort for eventual replication through regional efforts in other areas of Peru.

In FY80 the Mission will continue to work with the BVP because of its thorough familiarity with the HG Program, its extensive ongoing basic services program in pueblos jovenes, and the likelihood that housing programs and institutions will be less vulnerable to drastic changes by the GOP than in other sectors. The present project will permit the BVP to continue to provide financial assistance to low-income people for water, sewerage, and electricity services; make available the possibility of financing related community facilities such as schools, health posts, and markets in pueblos jovenes and similar communities; and, with money on-lent by the BVP, permit the S&Ls to expand their home improvement lending. The BVP would also be permitted to lend for home improvement loans in low-income settlements.

4. Target Group. The target group for this project is the residents of pueblos jovenes and similar communities in Lima and other cities. They are in the bottom half of the income distribution.

5. Relation of project to GOP shelter priorities. The proposed project is consistent with the GOP's National Development Plan. It addresses the shelter service problems of the urban poor and thereby furthers the Plan's equity objectives as set forth in the chapter on "Operational Plan for the Housing and Construction Sector."

6. History of proposed project. Field work on the Shelter Sector Assessment in early 1979 pinpointed some of the difficulties of dealing with the shelter needs of the urban poor, difficulties which are severely exacerbated during the current transitional economic austerity program. The findings are reflected in the Mission's Urban Strategy for Peru and specifically in the present project. The project is anticipated in the FY1981 CDSS (pp.48-49).

## B. Detailed Project Description

1. The Project. The Mission proposes that a \$20 million Housing Guaranty Program be authorized in FY 80. Half of the resources would be used in Metropolitan Lima; the other half would be used in secondary and tertiary urban centers outside Lima. The HG loan would permit the BVP to continue to finance (a) primarily water, sewerage, and electricity services; (b) related community facilities such as schools, health posts, markets, etc.; and (c) home improvements in pueblos jóvenes and similar communities. Home improvements would be on-lent by the S&L's from \$2,137,000 of HG funds made available by the BVP. This project follows on several earlier HG's which have been designed to assist the BVP in doing what the Mission feels the BVP does well: financing the upgrading of low-income settlements. In addition, the project proposes to introduce a number of technical innovations that will help the BVP and the MOHC to improve their programs for low-income people.

2. Project Objectives. The basic objectives of the project are to address the major deficit of basic services and community facilities of low-income urban families living in pueblos jóvenes and similar settlements and to enable the target group to upgrade its shelter through home improvement loans.

### 3. Participating Institutions.

BVP. The BVP will be the Borrower for the project and relend to the target group. It has extensive experience with AID-financed shelter programs. As the premier institution of the Peruvian shelter sector, it has been the Borrower on \$82 million of HG financing. The institution is mid-stream in implementing a low-cost shelter program, a major component of which is basic infrastructure services in pueblos jóvenes. It also is managing a similar HG loan for the S&L system.

Utility Concessionaires. ESAL, ESAR, Electro-Lima, Electro-Peru, or in their absence, the DGOS will work with the BVP, the communities, and with private contractors. The utility concessionaires are experienced in this type of project. Their technical capability and their outreach capacity are good. The current HG-financed projects are enhancing their ability to work with the target group within an administrative setting closely akin to the one for this project.

Builders. The builders will be private firms responsible for the brick and mortar aspects of services projects. Contracts will be awarded according to standard procedures established by the BVP and currently in use.

Community Organizations. The neighborhood councils will have an essential role in project development. The community should discuss and reach consensus on priorities for basic services and facilities, participate in the project design, discuss costs, come to grips with the impact of inflation, save for down payments, and contribute labor in an effort to avoid monetizing some construction costs. In some instances the neighborhood council will sign the construction contract directly with the private contractor. In these cases the community will have greater control over project development and possibly be able further to reduce costs.

Upon completion of a sub-project, each beneficiary will remain with a debt corresponding to his proportionate and individual share of the cost of

installing the given service or combination of services. The BVP will contract with the utility company (or with the DGOS performing in the absence of a public utility enterprise) to have the monthly quotas corresponding to amortization and interest on the loan included separately on a single billing for monthly consumption for each household.

4. Project Outputs. Half of the project funds will be used in Lima, half in other cities. The outputs will be infrastructure services (water, sewerage, electricity), community facilities, and home improvements. The expected allocation of funds between outputs can be summarized as follows (see Section III-B, "Summary Financial Plan"):

<u>Sub-programs</u>	<u>Investments</u>	<u>Percentage</u>	<u>Solutions</u>
Home improvements	\$ 2,500,000	11.00	4,200
Community facilities	750,000	3.00	n.a.
Water	8,561,000	36.00	11,000
Sewerage	6,546,000	28.00	7,600
Electricity	5,036,000	22.00	8,700
Total	<u>23,393,000</u>	<u>100.00</u>	<u>31,500</u>

The percentages for infrastructure services are the sum of quite different assumed distributions of demand between Lima and the provincial cities. For Lima, the projected demand for water, sewerage, and electricity is in the proportion of 40:20:40 respectively; for provincial cities, 45:45:10.

The project can assist about 31,500 households, about 28% of the expected increase in the number of households in pueblos jovenes during the 2-year project commitment period.

5. Project Inputs.

a. Financial. Total project funding will be:

\$20,000,000	HG
2,223,000	BVP
1,171,000	Beneficiaries
<u>23,394,000</u>	Total

\$2.5 million of the total will be allocated for home improvement loans and \$750,000 will be available for experimental projects to provide community facilities.<sup>1/</sup>

b. Technical assistance. The HG loan will finance

- \$24,000 for 2 person-months of short-term consulting with the BVP to assist them in their examination of present building and infrastructure standards and specifications. The aim of the BVP effort is to recommend to the Ministries which control building codes changes in the codes which are more appropriate for attending the needs of the target group.

- In addition, Technical Assistance will be provided from other AID sources estimated to cost \$14,000 consisting of 4 person-weeks of short-term consulting with the BVP in their effort to incorporate the recently developed environmental checklist in project and site selection criteria.

<sup>1/</sup> If, contrary to expectations, the demand for home improvement loans should inadequate, the funds will be allocated pro rata to other project activities.

In addition to the T.A. specially for this project, a \$100,000 IIPUP already authorized will finance T.A. to assist the work of a recently established multisectoral commission under the chairmanship of the MOHC which is to coordinate assistance to the pueblos jovenes. An initial study has been financed with the IIPUP funds to recommend ways in which the funds can be used to improve the quality of life of the urban poor. Remaining funds can contribute to the basic policy studies recommended in formulating GOP shelter policy.

### III. PROJECT ANALYSIS

#### A. Economic Analysis<sup>1/</sup>

1. The Current Economic Situation. During the past 3 years, 1977-79, the Peruvian economy has experienced its most severe recession since World War II. Per annum GDP growth has stagnated since 1977. Inflation accelerated from an annual pace of less than 10% in the early 1970s to 56% in 1978 and 68% in 1979 (on an annual average basis) due to monetized fiscal (and public sector) deficits and corrective devaluations. Simultaneously, decreased real credit to the private sector has reduced real demand, thereby eroding employment opportunities and real incomes in the urban sector. Since 1976, urban real wages and incomes have declined by about 30% for lower income households (and by even larger percentages for middle and upper income households), and unemployment and underemployment in the Lima metropolitan area have increased from a level of 26% in 1975 (April-May) to 47% in 1978 (July-August).

The Phase I military government which came to power in 1968 undertook structural reforms aimed at the creation of a more equitable distribution of income and wealth. A sweeping land reform redistributed 45% of Peru's best farmlands to workers' cooperatives. Through nationalization and the creation of new enterprises, the State took over direct control of 150 enterprises in key economic sectors. By 1973 the State had assumed the role previously held by foreign capital in electricity, telephones, and railways, and had taken over much of the mining sector and the banking system, virtually all export marketing, and the fishing sector. The State's role in capital formation also rose (from less than one-fourth of total investment in 1968-70 to about one-half in 1974-78). The role previously played by foreign direct investment was replaced by sharply increased utilization of external credits from foreign commercial banks.

By 1976 the Peruvian economic normalcy was threatened by the exhaustion of foreign exchange reserves and accelerating monetary expansion. The Phase II military government initiated a stabilization program in mid-1976 to arrest the growing balance of payments and fiscal disequilibria. It achieved initial success in terms of domestic policy implementation and of completion of a stabilization transaction, i.e. the external credits needed to close the balance-of-payments gap. This transaction broke down in mid-1977 due to the unwillingness of the government to maintain fiscal discipline, to abortive negotiations with the IMF, and to erosion of the confidence of external creditors. By the second quarter of 1978, Peru was no longer able to service short-term commercial credits on a timely basis and also was unable to comply with the terms of an IMF standby agreement signed in November 1977. From mid-1978, the GOP sharply devalued the currency, maintained a fiscal deficit of substantial magnitude, expanded banking system credit to the public sector and reduced real banking system credit to the private sector. These policies worsened recession and increased inflation.

<sup>1/</sup> Annex H presents a complete Mission analysis of the current economic situation

In the second half of 1978, a new economic team implemented a stabilization transaction composed of traditional elements (substantial external financing and fiscal austerity). An IMF standby agreement was obtained in September 1978 (which runs through 1980) and a rescheduling (of 90%) of the public sector debt due in 1979 and 1980 was negotiated with major creditor governments and foreign commercial banks in late 1978. The new economic team also complied rigorously with the fiscally-austere quarterly targets established in the IMF standby. Due to increased foreign exchange availability, the GOP decided in late 1979 to forego a portion of the debt relief.

Even though some aspects of Peru's recent severe recession can be linked to revolutionary experiments to achieve greater equity, from 1973 to 1976 government policymakers delayed undertaking policies to reduce real demand, and in 1977 they lacked the steadfastness necessary to maintain a stabilization transaction. Recession was thereby prolonged and made deeper than necessary. Exogeneous forces, such as the deterioration in external market conditions for Peru's exports after 1974, the increase in petroleum prices in 1974-77 (when imports were still necessary), and the anchovy decline (1973 and after) were also unfavorable.

Set against present conditions, the medium term outlook is for moderate improvement of the economic welfare of most urban Peruvians. Real urban incomes should increase 4-7% in 1980 and still more in 1981. This expectation is based on the very good performance of Peru's external sector in 1979, which increased foreign exchange availability sufficiently to permit the resumption of normal service of Peru's large external debt (\$9.3 billion at year-end 1979) and to pay for an increased volume of imports. Export earnings in 1979 increased 79% over the 1978 level. The increase in earnings derives from substantially higher export prices for petroleum, silver, and copper; generally buoyant market conditions for other traditional mineral and agricultural exports; and a \$342 million increase in non-traditional (generally industrial sector) exports. The brisk recovery of external account solvency fulfills the indispensable condition of allowing near-term growth of imports. A sustained increase in urban real incomes also depends on successive reductions in the rate of inflation (to increase real wages rapidly) and a revival of domestic investment activity (to increase employment opportunities). Due to normal lags in economic processes, however, urban income will not recover its pre-recession level until 1983-84.

The newly elected civilian government, which is to be installed in July, will have to focus initially upon economic policies promoting recovery. Barring a very adverse movement in the terms of trade, GDP growth on the order of 6.5% per annum is possible through 1985. Even though near-term inflationary pressures impose significant problems for policymakers, the pace of inflation should decline (but the official projection of 40% for 1980 may prove to be too low).<sup>1/</sup> Several medium-term policy areas demand attention: energy, external debt management, employment generation, and the allocation of public expenditures; but the overall prognosis is favorable.

---

<sup>1/</sup> The inflation rates of up to 80% p.a. in the past few years is an aberration in Peru's historical inflation experience. The CPI averaged a little less than 9.0% annually, 1966-1974.

2. GOP Capacity to Repay. The rescheduling of Peru's external debt in September 1978 reduced debt-service ratios to manageable levels. Nevertheless, the magnitude of the debt (nearly 80% of GDP), the relatively high debt-service ratio (estimated to be about 35% of export earnings in 1980), and the need to offset large public sector debt amortizations (about \$1.0 billion annually) suggest the need for careful debt management. Continued cooperation among the international financial institutions, major bilateral lenders, and the GOP will be essential to the success of efforts to improve the debt structure. The proposed loan assists that effort by providing long-term funds; and since the loan amounts to less than 0.3% of the outstanding external debt (9.3 billion at the end of 1979), it will not be a heavy additional burden for Peru.

3. Economic Benefits. It is not very informative to quantify the internal rates of return on a project of this type.

a. The market value of benefits can be quantified by comparing land values with and without the project, imputing the difference in value to the project. The exercise often produces internal financial rates of return on the order of 50-120% in projects of this type.

b. The economic (social) rate of return predictably is still higher. The labor component of economic project costs in Peru will be lower than market costs because there is considerable underemployment and unemployment. Construction industry capacity also is greatly underutilized during the current economic crisis; consequently, technical, managerial, and equipment economic costs are less than market costs. Materials are almost entirely produced locally. It is estimated that 1% of construction costs are direct foreign exchange costs. Although indirect foreign costs would add something to the 1%, the economic costs would be raised very little since Peru now maintains a relatively flexible exchange rate policy. In sum, economic costs will be less than market costs.

Social benefits, on the other hand, are higher than market-priced benefits. Society will benefit by more than the amount reflected in benefits which are paid for. For example, the project will be able to make only a start toward meeting the demand for these infrastructure services. At best, the project can provide benefits to some 120,000 families (including 2 rollovers). This is less than the percentage of those without services who would be willing and able to pay for services on project terms. Indeed, it is slightly more than the number of new pueblos juvenes families which will be formed during the next 2 years. There will be a significant excess quantity of services demanded. The existence of unsatisfied effective demand means that the market is underpricing the services and that the social benefits correspondingly are greater than the private benefits.

In sum, there is a presumption that the internal financial rate of return is quite high and that the economic (social) rate of return is even higher. The effective demand for the project services is great. The project is consonant with the GOP and AID policy of improving the quality of life of the urban poor. Rather than calculating internal rates of return, it is more appropriate in this case to examine whether the project is cost effective.

The proposed project is appropriate to the present economic straits of the urban poor; it is economically and financially sound; and it is a cost-effective means of delivering minimal infrastructure services to the urban poor in Peru. The Shelter Sector Assessment (SSA) completed in February 1979 concluded that formal sector housing was beyond the means of those in the bottom half of the income distribution. The unfinished core houses that had been offered as a low-cost solution under 527-HG-009 were then beyond the means of the target population. Peruvians who could afford that unit, those with incomes in the top 3%, would not purchase an unfinished core house. All indications were that the only viable program under the crisis economic conditions would be one which would provide financing for water, sewer, and electric connections, and for home improvement loans. No individual beneficiary was expected to be able to amortize a loan of more than \$1,000 (in round numbers) and the costs of the infrastructure hook-ups were found to be considerably less than that.

The SSA found that lighting and cooking were fueled predominantly by candles, wood, and kerosene, all of which cost substantially more than electricity. Furthermore, electricity enables the beneficiary to mount small repair businesses, dress-making, and other home industries. The economic benefit has not been specifically measured but in the recent evaluation done on 527-HG-009 (I), 75% of the beneficiaries interviewed for the evaluation stated that they highly valued the services received and would recommend the program to others.

Turning to the difference in cost between piped water and water purchased from tank trucks, one discovers that very recent statistics show that one cubic meter of piped water costs 20 soles, whereas the same amount delivered by truck costs 260 soles. Non-economic benefits of having piped water such as time saving and cleanliness need also to be taken into account.

Throughout the countries in which the HG operates there has been a discussion of communal services, usually related to water and usually meaning community standpipes. There has been no experience to date of adequate cost recovery in areas where community standpipes have been installed. There is also no effective method to date for controlling waste of this resource.

This loan will finance a construction standards and norms study which will examine the payment capacity of the target group and the technological possibilities available. The aim is to show how the lowest-cost, appropriate technology can be used to provide infrastructure to low-income communities. Costs and benefits, while unavailable at the present time, should be weighed in the decision-making process for the adaptation of new standards. The study being financed under the HG will provide the data and analysis for these decisions.

## B. Financial Analysis

1. Effective demand for project items. Annex I lists the median monthly household income for Lima and 15 other potential project cities. Annex J distinguishes between the Metropolitan Lima area and the provincial cities as a group and calculates what percentage of the target group can afford the project infrastructure for water, sewerage, and electricity in the pueblos jóvenes. It projects, for example, that 91% of the target group in Lima could afford electricity; 65% of the target group in other urban centers. (Annex M breaks down the component costs of infrastructure services.)

Residents of the informal settlement, currently pay more for substitutes than they would pay for the services to be provided by this project. ESAL assumes a minimum monthly consumption of piped water to be 45m3 in Lima. For this, their charge is \$3.54. The equivalent amount of water purchased from delivery trucks in the pueblos jovenes would cost from \$7.00 to \$30.00 at going rates, depending on the specific location. The minimum monthly consumption of electricity in Lima is estimated to be 30 KWH/month, for which ElectroLima charges \$0.35. The same number of hours of light provided by candles costs approximately \$2.80, by kerosene lamp \$0.70, by Coleman-type lamp \$1.00. There are no separate user charges for sewerage systems.

The following table compares the monthly dollar cost of the project services with the estimated current expenditures for lower quality substitutes. It is worth noting that in the instance of potable water service, piped to the house, many families will actually experience a diminution of total monthly costs by participating in the program.

Monthly Cost of Project Services and Alternatives(\$)<sup>a/</sup>

	<u>Unit Cost</u>	<u>Loan Amt.</u>	<u>Monthly Payment 10 yr.</u>	<u>Monthly Payment 15 yr.</u>	<u>Minimum Monthly Consumption Charge</u>	<u>Estimated Current Expenditures for Substitute Service</u>
WATER	776	737	14.99	13.77	3.54	18.50
SEWERAGE	858	815	16.57	15.22	b/	0
ELECTRICITY	576	547	11.12	10.22	.35	1.60

a/ Assumes 5% down payment, 10 and 15-year term, and 21.5% annual interest.

b/ Sewer charges are combined in the water bill; there is no separate user fee.

In order to bring basic infrastructure services to all of the target group by the year 2000--eliminating the existing "deficit"and accomodating all new target group households--would require an investment of some \$756 million at current costs. The target population itself could afford to pay for about \$559 million of this; the balance consists of "welfare cases" who could not now pay for the services.

The approximately 600,000 households now in the pueblos jovenes will increase by about 111,500 during the next 2 years (an annual compound increase of 8.9%). 91% of those in Lima, 65% outside Lima, could afford electricity (or some other combination of infrastructure services). This represents a potential effective demand of an additional \$38 million for project services. A \$20.0 million HG plus \$2.2 million of BVP resources could finance about 61% of the potential increase in effective demand. In short, the HG Loan will not suffer from a lack of demand. It is expected that the entire loan will be committed within 2 years.

2. Cost recovery. There are two possible subsidy elements inherent in the interest rate and the exchange rate. The interest rate initially will be negative in real terms--lower than the rate of inflation. The inflation rate of the past few years, however, is unrepresentative of Peru's historical experience. Peru has not been a high-inflation country until recently. The CPI averaged a 9.0% annual increase, 1966-1973. Inflation has been reduced in 1979, although not as rapidly as planned; and there is every expectation that inflation will continue to fall back toward historical norms. In that case, the lending rate to beneficiaries would become strongly positive in real terms (as high as 10% in real terms). Sub-project interest rates should average a positive real rate over the life of the sub-loans as well as over the life of the HG loan. During the first year or so, however, the probable lending rate (perhaps 21.5%) will constitute a subsidy to beneficiaries.<sup>1/</sup>

For each of its infrastructure projects the BVP routinely calculates costs to individual beneficiaries based upon the participation of 80% of the community in the project. That is to say, 100% of the costs are borne by 80% of the beneficiaries until such time as the entire community has been connected to the service. In addition, each project has a reserve fund to allow for contingencies and defaults.

The 527-HG-009 (I) Project Paper assumed a 7% default rate. It was not possible at the time of the evaluation done in June, 1980, to ascertain what the actual default rate is, if in fact there is any default.

One of the problems discussed in the evaluation report on 527-HG-009 (I) is that of cost recuperation. The BVP has been put on notice that the costs of the project must be recuperated in a timely fashion so as to terminate associated interest and commission charges. The Implementation Agreement for 527-HG-010 (as well as that for this project) requires that projects enter the recuperation phase much more rapidly.

The BVP's ability to bill has been improved by computerization of the entire process. Now information is consolidated at one location rather than relying upon BVP's central office relaying messages to branch offices and these in turn notifying beneficiaries. None of the projects are in sufficiently advanced billing stage to determine delinquency rates. There have been no discontinuances of service based upon non-payment of bills by beneficiaries.

The BVP's financial situation has been reviewed on several occasions by an expert from AID/Washington's FM/LD. This expert has found that, while the BVP at the present time is on a sound financial basis, it is not making a reasonable return on its funds. The BVP is aware of this as a problem which must be resolved in the context of financial and monetary policy.

<sup>1/</sup> FONAVI implicit interest rates will constitute a much greater subsidy to higher-income households. (See Annex K.)

The GOP, rather than the beneficiary, assumes any foreign exchange losses. Insofar as devaluations do not keep pace with decreases in the foreign-exchange value of the Peruvian currency, the GOP will have to reimburse the BVP for a foreign exchange loss. Since the beneficiary uses domestic currency and the GOP benefits by using the foreign exchange for other general purposes and since devaluation and inflation are the results of GOP economic policy decisions, it seems equitable that the GOP pay for any foreign exchange losses as it has done until now.

The Mission will require, as a condition to disbursement, that the BVP will obtain Ministry of Economy and Finance assurance that it will reimburse BVP in a timely fashion for exchange rate risk losses temporarily covered by the Bank. This provision has been included in the Implementation Agreement (527-HG-010) recently negotiated with the BVP.

### 3. Summary Financial Plan (thousand of dollars)

<u>Sub-Program</u>	<u>Number of Solutions a/</u>	<u>HG</u>	<u>BVP</u>	<u>Beneficiaries</u>	<u>Total Investments</u>
Home Improvement <sup>b/</sup> Community Programs <sup>c/</sup> Infrastructure	4,200 n.a.	2,137 641	238 71	125 38	2,500 750
<u>Lima (sub-total)</u>	<u>(14,500)</u>	<u>(8,611)</u>	<u>(957)</u>	<u>(504)</u>	<u>(10,072)</u>
Water	5,200	3,444	383	202	4,029
Sewerage	2,300	1,722	191	101	2,014
Electricity	7,000	3,444	383	202	4,029
<u>Provinces (sub-total)</u>	<u>(12,800)</u>	<u>(8,611)</u>	<u>(957)</u>	<u>(504)</u>	<u>(10,072)</u>
Water	5,800	3,875	430	227	4,532
Sewerage	5,300	3,875	430	227	4,532
Electricity	<u>1,700</u>	<u>861</u>	<u>96</u>	<u>50</u>	<u>1,007</u>
TOTALS	31,500	20,000	2,223	1,171	23,394

a/ First round. Rollovers will be used for the same kind of activities.

b/ Assumes an average home improvement investment of \$600.

c/ These will be designed into sub-projects and their \$750,000 total cost will be included in the costs of infrastructure.

### C. Administrative Feasibility

1. Summary Assessment. When examined from the point of view of the capability of each participating institution to execute the role assigned to it, the Mission concludes that the administrative structure is sound and offers every promise of effective project implementation. The participating institutions all have previous, ongoing experience working together on similar projects. Further, the BVP is modifying its organization to achieve more effective sub-project management and follow through. (The organizational and procedural changes should be operational by August 1980.) The adjustments planned by the BVP, based on program feedback, should strengthen overall control of sub-project implementation and effectively shorten the time required to run the total implementation cycle from promotion to completion of construction. A condition precedent will be that the reorganization plan has been implemented. (See Section IV-C, "Conditions, Covenants, and Negotiating Status.")

2. BVP. The BVP will be the borrower for the project. The BVP has extensive experience with AID-financed shelter programs. It has been the Borrower for \$82 million of HG loans. Annex L shows the sound financial position of the BVP and its financial evolution, 1970-1979. Lending for basic infrastructure has become increasingly important: 37.8% of lending for electricity in the 10 years 1968-1978 was in 1978; 33.1% of its lending for water and sewerage. During 1978, BVP's lines of credit amounted to \$7.9 million for electricity (28,652 connections) and \$14.9 million for water and sewerage (22,155 units). Its disbursement of HG funds has been growing at a compound rate of 25% annually since 1975. BVP disbursements in the past 3 years were millions of dollars:

<u>Source</u>	<u>1977</u>	<u>1978</u>	<u>1979</u>
BVP	64.3	39.4	31.5
GOP	0.8	2.0	8.1
External	8.1	7.8	26.0
Total	<u>73.2</u>	<u>49.2</u>	<u>65.7</u>

External capital amounted to 11%, 16% and 40% respectively of total disbursements during the 3 years.

As the total volume of lending grew appreciably and with it a changed weighting of the respective program lines offered, the management of BVP undertook an OD exercise to rationalize its administrative structure and to bring it more closely in line with actual operations.

In this regard, an analysis of BVP experience with AID and World Bank financed basic infrastructure projects showed that the technical procedures and staffing are effective but that there is a need to strengthen project management and inter-institutional coordination. Accordingly, the Technical Office of BVP will keep its present structure. It has the size and the professional experience and composition to effectively handle implementation of this project.

Administrative analysis of past implementation of the basic infrastructure services type of program contemplated here revealed no significant weakness in the technical capacity or ability of any of the individual participating institutions to execute assigned roles. What did surface was the need to significantly strengthen overall sub-project management, a role clearly falling to the BVP. The administrative changes planned and discussed above should, in the person of project managers assigned responsibility for shepherding through specific sub-projects, reduce the processing and approval time at the various institutions and permit efficient, effective implementation at the scale represented by this project. The Mission will continue to encourage the BVP to improve and speed up its program design, implementation, and cost recovery procedures.

Furthermore, to make inter-institutional communication and collaboration more efficient, a standing working group relationship at the middle management level will be inaugurated with this project. It will take the form of fixed, regular meetings between the appointed project chief at the BVP and a corresponding official of the respective participating concessionaires to surface problems and prevent sub-project submissions from "floating" between or in institutions, resulting in costly delays.

The attached chart (p. 24.a.) highlights BVP's actual and projected record to place USAID generated soles. What the Mission has been encouraging the Bank to consider are ways to speed up the design, implementation and recovery phases of program development to achieve a greater institutional impact with its resources. (see Conditions Precedent, p. 42).

3. Utility Concessionaires. ESAL, ESAR, Electro-Lima, Electro-Peru, or in their absence, the DGOS, have extensive experience working with the target group in extending basic services to the evolving settlements at the expanding fringes of Peru's cities. The utility concessionaires will be doing precisely what they do quite effectively despite increasingly severe budgetary constraints. The paralysis in the home building industry resulting from the drying up of effective demand for housing in the current economic situation in Peru has left the respective concessionaires currently operating at levels considerably below previous performance levels. Despite austerity-budget induced staff reductions, current demand for connections is still running far below respective staff capacities. For example, the Office for Pueblo Joven Coordination in Electro-Lima, charged with extending services to the pueblos jovenes and similar communities, has extended service to approximately 16,000 lots in the past 4 years. It is estimated that current staff capacity could support a volume of work producing 10,000-12,000 new connections annually. Their technical capability and their outreach capacity are good. Institutional deficiencies in planning and programming are largely attributable to uncertain budgeting aggravated by the loss of flexibility stemming from serious inflation. In terms of ability to execute, the utility concessionaires must be rated as seasoned, effective partners. Furthermore, the drying up of effective demand has so reduced the call for services derived from new construction that the addition represented by this program still implies working well below previous production highs and below staff capacity. In the case of Electro-Lima, for example, total domestic electrical connections in all of Lima fell from a 1971 annual high of 73,000 connections to the annual average of 28,000 for the last two years. The estimated annual increase for Lima attributable to this project is 4,500 new connections, well below current staff capacity.

ESAL connected 22,385 units to potable water in 1979 compared to a high of 58,492 units in 1978. During the period 1971-79, connections ranged from a low of 12,900 in 1975. As in the case of Electro-Lima, there is adequate capacity to increase its level of operations. (About 25% of the connections since 1971 have been in pueblos jovenes.)

The Mission does not believe that "revitalizing" the utility concessionaires is at issue. The institutions currently are underutilized because high finance and construction costs have restricted their output. The capacity is there; what is lacking is the long-term financing needed to permit using existing capacity to its full.

RECENT USAID LOAN HISTORY WITH BVP(\*)

(In US Dollars)

<u>FY</u>	<u>DL</u>	<u>HG</u>	<u>TOTAL</u>
1971	--	3,981,000	3,981,000
1972	--	--	--
1973	134,456	2,900,000	3,034,456
1974	--	2,000,000	2,000,000
1975	319,444	5,100,000	5,419,444
1976	4,224,702	3,600,000	7,824,702
I.Q.	1,197,058	1,800,000	2,997,058
1977	4,300,500	4,500,000	8,800,500
1978	2,773,430	8,500,000	11,273,430
1979	2,050,410	5,600,000	7,650,410
1980	--	10,200,000****	10,200,000
Anticipated '81	<u>5,000,000</u>	<u>12,000,000</u>	<u>17,000,000</u>
TOTAL	<u>20,000,000</u>	<u>58,181,000</u>	<u>78,181,000</u>

TOTAL AUTHORIZED:	23,000,000	68,281,000	91,281,000
AVAILABLE:	8,000,000**	22,100,000***	30,100,000

\* 055, 055/008, 009(I), 009 (II), 063, 010

\*\* IRD-063

\*\*\* 009 (I) 100,000  
 009 (II) 7,000,000  
 010 15,000,000  
22,100,000

\*\*\*\* Anticipate \$2 million closing for work in place.

UDD: 8/28/80

4. The Savings and Loan System. The Savings and Loan System consists of 17 separate associations, 10 of which are located outside of metropolitan Lima. Counting branch offices, there is a total network of 89 locations from which the S&Ls can mount programs. Represented are Piura, Arequipa, Trujillo, Chimbote, Tacna, Cuzco, Ica, Iquitos, Chiclayo, and Huanacayo, all cities impacted by rapid urbanization and all with significant numbers of Pueblos Jovenes.

Along with the geographical coverage represented by the system, it should be pointed out that there are 5.2 million Peruvians classified as economically active and one million individual savings accounts with the S&Ls.

The S&Ls represent a formidable, in-place capacity to lend funds for housing and housing related purposes. Given the incremental nature of the shelter process by which the majority of lower income families house themselves, financing home improvements was seen as a means of accelerating the process and improving the quality of life of the urban poor. The S&L network was viewed as an effective credit channel for speedy, widespread disbursement. To test this hypothesis, HG-009 provided for the financing of a \$750,000 pilot program of on-lending for home improvements by the BVP to a number of S&Ls. After initial drawing board delays, the project is now operational and quickly accelerating.

As of September 1979, the BVP had committed an additional \$750,000 from the second tranche, bringing the total available for the project to \$1.5 million. The BVP has contracted with seven separate S&L Associations for on-lending and program implementation, with the resulting distribution of funds falling approximately one-third Lima, two-thirds provincial cities.<sup>1/</sup>

Loans have been made and funds disbursed by S&Ls outside of Lima, and similar results are shortly expected for Lima as well. Initial market samplings and promotional efforts by the respective S&Ls have been most encouraging. The Mutual Tacna received the first 30% drawdown from the BVP and placed the entire amount within the first two weeks of the program offering. Within 30 days, an additional 337 loan applications were received from the intended beneficiaries. The experience of Mutual Arequipa has been similarly encouraging. Shortly after launching promotional efforts, 72 loans requests were received. In short, while the pilot program experience garnered under 009 has not produced data for an entire cycle, the preliminary response has been so strong as to support earmarking some of the HG funds (about \$2.1 million) to expand this home improvement program by the savings and loan system.

Administratively, the task of moving such an amount via a network of 89 Savings and Loan offices in place and operational is far less demanding than utilization of a single conduit. In absolute terms, the volume which any single association is being asked to place and service is actually modest compared to their existing volume of operations.

<sup>1/</sup> BVP loans to the S&Ls are at 17% annual interest plus a one-time 1% commission at drawdown. The S&L has up to 12 months to use the funds. The term is 12 years, from total disbursement or month 13, whichever is earlier. The S&Ls relend at terms of up to 25% annual interest for up to 12 years.

5. Neighborhood Councils. One of the most far reaching reforms enacted under the Revolutionary Government was the formal recognition of and assistance to the democratic, participatory community organizations of the urban poor. These neighborhood councils provide the target group with a forum for establishing consensus on local issues as well as group initiative to search for and secure the inputs needed for incremental development of their communities. In many cases these organizations are found to have out-distanced available financing. The project design team encountered evidence at the BVP that many communities already have determined their priorities regarding infrastructure services, have saved money and contracted for the private design of plans and specifications, and secured the necessary approvals but lack the financing to put a project into operation. Many of the neighborhood councils are well-organized, their participatory democracy is vigorous, and they are in the lead on the question of securing basic infrastructure and directly improving the quality of life of the target group.

#### Community Outreach

Some important changes have taken place within the Peruvian Government since the writing of the P.P. With the assumption of the Presidency by Belaunde, new policies are beginning to be articulated which will address the concern that the BVP needs to work in closer collaboration with community groups. Some historical perspective here is useful.

One of the BVP's first major experiences with the financing of water, sewer and electricity for the pueblos juvenes came under 527-HG-009, a \$25 million HG authorized in 1976. The first tranche of \$15 million is just being completed and the project liquidation is expected by December 1980. When the project paper for the 009 loan was developed, community organizations were formulated and assisted by the GOP's SINAMOS, the Sistema Nacional de Apoyo a la Mobilizacion Social. This group, created in 1968, was particularly active in the pueblos juvenes until it was abolished in 1978. At that time its functions were transferred to the MOHC. Since the MOHC lacked adequate resources to carry out these functions, they have fallen into abeyance.

SINAMOS served as an advocate for the communities in which it worked. It helped groups obtain technical assistance and participated in the development of infrastructure projects for the pueblos juvenes. The problem was to obtain financing for these projects once they were developed. The HG made financing available.

Whether in the form of SINAMOS or some other entity, it was indispensable that these functions - advocacy, community organization work, technical assistance - be continued. Community groups needed to know of the existence of the BVP financing and how to qualify for it. The BVP was not prepared to work directly with community groups in taking them through the process and no other organization was performing that function.

Both the BVP and AID were aware of the technical assistance gap at the community level. The BVP recognized that modifications in its method of doing business were necessary but the BVP did not think it appropriate for it to replicate what SINAMOS had done. Under the pre-Belaunde GOP, the BVP entertained the creation of a new Promotion and Development Department. This Department would have had the role of establishing closer collaboration with participating communities and would have implied an increase in the BVP's staffing and administrative costs.

The Mission has had the opportunity to discuss the \$20 million HG with the newly appointed BVP officials. When the P.P. was written a condition was included which would have required the BVP to create a new Promotion and Development Department prior to either the seeking of a U.S. investor or the first loan disbursement to the borrower. It now appears that the condition should be modified since the Belaunde Government expects to revive Cooperacion Popular, a community organization, advocacy, and technical assistance effort which existed during Belaunde's former presidency. The BVP would be prepared to work with community groups but would not be prepared to do grass roots organizational and technical assistance work. For example, the BVP would be able to conduct orientation and training sessions for Cooperacion Popular employees (most probably promotores) who could describe the BVP's programs and processes. These employees would get the information out to the communities interested in water, sewer, electricity, and community facilities. Thus, the BVP could continue its appropriate banking function and be more responsive to community needs without increasing its administrative costs (see Conditions Precedent, p.42).

In 1963, shortly after the Belaunde Government took office the Comité Interministerial de Cooperación Popular was created. In 1964 the name was changed to the Dirección General de Cooperación Popular and it was situated in the Ministerio de Fomento y Obras Publicas. This Ministerio was the precursor to the Ministry of Housing and Construction and the Ministry of Transport. Under this system the GOP made small amounts of money and technical assistance available to communities to finance small scale projects such as community roads, health centers, markets and irrigation projects. Peace Corps volunteers began to work with Cooperación Popular and AID financed a small rotating fund. The major activities financed in pueblos jóvenes at this time were classrooms. The current Belaunde Government's proposal is to create the Sistema Nacional de Cooperación Popular to be headed by a ministerial level appointee. This individual would participate at ministerial level meetings but would not vote at such meetings. This proposal must go before the Peruvian Congress for modification and/or approval.

In addition to the BVP/Cooperacion Popular outreach functions, the Peruvian Government has established a Multisectorial Commission on Pueblos Jovenes composed of the Ministries of Housing and Construction, Health, Education, and Agriculture, and the National Planning Institute. This Commission, with the MOHC in the lead, is charge with the task of establishing an integrated approach to the solution of the problems faced by pueblos jóvenes. In FY 1980, the Mission received \$100,000 in DS Bureau Central Grant IIPUP Funds. (IIPUP funds may be used for a broad range of shelter and community development projects. The acronym, IIPUP, means Integrated Improvement Program for the Urban Poor.) These funds will be used to provide technical assistance to the Multisectorial Commission at two major levels. The first involves the selection of those pueblos jóvenes which should receive integrated assistance. This would involve an urban planning exercise which would set criteria for community selection. The second part of the assistance would focus on the kinds of services actually to be provided at the community level. Close work with the community councils will be required. The first part of the IIPUP project is expected to be undertaken in September and October, 1980.

#### D. Social Analysis

Annex F presents the social soundness analysis of the proposed loan. It is based on an IIPUP study of the social needs and services in the pueblos jovenes of metropolitan Lima.<sup>1/</sup> The study confirmed that the residents of the pueblos jovenes are the poorest, least educated, and most vulnerable segment of the city.

The pueblos jovenes are organized into neighborhood councils, which in the past have been instrumental in helping the community to negotiate loans for basic services. The councils will have a key role in negotiating sub-projects under the new loan. Sub-projects will have a positive impact on the health and general quality of life of the participating communities.

1. The Social Landscape. The pueblos jovenes are one of the most pervasive features of urban Peru. They are among the first sights a visitor encounters when approaching Peruvian cities. Located on the urban fringes, the settlements are usually unordered groupings of reed-mat or mud-and-wattle huts put up on sandy lunar landscapes which lack basic infrastructure. As one moves closer to the urban center, these give way to more orderly but still rudimentary communities--mixtures of reed-mat or huts and more solid construction with one or more of the basic amenities. Some of the pueblos jovenes closest to the urban shell are almost indistinguishable from the neighboring communities within the formal city limits.

The squatter settlements are the result of more than 40 years of population growth and increasing rural to urban migration in Peru, the pattern flowing from rural communities to small urban centers to larger cities and finally to Lima. More than half of Peru's urban population lives in Lima, over 75% of that in the pueblos jovenes and inter city tugurios. The pattern and percentages are similar in other major urban areas. Demographic projections indicate that at current fertility rates, Peru's population will double by the end of the century. The population of Peru's urban squatter settlements will grow even faster.

Those who come to the cities from the rural areas begin at the bottom of the socio-economic scale, although their relative position may be an improvement over their former rural condition. The emigrants arrive with relatively poor education and have few marketable skills for a successful transition to the urban environment. Only 48% of the rural population is literate; 67% of rural women and 42% of rural men are illiterate.<sup>2/</sup> The quality of rural education is poor and rarely offers more than primary level schooling. The severe economic recession which has afflicted Peru since 1977 has sharply reduced employment opportunities in areas of work which might normally be job entry points for rural migrants to the cities. As a result, urban unemployment and underemployment are high, with particular impact on those with few skills or experience.

<sup>1/</sup> "Report on Peruvian Pueblos Jovenes Problems and Possibilities for USAID IIPUP Technical Assistance," Sivkin Associates, Work Order No. 7, November 1979.

<sup>2/</sup> AID:PERU, CDSS, FY1982, January 1980.

The employment opportunities open to job-seekers from the squatter settlements fall into low-paying, low-skill jobs--largely street-vending and domestic employment. A survey of eleven pueblos jóvenes and similar low-income communities conducted by the Mutual Metropolitana of Lima in 1978 indicated that only 48.6% of workers had stable incomes. At the same time, inflation has hit hardest at those in the lower socio-economic strata. A study conducted by the Compañía Peruana de Investigaciones de Mercado in June 1978 indicated that the loss in real income for the average low-income Lima household from December 1975 to December 1978 was 29.5%. A low-income family had to spend 67.4% of its earnings on food and a very low-income family spent up to 74.3% on food.<sup>1/</sup>

The impact of inflation and high interest rates has forced the sizeable proportion of the population which lives in huts made of reed mats (esteras) or in partially-built homes of more solid material (usually brick) to postpone construction of more adequate shelter. Nevertheless, the residents of pueblos jóvenes place a high priority on the acquisition of their own homes and are prepared to make considerable sacrifices in order to obtain them. Status is probably as much involved as the physical need for shelter, as evidenced by the use of expensive materials such as brick rather than less costly but serviceable alternatives.

Given the high incidence of unemployment, underemployment, poor housing, lack of basic infrastructure, and the large percentage of family income which must be spent on food, it is not surprising to find that serious health problems beset the squatter communities. In addition, more than 25% of low-income families in metropolitan Lima suffered from severe nutritional inadequacy in 1979. <sup>2/</sup> The impact of these figures can be seen in related statistics of the Children's Hospital of Lima, where more than 69% of the children admitted in 1976 were malnourished; 29% of the infants under one year of age showed symptoms of third-degree (extreme) malnutrition.<sup>3/</sup> Medicines are almost totally beyond the reach of the target population, having risen 366% in price between 1972-1976. While health posts sponsored by the Ministry of Health, private voluntary organizations and the communities themselves do exist, they do not begin to meet the need. Many remain empty shells, since neither the government nor other sponsors can finance operating costs.

The environment itself of the pueblos jóvenes constitutes a health hazard. Some squatter communities are on former municipal garbage dumps. Garbage collection in the pueblos jóvenes is sporadic; and mounds of garbage, often burning, are a common sight in many of the low-income communities.

<sup>1/</sup> AID:PERU Research on Malnutrition...A Quantitative Study on the Recent Situation in Lima. Mission Memorandum A-19, May 7, 1979.

<sup>2/</sup> Ibid.

<sup>3/</sup> Instituto Nacional de Estadística (INE) del Perú, El Niño en el Perú, Lima, 1979

Public education facilities in the low-income communities are not adequate. Private programs, such as the schools of Fe y Alegria, a church-sponsored program, must supplement public resources. Pre-school and child care facilities are scarce, in spite of the efforts of public and private resources in this area. In 1977, only 1,970 infants were cared for in nurseries in metropolitan Lima. A 1979 study indicated that in 1975 only 5.5% of the children eligible for the services were enrolled in pre-school centers in Peru.<sup>1/</sup>

The role and situation of women in the pueblos jóvenes is an area in which few studies have been made. Although women heads of households are not formally discriminated against in terms of property rights and eligibility for credits, much more needs to be known about their number, marital status, economic and family role, and their attitudes and needs. Informal observation and interviews, as well as such data as exist, suggest that the move from the rural environment to the cities radically changes their position. Most households in Peru are headed by men and they, in fact, would tend to be preferred beneficiaries under the proposed project; however, women heads of households will be encouraged to take advantage of their rights. An attempt will be made to ensure that benefits are distributed equally between men and women heads of households.

In the rural setting women have an important role in almost all phases of agricultural production and marketing, as well as the traditional responsibilities of child-rearing, housekeeping, sewing, cooking, and tending to domestic animals. They also play an important economic role in producing handiwork ranging from knitted alpaca sweaters and ponchos to woven rugs, baskets, and ceramics. These are all important sources of family income. Few rural women, however, have formal jobs outside the domestic setting. While schools are nominally open to both boys and girls, few rural women complete their primary education. Literacy rates for rural women are considerably lower than those of rural men.

When these women come to the cities, they are ill-prepared for the challenges of urban life. While many of their family responsibilities (child rearing, housekeeping, cooking) remain the same, they are cut off from many other areas of their former lives which gave them standing in the family. The natural resources which contribute to housekeeping and economic support in rural areas are not available in urban areas. There are little data on the raising of domestic animals in the pueblos jóvenes although some of this does take place on a very limited scale. There appear to be few cottage industries in the urban communities which might give women opportunities to supplement family income. Women's activities are therefore much more circumscribed to housekeeping and child rearing in the cities. On the other hand, economic realities have forced more and more of the women to seek employment outside of the home. Their poor educational background and almost total lack of vocational preparation leave them few employment alternatives other than street-vending and domestic service. Child care is becoming an increasingly important problem for these women. It should be added that the phenomenon of women heads of households is much more prevalent in the cities than in the rural areas.

<sup>1/</sup> Overseas Education Fund of the League of Women Voters, Child Care Needs in Urban and Rural Peru, Washington, D.C., August 1979

2. Organizational Context. The pueblos jóvenes of Peru are unique in that the Peruvian government has institutionalized what in many other developing countries are allowed to remain simply as chaotic by-products of the development process. Originally termed barriadas, the shanty-towns which began to spring up around Peruvian cities in the 1930's were later baptized as pueblos jóvenes ("young towns") by the Velasco administration in 1968, and an effort was made to change the negative image of the barriadas and to gain their support for the reforms and socio-economic changes planned by the revolutionary government. In order to channel and mobilize that support, the government created SINAMOS (Sistema Nacional de Apoyo a la Mobilización Social), a movement to create cadres at the grass-roots level to implement the proposed social and economic reforms. SINAMOS organized the pueblos jóvenes along the pyramidal lines which still are the basic organizational pattern of these communities. Each community block elected representatives to a neighborhood committee. This committee, consisting of a coordinator, treasurer, secretary and, optionally, a sports or recreation coordinator, women's committee representative, etc., in turn sent its coordinator to represent it on a central committee of the pueblo joven. The president of the executive committee was also the community's representative to a zonal association of pueblos jóvenes, and this association was represented at a city-wide association of the communities.

The social promoters gave this structure considerable technical assistance in organizational techniques and leadership development, which enabled the communities, with SINAMOS frequently playing an ombudsman role, to gain access to the central government for assistance or solution of problems to a degree they had never known before. SINAMOS's backing was particularly helpful in moving many communities through the frequently tortuous remodeling-entitlement process which had been established to formalize the situation of the families living on invaded land and to help the communities to obtain basic infrastructure.

Those communities which received concentrated technical assistance from SINAMOS have maintained their cohesion and the advantages are apparent in the degree to which they have been able to move ahead in obtaining infrastructure, building permanent shelter, developing green areas and other community facilities. The MOHC, as a policy matter as well as budgetary restrictions, provides only limited technical assistance to the pueblos jóvenes, and this is focused on moving them through remodeling-entitlement. The MOHC's current resources cannot adequately meet the need for assistance even on this level.

As a result, many community organizations are experiencing varied degrees of disintegration, lack of confidence in their leadership, lack of member participation in meetings and community affairs, and inter-personal, intra-community dissension. This tends to weaken the effectiveness of community decision-making on important issues such as infrastructure projects and other joint community activities. Frustration and narrow interests sometime prevail and costly mistakes are made. Two instances serve to illustrate this point. In one case a community was divided over the issue of whether to install both water and a sewerage system. One group wished to go ahead with the project, another group balked at the cost. Community

leadership was not able to resolve the issue. As the debate went on for many months, costs rose, to the dismay of the group which wanted to go ahead with the project. Finally it decided to move on its own, and had the infrastructure installed for the half of the community it represented leaving the other half without these services. At last report the situation had not changed, and the community's social fabric had been torn apart in terms of pulling together in the future resolution of other community needs. A second instance, in another smaller community, saw a similar controversy arise over the issue of electricity, with the same results. It is important to note these examples since the neighborhood councils will have an important role in project development.

3. Institutional Relationships. The BVP has had considerable experience dealing directly with low-income communities. Since 1969 the BVP, assisted by AID development and HG loans, has been instrumental in financing low-cost and self-help shelter as well as basic infrastructure programs.

The BVP is sensitive to the requirements of the target group. It is to establish a new department which will, inter alia, work with the low-income communities. The department can open the door to a variety of expanded roles for the BVP in the pueblos juvenes and other low-income communities.

The utility concessionaires involved with the project (ESAL, ESAR, Electro-Lima and Electro-Peru) have had considerable experience in working with the BVP, in low-income communities, and with private contractors in similar projects. There has, however, been a feeling expressed by some representatives of the pueblos juvenes that the utility companies have not always been sensitive to their needs. Whether these complaints have merit or not, it will be important for the representatives of the companies, as well as those of the BVP and private contractors, to establish a climate of mutual trust in negotiations with the communities, and to make certain that the terms and procedures of the proposed sub-projects are clearly understood during both the design and the implementation phases.

4. Motivation. If past performance is indicative, there will be considerable interest on the part of the target group to participate in the project. The installation of these facilities provides electricity and water at significantly lower cost than water from trucks and other sources of illumination.

5. Obstacles. While the proposed loan follows in the steps of previous similar programs, it is nonetheless important to flag possible obstacles to attaining project objectives.

a. Disparities in income, particularly during the severe recession that Peru currently is experiencing, may create problems in reaching community agreement. Delays or even indefinite postponement of projects can result, as has occurred in the past.

b. The success of the proposed projects depends on the effective functioning and participation of community councils. While many existing councils continue to function well, others do not function as well for a variety of reasons. With the restricted resources of the MOHC, a technical

assistance vacuum exists, and the councils are largely left to shift for themselves. Technical assistance by the BVP will be essential to sub-projects. Coordination with the MOHC is important as a means of increasing the impact of technical assistance to the community organizations.

c. The sophistication and effectiveness of community organizations is more limited in cities outside of Lima. Particular sensitivity and skills will be required in order to avoid misunderstandings.

6. Communication Strategies. Information on the programs must be made available to the target groups. This will require the BVP to use diverse channels of communication which are most likely to reach those living in the pueblos jovenes and similar communities. The technical assistance and community organization units of the Ministry of Housing could play a useful role in this regard.

7. Spread Effects. There will be several important spread effects.

a. The program reinforces a model for the development of infrastructure projects in low-income communities which can be replicated by other government and private lending institutions.

b. The program provides opportunities for greater collaboration between the BVP and the MOHC.

c. Financing community facilities (schools, health posts, markets) will stimulate communities to improve their own organizational ability. The larger benefits accruing from such experiences are to increase community cohesion, to sharpen group problem-solving skills, and to enable the communities to move into broader areas of community development.

d. The project enables the utility companies and private contractors to work with low-income groups; and this continuing experience should provide a good base for further work with these groups outside of AID-sponsored programs.

e. The community facilities will strengthen collaboration between the communities and public institutions as well as among the institutions themselves.

f. Installation of electricity will provide opportunities for the development of cottage industries and small businesses.

8. Social Consequences and Benefit Incidence. Those most immediately benefitting from this program will be the individual families which participate in HG loan projects. The most tangible benefits will be in improved health, decreased costs for water and electricity, and increased security (often mentioned as a prime concern where electricity for illumination is lacking). The communities themselves will benefit from an improvement in self-image, which can act as a strong psychological stimulus to seek further improvements on an individual and community level. The communities will further benefit directly from the strengthening their organizational capabilities and indirectly from the increased coordination among public and private institutions which should result.

Contractors, laborers and others involved in diverse segments of the construction industry will also reap economic benefits. A large percentage of the laborers employed in construction projects live in pueblos jovenes and similar communities.

Women may experience a number of direct and indirect benefits. Water connections and electricity will make the task of housekeeping considerably easier. Improved health will have a positive impact for women as individuals and in their role as family nurse. Increased organizational activities in the community can provide new outlets for women to participate in planning for community development. Women could benefit economically through employment on various levels in health posts, schools, and child care centers and in community-based industries.

The poorest of the pueblos jovenes and other low-income communities whose income level puts them below the range of any credit program will not benefit directly from the current loan except insofar as the project provides employment for construction laborers.

9. Changes in Power and Participation. The project stresses participation of neighborhood councils in the design and development of projects and will make technical assistance through the BVP available to these councils to ensure that their participation is effective. The important involvement of the neighborhood councils in activities which will have considerable impact on their communities should enhance their ability to deal with public and private institutions in the future, giving the communities greater control over their development.

#### E. Technical Feasibility

##### 1. Technical Considerations.

a. Electricity and Public Lighting. This sub-program encompasses the implementation of low-tension electrical networks, including the household connection with its respective meter, and connections to high tension lines and transformers. These low-tension networks will also include public lighting.

The plans, materials, equipment, and construction standards will adhere to the specifications of the Electric Code of Peru (which is similar to the U.S. National Electric Safety Code) and will require prior approval by the local utility company.

While costs will vary from one sub-project to another due to site differences and distances from primary systems, it is estimated that the cost for low-tension, public lighting and house connections, including meters, will average S/150,000 (\$576) per lot. (See Annex M, "Illustrative Cost Estimates for Public Utility Projects.")

The MOHC realizes that infrastructure costs could be reduced if more appropriate codes and standards were adopted. It has a continuing program to have reduced standards adopted. As in the case of Project 010, utility companies will once again be urged to utilize cost-saving features such as: (a) paired house connections with meter boxes back-to-back; (b) using standard, mixed-light lamps costing S/6,900 each in place of mercury vapor lamps which cost S/31,800 each; and (c) overhead wiring in place of underground where terrain and maintenance cost analysis indicate clear economies.

b. Water Supply. This sub-program will provide piped potable water and includes the following components: (1) connections to existing main trunk lines; (2) secondary lines network; and (3) house connections including meters. In certain cases additional funds will be allocated to provide for the extension of primary trunk lines, deep wells, pumping stations or other similar solutions. Nevertheless, one of the criteria for sub-project approval will be location relative to a main basic infrastructure facility for water.

Plans, materials, equipment and construction standards will adhere to the Sanitary Norms of the Rules for Construction of Peru, and will require prior approval of the respective utility company and/or the Regional Office of the Ministry of Housing.

As in the case of electricity costs will vary from site to site; but the average unit cost per household is estimated to be S/202,000(\$776).

c. Sewerage System. This sub-project includes: a) house connections, including inspection boxes; b) street line network; c) trunk lines discharging into primary collectors, or pumping substations or treatment plants, or into open waters. Total costs of a given project will vary in accordance with the location and topographic conditions. The average cost per household is estimated to be S/223,000 (US\$858).

As in the case of water supply sub-projects, the plans, materials equipment and construction standards will adhere to the provisions of the Sanitary Norms of the Rules for Construction of Peru, and will require prior approval of the respective utility company and/or the General Directorate for Sanitary Works of the Ministry of Housing. With a view to cost savings, utility companies will be requested to examine the possible use of pairing two house connections at the lot lines. Furthermore, depending on the type of terrain and lot size, the alternatives of individual and multiple-unit septic tanks will be studied.

d. Home Improvements. The administration and supervision of this sub-program will be delegated by contracts to the S&Ls by the BVP. The S&Ls have competent technical personnel to evaluate the individual loan requests as well as to inspect and monitor the execution of the repairs, additions, and improvements to homes. All works will adhere to the National Construction Code of Peru. The maximum individual loan amount will be S/650,000 (US\$2,500), with the average loan expected to be considerably below this figure.

Home improvement loans can cover:

- (1) Interior installation of water, sewerage and light,
- (2) Floors, ceilings, roofs, and carpentry work,
- (3) Expansion of the unit,
- (4) Repair and/or replacement of deteriorated building components.

This sub-project line of financing will test the priority which pueblos juvenes give to communal facilities and will test the flexibility and administrative capability of the responsible governmental agency to receive, staff and/or equip and subsequently maintain the specific facility. Such facilities offer no particular problems from a design or construction perspective. Design must conform to the standards and specifications of the agency which will "receive" the facility.

## 2. Construction Aspects.

a. Use of aided self-help. Peru has a long and quite positive tradition of widespread community participation in the construction of public and community works. The success of self-help efforts are clearly related to the degree of organization of any given community, and the extent to which a given contractor has discussed and arranged his work schedule with the community leadership. The basis for such local participation and its programming are items which must be covered in the construction contract.

b. Availability of Contractors and Building Materials. There are numerous contracting firms in the cities which are competent and available to undertake the volume of contracting represented by the current and projected investment level. Moreover, in the current context of a depressed construction sector, there is no likelihood of a constraint from this quarter.

The materials normally employed by the construction industry in the types of basic infrastructure services contemplated are fabricated locally. Only certain components of the electrical installations are imported.

c. Contracting Procedures. Bidding and contracting procedures will be those currently in force at the respective institutions. Given the various combinations from which contracts can result, experience would lead one to expect continuation of the combination of public bidding (mandatory for GOP entities), private competition with a minimum of 3 firms competing, and direct negotiation between a community association and a contractor.

Due to the recent high rates of inflation, construction contracts are no longer "fixed price" contracts. Rather, the GOP has devised and approved the application of periodic readjustments of contract costs based on the stage of work in place and employing a readjustment formula. In essence, the builder and his client fix in the contract the cost incidence of the various factors (labor, materials, etc.). On a monthly basis, the GOP publishes the indexes of costs for the different factors and the budget is accordingly readjusted.

d. Flow Chart for Typical Sub-Project Group. Annex N diagrams the stages a typical community might pass through. The chart assumes that the group originally settled on invaded government land, went through the various stages of legalizing tenure, and now is securing services and moving to higher stages of physical development of their shelter environment via this project. From the second level on down, the chart also serves as a typical flow chart for sub-project implementation showing principal benchmarks and the respective institutional responsibility.

### 3. Environmental Considerations

a. Summary of Initial Environmental Examination. Based upon the Initial Environmental Evaluation (IEE) performed in December 1979, a Positive Threshold Determination was recommended and approved. Therefore, further environmental planning was required. The reasons for making this Positive Determination consisted of two main findings: (1) strained municipal resources for supplying the intended services of potable water and sewerage; and (2) the potential for negative impacts caused by actions of the Peruvian natural environment (including earthquakes, landslides, floods, tidal waves, and unstable sand dunes).

#### b. Summary of results of further environmental investigations.

The findings of the second phase of environmental investigations result in an overall conclusion that the foreseeable positive impacts of the proposed action should markedly outweigh the foreseeable negative impacts. The essence of the program is to bring improved infrastructure services to those who totally or partially lack them. Therefore, from the environmental standpoint, the program should be implemented. This conclusion is based on extensive work during HG-010 and subsequent fieldwork for the current HG.

As continually indicated by conditions throughout the Peruvian urban environment, the two basic concerns enunciated in the IEE remain as the salient environmental difficulties to be mitigated: (1) the carrying capacity of urban infrastructure systems; and (2) the recurrent negative natural phenomena must inevitably guide and mold the ensuing project development process. In order to ensure sound project-specific decisions, the twin principles of site selection criteria and appropriate design criteria can be utilized.

Therefore a methodology was developed jointly by the BVP and AID, attached in Annex G as the Environmental Checklist, to achieve this goal. A full range of environmental concerns are delineated by the form. A quickly-apparent sense of environmental difficulties can be gained by reviewing the results of the questionnaire. Space is provided for observations responding to any perceived difficulties. A project may be rejected if the results of the environmental investigations leave no room for prudent and feasible project modifications. The BVP has in the past suffered from environmentally unsound projects, so they are conscious of the need for environmental planning. The BVP responded quite positively to the development of the environmental checklist.

Importantly, the issues raised by the checklist will be presented to project initiators by the BVP. In this manner, each proposal will be required to set forth the salient environmental conditions associated with it. At the present time there are, inter alia, requirements for soil analysis, certification of potable water availability, and project permits from the municipal authority. This form would build upon these existing requirements and result in a greatly improved environmental review of each proposal. The Mission Engineering Department is staffed by personnel who would periodically review BVP proposals for AID financing including their environmental component.

c. Recommendations. In order to ensure sound environmental planning for the program, the following recommendations are offered:

(1) Utilize the environmental planning forms which have been developed by the BVP in conjunction with DS/H technical assistance for the technical analysis of all proposals.

(2) As corollaries to the above recommendation, the following concepts should be continued.

- Specific infrastructure elements (water, sewerage, electricity) should be selected in each particular project only where there is proven capacity to supply such elements. Such selection may include all three elements, a lesser number in combination or just one element for a specific site. Provision of services should be determined within the municipal context, so that aspects such as daily level of service and average consumption rates will be controlled by intrinsic municipal capabilities and practices.
- Site selection of locations should occur only in those areas which are not environmentally disaster-prone.

(3) In conjunction with the proposed TA regarding existing building and infrastructure standards and specifications, it is recommended that environmental factors be explicitly included within the criteria used to measure the degree of appropriateness of the existing regulations. For whatever gaps are found, then the opportunity should be utilized to incorporate environmental planning into the proposed changes in order to close the gaps.

#### F. Technical Assistance

Section II-B-5 (Project Inputs) briefly describes and costs the two proposed T.A. elements and the associated IIPUP program. The goal of the first T.A. is to lower the costs of basic shelter services so that they can be afforded by a greater percentage of the target group. The BVP is setting up a committee which will review current standards and specifications. The aim is to devise a set of recommendations on how existing codes should be modified in order to better accommodate the target group. The project T.A. would work with the BVP committee on this task. The recommendations would be submitted to the Ministries which establish norms and have the authority to modify standards and specifications.

In addition to the above T.A. inputs, the Mission has requested DS/H assistance in the monitoring of the environmental review work to be conducted by BVP. An Environmental Consultant will visit Lima periodically (twice a year) during the implementation phase of HGs 010 and 011. The environmental T.A. builds on the achievement to date. An environmental checklist has been developed with the BVP. Short-term consultant T.A. will ensure that the checklist is maintained up to date and is incorporated into the BVP sub-project approval criteria, and that it becomes a standard consideration in project design and site selection.

In preliminary conversations with the new President of the BVP it was evident that the Belaunde government will be actively undertaking a study of standards in an effort to reduce the cost of services to be developed in low-income areas. He was particularly pleased that HG resources could be used to support the effort. He also felt that BVP is in a position to influence the scope of work of the study, probably to be directed by the MOHC, as well as to be an active participant in the review process.

The scope of work of the standards review and recommendations study group would be to:

- (a) Review typical standards being utilized in developing basic services projects (sewerage, water, electricity) in low-income areas, and to establish the component costs of each of the related basic services (e.g., sewerage: sewerage treatment, collection lines, individual house connections, and inside dwelling unit fixtures).
- (b) Review innovative projects that have been developed by utility companies and to determine component costs for each service.
- (c) Scan the literature for other experimental standards being utilized in the design of basic services systems.
- (d) Finally, and most importantly, find out what people in low-income areas can afford to pay for the various basic services and to determine what such investments can purchase in the way of basic services; develop recommendations based on what people can afford to pay, taking into consideration items a-c above; and present the findings and recommendations to the appropriate Ministries for their review and promulgation of new standards that are appropriate to the needs and capacity to pay of the target group.

A special working committee would have to be created composed of representatives from the Ministries of Housing, and Mining and Energy, the utility companies, and the BVP. HG loan resources would provide staff support to this working group. Staff (HG-supported) would consist of:

	Days	Total Cost
Engineer (US) <sup>1/</sup>	10 (US) 15 (Lima)	\$ 9,300
Engineer/Planner (Peruvian)	100	9,200
Social/Planner (Peruvian)	40	3,000
Local Travel		\$21,500
		2,500
		<u>\$24,000</u>

AID also should be prepared to support the efforts of the new government as it undertakes the basic studies preparatory to establishing long-term shelter sector policies. DS/H and the Mission will also provide on-going progress in placing HG-generated resources, establishing and maintaining cost recovery records, and reviewing longer range financial projections of the Bank. The mission also will provide limited technical assistance in the engineering review of projects.

D. Other Donors

The GOP currently is receiving assistance in the shelter sector from:

-- an IDB concessional loan of \$30.5 million to carry out the third stage of the National Water Supply and Sewerage Plan in 27 cities--all major cities except Lima and Arequipa. The work on this loan is expected to be completed by 1981. The interest rate on the loan is 2%; the loan is for 30 years with a 7 1/2 year grace period.

-- a World Bank loan of \$21.6 million plus counterpart funds for sites and service projects in Lima and Arequipa. Most of the loan is being used for industrial parks, access roads, health centers, and other community facilities. The project is expected to be completed by December 1982. The interest rate on the loan is 8.85%; the loan is for twenty years including a three year grace period.

-- a World Bank loan of \$8.8 million plus counterpart financing to assist ESAL lay the basis for a long-term solution of Lima's water supply problems. The interest rate on this loan is 7.35; the loan is for 10 years including a 2 1/2 year grace period.

These projects complement the purposes of the proposed loan by increasing the capacity of infrastructure services. The cost recovery philosophy of the projects is consistent with the proposed recovery systems for this project. The Mission has begun to work with the World Bank in the development of policy issues and related studies that should be considered by the new government. The Mission and the World Bank will jointly encourage the GOP to develop a more comprehensive urban development policy, including the definition of investment programs to which aid donors can rapidly respond.

1/ It is contemplated that the Senior Engineer will develop an in-depth scope of work for this study. A methodology which would enable the Peruvians to consider the maximum range of technologically feasible variables in designing the lowest cost shelter and infrastructure will be utilized.

#### IV. IMPLEMENTATION

##### A. Implementation Plan

1. Participating Entities. Section III-C "(Administrative Feasibility)" identifies and evaluates the participating entities for the project and examines the roles which each entity is to perform.

2. Activities Scheduling. The implementation plan itself takes the project from authorization through the commitment and disbursement of the \$20 million. It is expected that the sub-projects will be approved and committed within two years according to the following implementation schedule.

	<u>Responsibility</u>	<u>Time/By Date</u>
a. Project Authorized	AID/W	09/80
b. Letter of Advice	DS/H-USAID	10/80
c. Negotiate Implementation Agreement		11/80
d. Conditions satisfied including USAID approval of BVP Implementation Plan which lists participating entities, assignment of money, operating agreement.	USAID/BVP	03/81
e. Advertisement for Investor	DS/H	04/81
f. Contract Agreements Negotiated and Signed	BVP/Investor	06/81
g. BVP requests an advance of funds from USAID	USAID	06/81
h. BVP refines local promotion plan; projects are submitted by community associations (CA); select projects based on project selection design criteria developed between BVP and S&Ls.		06/81
i. BVP sign implementation agreements with participating community associations and concessionaires (C).	CA	07/81
j. Local concessionaires and/or community associations will contract with contractor (CN) to develop site plans and cost estimates.	BVP/CA/CN	07/81
k. BVP will periodically conduct field checks of projects as will the Engineering Office USAID.	BVP/USAID	06/81
l. First Annual Evaluation	USAID	06/82
m. Continuation of project through		06/83

3. Disbursement Procedures. Disbursement procedures for the loan will be in accordance with the Implementation Agreement and the Loan Agreement negotiated with the investor(s).

B. Evaluation

A regular evaluation is planned. The progress of the project will be evaluated on an on-going basis in terms of the Logical Framework (see Annex D). Joint AID/BVP evaluations will assess the overall progress against an agreed upon implementation plan. Regular annual evaluations are planned using the DS/H Evaluation Guidelines.

C. Conditions, Covenants, and Negotiating Status

1. Negotiation. After authorization of the loan, standard DS/H implementation procedures will be followed in implementing the program. It is anticipated that the four basic DS/H contract documents will be negotiated and signed by February 1981.

2. Conditions Precedent. It is expected that the conditions precedent will be met before an investor is sought or the first loan disbursement to the borrower.

a. Prior to first disbursement under the loan, the borrower will submit, in form and substance satisfactory to AID, evidence that the BVP has implemented new administrative procedures that are designed to improve BVP's management of AID supported projects. Such evidence shall include information that:

- 1) The BVP has revised internal project review procedures and has simplified the project approval process.
- 2) The BVP has revised procedures to expedite the acceptance of project construction by utility companies and GOP agencies.
- 3) The BVP has analyzed the capacity of community promotion agencies and has entered into contracts with competent entities that will be in charge of assisting in organizing project beneficiaries. The contracts will include provisions requiring such entities to communicate bank requirements for projects to beneficiaries; to obtain, in certain instances, subscription contracts from project beneficiaries; and to keep project beneficiaries apprised of project costs revisions.
- 4) The BVP has developed a reporting system that shows on a regular basis the repayment record of loans by project beneficiaries and actions taken in dealing with default problems.
- 5) The BVP has established an evaluation system and will include in this system means to monitor how a project affected the intended beneficiaries after completion of the project.

In addition the BVP shall submit to USAID evidence that it has developed an effective mechanism to assist community groups seeking financing under this project. At a minimum this evidence shall include: (1) simple written promotional materials describing the program and its requirements; (2) a step-by-step breakdown of the process to be undertaken to obtain financing; and (3) an orientation and training capability which could be made available to community groups and their representatives.

b. The BVP will submit evidence to USAID that it has created a project implementing agencies work group that will expedite project implementation prior to the first loan disbursement.

c. BVP will submit a Master Project Delivery Plan to the Mission prior to advertising for a lender.

d. Before the first loan disbursement, the BVP in consultation with appropriate GOP entities will submit to the Mission the terms of reference for a construction standards and cost study that will ensure that the lowest cost appropriate technology is being employed in HG projects. This study will be conducted during the initial phase of this project and will be financed, in part, with HG loan resources.

e. Prior to the disbursement of any monies in excess of \$5.0 million under the loan, and within twelve months from the date of the signing of the implementation agreement, the Ministry of Housing and Construction (MOHC) will submit to AID in form and substance satisfactory to AID: (1) a scope of work developed by MOHC, in consultation with World Bank and AID, an implementation plan and a budget for an in depth urban policy review to be undertaken by the Ministry of Housing and Construction; and (2) evidence that the BVP has approved that part of the policy review budget that is related to the use of HG resources.

(Note: World Bank Urban Mission leader anticipated that work on policy issues should be completed by October 23, 1980. USAID/Peru will then work with Ministry of Housing on the outline for the proposed policy study, based largely on findings and recommendations of the World Bank.)

### 3. Covenants

a. Rollover funds including net proceeds earned from the loan monies held in escrow are to be used for the same purposes as specified in the BVP for the original project.

b. The implementation agreement will include a covenant to meet the recommendations of the environmental assessment as set forth in the Project Paper.

c. In the case of ancillary facilities which are not self-financing, a written assurance will be obtained that operating and maintenance costs will be provided by the appropriate Ministry or other agency. This assurance will be a part of sub-project documentation and will be subject to the approval of AID.

ANNEX A

DEPARTMENT OF STATE  
Agency for International Development  
Washington, D.C. 20523

GUARANTY AUTHORIZATION

Provided from: Housing Investment Guaranty Authority  
Peru : Housing Bank of Peru  
Project : Upgrading Low Income Settlements #527-HG-011

Pursuant to the authority vested in the Assistant Administrator, Bureau for Latin America and the Caribbean by the Foreign Assistance Act of 1961, as amended (FAA), and the delegation of authority issued thereunder, I hereby authorize the issuance of guaranties pursuant to Section 222 of the FAA of not to exceed twenty million dollars (\$20,000,000) in face amount, assuring against losses of not to exceed one hundred percentum (100%) of loan investment and interest with respect to loans by eligible U.S. investors ("Investor") acceptable to A.I.D. made to finance basic services for upgrading low-income settlements in Peru.

This guaranty shall be subject to the following terms and conditions:

Term of Guaranty: The loan shall extend for a period of up to thirty years (30) from the date of disbursement of the first installment of the loan, including a grace period on the repayment of principal not to exceed ten (10) years. The guaranty of the loan shall extend for a period beginning with the first disbursement of the loan and shall continue until such time as the Investor has been paid in full pursuant to the terms of the loan.

2. Interest Rate: The rate of interest payable to the Investor pursuant to the loan shall not exceed the allowable rate of interest prescribed pursuant to Section 223 (f) of the FAA and shall be consistent with rates of interest generally available for similar types of loans made in the long-term United States capital markets.

3. Government of Peru Guaranty: The Government of Peru shall provide for a full faith and credit guaranty indemnifying AID in United States dollars assuring against all losses arising by virtue of A.I.D.'s guaranty to the Investor or from non-payment of the guaranty fee.

4. Fee: The fee of the United States shall be payable by Borrower in dollars and shall be one-half of one percentum ( $\frac{1}{2}\%$ ) per annum of the outstanding guaranteed amount of the loan plus a fixed amount equal to 1% of the loan to be paid as A.I.D. may determine upon disbursement of the loan.

5. Other Terms and Conditions: The guaranty shall be subject to such other terms and conditions as A.I.D. may deem necessary.

\_\_\_\_\_  
Acting Assistant Administrator  
Bureau for Latin America and the  
Caribbean

Date: \_\_\_\_\_

Clearance:

DS/H: David McVoy \_\_\_\_\_

GC/H: Barbara Davis \_\_\_\_\_

DS/H: Margery Sorock \_\_\_\_\_

SER/FM/LD: Ernest Wilson \_\_\_\_\_

LAC/SA: William Rhodes \_\_\_\_\_

GC/LAC: Barton Veret \_\_\_\_\_

LAC/DR: M. Brown \_\_\_\_\_



MINISTERIO DE ECONOMIA Y FINANZAS

Lima, 22 SET. 1980

OFICIO N° 7575 -80-EF/75.02

SEÑOR : Carlos Morales Machiavello  
 Presidente del Banco de la  
 Vivienda del Perú

ASUNTO : Programa de Garantía para Vivienda N° 527-HG-  
 011 por US\$ 20'000,000

REFERENCIA : Oficio N° 6718-80-EF/101-44

Por encargo del Ministro, es grato dirigirme a usted, en relación a su oficio de la referencia en el cual solicita la decisión de este Ministerio respecto a la conformidad de las gestiones realizadas ante la Agencia para el Desarrollo Internacional -AID-, para la obtención de recursos dentro del Programa de Garantía para Vivienda a efecto de destinarlo al financiamiento de proyectos de asentamiento habitacional, orientados a familias de bajos ingresos.

Al respecto, me permito manifestarle que no existe inconveniente en que el Banco de la Vivienda del Perú continúe con las referidas gestiones, debiendo iniciarse en el momento oportuno las coordinaciones correspondientes con el Instituto Nacional de Planificación.

Es propicia la oportunidad para expresar a Ud. los sentimientos de mi especial consideración.



Atentamente,

*Benedicto Ciguena Guevara*  
 BENEDICTO CIGUENA GUEVARA  
 Director Superior de Hacienda

MINISTRY OF ECONOMY AND FINANCE

(TRANSLATION)

Lima, September 22, 1980

Letter No. 1575-80-EF/75.02

TO : Mr. Carlos Morales Machiavello  
President  
Housing Bank of Perú

SUBJECT : Housing Guaranty Program No. 527-HG-011  
for US\$20'000,000

REFERENCE: Letter No. 6718-80-EF/101-44

By request of the Minister, I am pleased to address you with regard to your letter of the reference, in which you solicited the concurrence of this Ministry for the processing of the obtention from AID resources from the Housing Guaranty Program to finance shelter projects for low income families.

To this respect, I advise you that there is no inconvenience in the Housing Bank of Peru continuing with the referenced actions including at the appropriate time, the needed coordination with the National Planning Institute.

At this time, I would like to express you the assurances of my special consideration.

Sincerely,

Benedicto Cigueñas Guevara  
Director Superior  
Ministry of Economy and  
Finance

CR

*Banco de la Vivienda del Perú*  
*Presidencia*

" Año de los deberes Ciudadanos "

Lima, 23 de Setiembre de 1980  
N° 7162/30-EF/401.10

Señor  
Leonard Yacger  
Director USAID - Lima  
CIUDAD

Ref.: Programa de Garantía para Vivienda  
N° 527-HG-011 U.S. \$ 20 millones

Asunto: Actualización de planteamiento del B.V.P.

De mi consideración :

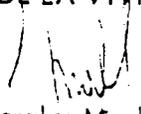
Me es grato dirigirme a usted, en atención a la solicitud que nos formulara AID con carta de fecha 27 de Agosto de 1980, respecto a la actualización de nuestro planteamiento para la obtención de recursos para el financiamiento del Programa indicado en la referencia.

Sobre el particular, me complace poner en su conocimiento que, contando con la opinión favorable del Ministerio de Economía, Finanzas y Comercio, según oficio N° 1575-30-EF/75.02 cuya copia se adjunta, nuestra Institución proseguirá con los trámites subsecuentes conducentes a que la Agencia para el Desarrollo Internacional nos extienda la garantía correspondiente al Préstamo que por U.S. \$ 20 millones gestiona el Banco para el financiamiento del Programa N° 527-HG-011.

Pendiente de la comunicación de AID respecto a la garantía antes referida, hago propicia la oportunidad para renovar a usted, los sentimientos de mi especial consideración y estima personal.

Muy atentamente,

BANCO DE LA VIVIENDA DEL PERU

  
Carlos Morales Machiavello  
Presidente

# TELEGRAM

INDICATE  
 COLLECT  
 CHARGE TO **USAID**

	FROM: <b>EMBASSY LIMA</b>	CLASSIFICATION: <b>UNCLASSIFIED</b>	
12065: O. <del>11892</del>	M/A <span style="float: right;">7</span>		
TAGS: SUBJECT:	<b>ROF Request for FY-80 Housing Guaranty Project 527-HG-011</b>		
ACTION:	<b>SecState MASHDC <u>IMMEDIATE</u></b>		
	<b>UNCLASSIFIED-LIMA</b>		
	<b>AIDAC</b>		
<u>DIST:</u> AMB DCM ECON USAID CINCH	<b>FOR: M.Parker, LA/DR; M.Serock, DG/M</b>		
	<b>REFERENCE</b>		
	<p>1. The Mission received September 23, 1980 the following letter in Spanish from the President of the Housing Bank of Peru requesting the proposed Housing Guaranty Project 527-HG-011 for \$20 million dollars:</p> <p>(quote I am pleased to address your request dated August 27, 1980, with regard to the updating of our request of resources for the financing of the referenced program.</p> <p>On this matter, I have the pleasure of informing you that we have the favorable opinion of the Ministry of Economy, Finance and Commerce, by letter No. 1575-80-EP/75.02, copy of which is attached, and that our Institution will continue with the corresponding process to obtain from the Agency for</p>		
DRAFTED BY:	<b>UDO:PCWitala:sgn</b>	DRAFTING DATE: <b>9/23/80</b>	TEL. EXT. <b>430</b> CONTENTS AND CLASSIFICATION APPROVED BY: <b>D:Leonard Yeager</b>

REFERENCES:

**HLA:Switzer**

**UNCLASSIFIED**

CLASSIFICATION:

**UNCLASSIFIED**

Classification

**International Development the Guaranty for the US\$20 million  
loan to finance the 527-HG-011 Program.**

**XXX awaiting communication from AID on the ref. guaranty,  
we express to you our special consideration and personal  
esteem. /Signed by the President of Housing Bank of Peru  
(Carlos Morales Machiavello)**

**2. Will pouch to LA/DE copy of letter plus backup letter  
to BVP from the Ministry of Economy and Finance for  
inclusion in the Project Paper.**

**XXXXXXXX**

**SILVERMAN**

**UNCLASSIFIED**

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

THE HOUSING GUARANTY PROGRAM

STATUTORY CHECKLIST

PERU

Answer YES/NO (\* Items  
Requires Reference to  
Project Paper Pages)

A. General Criteria Under HG Statutory Authority.

Section 221(a)

Will the proposed project further one or more of the following policy goals?

- (1) is intended to increase the availability of domestic financing by demonstrating to local entrepreneurs and institutions that providing low-cost housing is financially viable; No
- (2) is intended to assist in marshalling resources for low-cost housing; No
- (3) supports a pilot project of low-cost shelter, or is intended to have a maximum demonstration impact on local institutions and national policy; and No
- (4) is intended to have a long run goal to develop domestic construction capabilities and stimulate local credit institutions to make available domestic capital and other management and technological resources required for low-cost shelter programs and policies? Yes

Section 222(a)

Will the issuance of this guaranty cause the total face amount of guaranties issued and outstanding at this time to be in excess of \$1,555,000,000? No

Will the guaranty be issued prior to September 30, 1982. Yes p.3

Section 222(b)

Will the proposed guaranty result in activities which emphasize:

- |   |                |
|---|----------------|
| (1) projects providing improved home sites to poor families on which to build shelter and related services;                             | <u>Yes p.1</u> |
| (2) projects comprised of expandable core shelter units on serviced sites;  | <u>No</u>      |
| (3) slum upgrading projects designed to conserve and improve existing shelter;  | <u>Yes p.1</u> |
| (4) shelter projects for low-income people designed for demonstration or institution building; and                                      | <u>Yes p.3</u> |
| (5) community facilities and services in support of projects authorized under this section to improve the shelter occupied by the poor? | <u>Yes p.1</u> |

Section 222(c)

If the project requires the use of conservation of energy, was consideration given to the use of solar energy technologies, where economically or technically feasible?

N.A.

Section 223 (a)

Will the A.I.D. guaranty fee be in an amount authorized by A.I.D. in accordance with its delegated powers?

Yes

Section 223(f)

Is the maximum rate of interest allowable to the eligible U.S. Investor as prescribed by the Administrator not more than one percent (1%) above the current rate of interest applicable to housing mortgages insured by the Department of Housing and Urban Development?

Yes

Section 223(h)

Will the Guaranty Agreement provide that no payment may be made under any guaranty issued for any loss arising out of fraud or misrepresentation for which the party seeking payment is responsible?

Yes

Section 223(j)

(1) Will the proposed Housing Guaranty be coordinated with and complementary to other development assistance in the host country? Yes CDSS FY-81

(2) Will the proposed Housing Guaranty demonstrate the feasibility of particular kinds of housing and other institutional arrangements? Yes p.2

(3) Is the project designed and planned by A.I.D. so that at least 90 percent of the face value of the proposed guaranty will be for housing suitable for families below the median income, or below the median urban income for housing in urban areas, in the host country? Yes p.9

(4) Will the issuance of this guaranty cause the face value of guaranties issued with respect to the host country to exceed \$25 million in any fiscal year? No

(5) Will the issuance of this guaranty cause the average face value of all housing guaranties issued in this fiscal year to exceed \$15 million? No

Section 238(c)

Will the guaranty agreement provide that it will cover only lenders who are "eligible investors" within the meaning of this section of the statute at the time the guaranty is issued? Yes

B. Criteria Under General Foreign Assistance Act Authority.

Section 620/620-A

1. Does the host country meet the general criteria for country eligibility under the Foreign Assistance Act as set forth in the country eligibility checklist prepared at the beginning of each year?
2. Is there any reason to believe that circumstances have changed in the host country so that it would now be ineligible under the country statutory checklist?

Yes NS

No

PROJECT DESIGN SUMMARY  
LOGICAL FRAMEWORK

Life of Project:  
From FY 80 to FY 82  
Total U.S Funding \$5.0m  
Date Prepared: 5/08/80

Project Title & Number: 527-HG-011 Low Income Settlement Upgrading

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
<p>Program or Sector Goal: The broader objective to which this project contributes:</p> <p>Increase the availability of basic services affordable by low-income families.</p>	<p>Measures of Goal Achievement:</p> <ol style="list-style-type: none"> <li>Increase in number of urban poor who receive project services by supporting on-going GOP programs, principally BVP's basic services and community facilities projects.</li> </ol>	<ol style="list-style-type: none"> <li>Records of BVP performance to be provided by BVP.</li> </ol>	<p>Assumption for achieving goal targets:</p> <ol style="list-style-type: none"> <li>GOP policies and institutions will continue to support the self-help, evolutionary upgrading of low income neighborhoods.</li> <li>Economic recovery period will take place within 12-24 month period, thus permitting increased GOP support to sector.</li> </ol>
<p>Project Purpose:</p> <p>To assist GOP during economic recovery period to continue to finance a minimum level of basic infrastructure and community facilities and service projects in low income settlements in Lima and in other rapidly growing urban centers.</p>	<p>Conditions that will indicate purpose has been achieved: End of project status.</p> <ol style="list-style-type: none"> <li>Disburse \$20m HG loan within 2 years.</li> <li>Number of projects approved and families served.</li> <li>Rapidity of BVP response to promoting/developing projects.</li> <li>Low cost solutions being financed by BVP.</li> <li>Encouraging the development of projects in secondary and tertiary urban centers.</li> </ol>	<ol style="list-style-type: none"> <li>BVP reports based on implementation records including entities participating, number of individual projects, participants and unit costs.</li> </ol>	<ol style="list-style-type: none"> <li>BVP will be able to continue to expeditiously implement their programs.</li> <li>There are no unforeseeable delays in project approvals by MOKIC and participating agencies.</li> <li>Inflation does not drop so rapidly that the project interest rate exceeds the market rate during loan period.</li> <li>PP.JJ. community associations will cooperate as expected.</li> </ol>
<p>Outputs:</p> <ol style="list-style-type: none"> <li>Basic services and facilities packaged.</li> <li>Strengthened BVP system which enables it to attend to the needs of the target group.</li> </ol>	<p>Magnitude of Outputs:</p> <ol style="list-style-type: none"> <li>Water - 11,000</li> <li>Sewerage - 7,600</li> <li>Electric - 8,700</li> <li>Home improvement - 4,200</li> <li>Number of projects implemented</li> <li>Number of people impacted</li> </ol>	<ol style="list-style-type: none"> <li>BVP, participating entities records.</li> <li>Commitment and disbursement records.</li> <li>AID monitoring.</li> </ol>	<p>Assumptions for achieving outputs:</p> <ol style="list-style-type: none"> <li>There will be adequate effective demand for services.</li> <li>There will be sufficient applications for sub-projects.</li> <li>Sub-project approval and implementation procedures will be efficient.</li> </ol>
<p>Inputs:</p> <ol style="list-style-type: none"> <li>Housing guaranty loan.</li> <li>Government guaranty.</li> <li>Government assumption of exchange risk.</li> <li>5% down payment by target group.</li> <li>BVP workshops/seminars for S&amp;L's.</li> <li>BVP finances 10% of balance.</li> </ol>	<p>Implementation target (Type and Quantity)</p> <ol style="list-style-type: none"> <li>HG \$20m loan + local contributions.</li> <li>Disbursement of HG loan within 2 years of loan signing.</li> <li>Workshops/seminars/technical assistance                     <ol style="list-style-type: none"> <li>cost reductions introduced;</li> <li>environmental soundness system in place;</li> </ol> </li> </ol>	<ol style="list-style-type: none"> <li>Reports and records of AID, GOP, Investor, BVP, and S&amp;L's.</li> </ol>	<p>Assumptions for providing inputs:</p> <ol style="list-style-type: none"> <li>Investors will be found.</li> <li>GOP continues to give high priority to target group.</li> <li>No drastic decrease in present effective demand/affordability.</li> </ol>

NNNNVV ES80538RA558  
PP RUESLM  
LE RUFHC #9215/01 0831420  
ZNR UUUUU ZZH  
P 021244Z FEB 80  
FM SECSTATE WASHDC  
TO AMEMBASSY LIMA PRIORITY 2871  
BT

RECEIVED  
UNCLAS  
MAIL ROOM

**ACTION COPY**  
ACTION TAKEN: \_\_\_\_\_  
DATE: \_\_\_\_\_  
INITIALS: \_\_\_\_\_

UNCLAS SECTION 01 OF 02 SPATH 02015/01

AIDAC

E.O. 12065:N/A

A3S:

ACTION: *Lid*  
Info: *OR*  
*PLCC*  
*ENT*  
*JA*

*2/6*  
*5-29215*

SUBJECT: DAEC REVIEW OF PID FOR UPGRADING LOW-INCOME SETTLEMENTS

1. THE FIRST \$25 MILLION TRanche OF THE SUBJECT PID WAS REVIEWED AND APPROVED FOR PP DEVELOPMENT BY THE DAEC ON JANUARY 19, 1980. THE FOLLOWING GUIDANCE IS PROVIDED FOR PP PREPARATION. THE PROVISION OF FUTURE ASSISTANCE IN THE SECTOR IS DEPENDENT ON THE GOP'S PERFORMANCE IN FULFILLING CERTAIN POLICY ANALYSIS REQUIREMENTS WHICH WILL BE CARRIED OUT UNDER THE FY 80 HE (SEE PARA 2 BELOW). IF PERFORMANCE IS SATISFACTORY, THE MISSION WILL BE EXPECTED TO SUBMIT A PID FOR ANY NEW OR ADDITIONAL PROGRAM. THE MISSION IS ALSO ADVISED THAT THE FULL \$25 MILLION IN FY 80 MAY NOT BE AVAILABLE DUE TO LIMITATIONS IMPOSED ON HE.

2. PROJECT STRATEGY. THE DAEC ACKNOWLEDGED THAT THE PID OUTLINED DETAILS OF A SOLID BASIC HUMAN NEEDS PROJECT THAT FOCUSED DIRECTLY UPON MEETING SHELTER AND BASIC SERVICE NEEDS OF THE PERUVIAN TARGET GROUP. DESPITE RECOGNITION OF THESE POSITIVE FEATURES OF THE PROJECT, THE DAEC WAS CONCERNED WITH THE MISSION'S CONTINUING EMPHASIS ON PROVISION OF BASIC SERVICES WITHOUT FULLY ADDRESSING SOME FUNDAMENTAL PROBLEMS IN THE SHELTER SECTOR (E.G., LACK OF FINANCING FOR LOWCOST HOUSING, PROVISION OF THE FINANCIAL BASE OF THE HOUSING INSTITUTIONS AND ATTENDANT GOP INPUTS REQUIRED TO KEEP THE RVP AND SAL'S FINANCIALLY SOLVENT, INSUFFICIENT GOP BUDGETARY ALLOCATIONS TO THE SECTOR INCLUDING BASIC INFRASTRUCTURE AND UNCERTAIN GOP SHELTER POLICIES. FOR THE SHORT-TERM, HOWEVER, IT WAS RECOGNIZED THAT THE COUNTRY'S CURRENT ECONOMIC CRISIS PRECLUDED IMPLEMENTATION OF ANY ALTERNATIVE STRATEGY. OVER THE LONGER-TERM, THE MISSION IS ENCOURAGED TO DISCUSS THESE PROBLEMS AND OTHERS IDENTIFIED IN THE SHELTER ASSESSMENT AND SUBSEQUENT STUDIES WITH THE NEW GOVERNMENT, SCHEDULED TO TAKE OFFICE IN JULY, 1980. THE MISSION SHOULD URGE THE NEW GOVERNMENT TO ADDRESS THESE FUNDAMENTAL ISSUES IN A POLICY STUDY WHICH COULD BE FINANCED BY THE FY 80 HE LOAN AND WHICH WOULD LAY OUT A PLAN FOR COMMITTING GOP RESOURCES TO ASSUME AN INCREASING SHARE OF THE COSTS OF DELIVERING

BASIC SERVICES TO THE PUEBLOS JOVENES AND FOR PLACING THE FINANCIAL INSTITUTIONS IN THE SECTOR ON A SELF-FINANCING BASIS. A STRATEGY FOR FURTHER MOVING THE HOUSING BANK OF PERU (BVP) INTO LOW-COST HOUSING PROJECTS FOR OUR TARGET GROUP SHOULD ALSO BE INCLUDED. THE PP SHOULD FULLY DESCRIBE THE POLICY STUDY TO BE UNDERTAKEN BY THE NEW GOVERNMENT INCLUDING A DRAFT SCOPE OF WORK. AS STATED ABOVE, FUTURE ASSISTANCE IN THE SECTOR WILL BE CONDITIONED UPON THE ADEQUACY OF THE GOP'S POLICY ANALYSIS SHOWING INCREASED GOP RESOURCES ALLOCATED FOR BASIC SERVICES AND LOW-INCOME HOUSING. DURING INTENSIVE REVIEW, THE CURRENT GOVERNMENT SHOULD BE ENCOURAGED BY THE MISSION TO BEGIN TO DEVELOP BACKGROUND INFORMATION AND DATA WHICH WOULD BE USEFUL TO THE NEW GOVERNMENT OFFICIALS IN JULY. THIS INFORMATION COULD ADDRESS SUCH QUESTIONS AS THE EXISTING AND PROJECTED DEFICIT FOR THOSE AT THE POVERTY THRESHOLD LEVEL IN SHELTER AND RELATED INFRASTRUCTURE, FINANCIAL REQUIREMENTS TO OVERCOME THE PROJECTED SHORTFALLS IN THE SECTOR, THE ACTUAL COSTS OF DELIVERING BASIC INFRASTRUCTURE SERVICES BY BOTH THE PUBLIC AND PRIVATE UTILITIES, IMPACT ANALYSIS OF INDIVIDUAL UTILITY COSTS ON OUR TARGET GROUP FAMILIES, AND AN ANALYSIS OF ALTERNATIVES FOR DELIVERING CERTAIN SERVICES, SUCH AS WATER, AT A LOWER COST IN ORDER TO INCREASE COVERAGE (E.G., FREE STANDING COMMUNITY PIPES VERSUS INDIVIDUAL HOME CONNECTIONS).

3. ABSORPTIVE CAPACITY - THE PP SHOULD CLEARLY DEMONSTRATE THAT THE BVP AND THE UTILITY COMPANIES HAVE THE MANAGERIAL AND ADMINISTRATIVE CAPACITY TO EFFECTIVELY UTILIZE THE NEW EG RESOURCES. THIS ISSUE HAS NOT BEEN FULLY EXAMINED IN PREVIOUS PPs OR THE SHELTER ASSESSMENT. WE ARE ESPECIALLY CONCERNED THAT THE UTILITY COMPANIES BE ABLE TO MEET THE INCREASED DEMANDS PLACED ON THEIR STAFFS BY THIS PROJECT.

4. SUB-PROJECT COMPONENTS:

A. SOCIAL INFRASTRUCTURE: THE MISSION MUST DEVELOP A STRONG CASE FOR INCLUSION OF THIS COMPONENT IN THE PROJECT BECAUSE BVP HAS HAD LIMITED PREVIOUS EXPERIENCE WITH THIS TYPE OF LENDING AND BECAUSE OF CONSIDERABLE PROBLEMS IN STAFFING AND MAINTAINING COMMUNITY FACILITIES. AT A MINIMUM THE PP SHOULD DESCRIBE HOW THE CONSTRUCTION COSTS OF THESE FACILITIES WILL BE DISTRIBUTED AMONG COMMUNITY GROUPS, HOW THE OPERATING COSTS OF THESE FACILITIES WILL BE FINANCED, AND THE TYPE OF COORDINATION WHICH WILL BE ESTABLISHED WITH THE SECTOR AGENCIES OR MINISTRIES, BVP, AND THE COMMUNITY ORGANIZATIONS. IN ADDITION, THE BASIS FOR THE BVP'S CHARGING THE 29 PER CENT INTEREST RATE FOR THIS ACTIVITY SHOULD BE EXPLAINED.

B. HOME IMPROVEMENT LENDING: WE ENCOURAGE THE BVP TO UNDERTAKE THIS ACTIVITY IF THE RESULTS FROM THE PILOT PROJECT FINANCED BY EG ARE FAVORABLE. THE PP SHOULD INCLUDE AN EVALUATION OF THE PILOT ACTIVITY AND INDICATE WHETHER THIS COMPONENT SHOULD BE INCLUDED IN THE PROJECT.

UNCLASSIFIED

NNNNVV ESB057BRA669  
PP RUESLM  
DE RUEHC #9215/02 0331422  
ZNR UUUUU ZZ4  
P 021244Z FEB 90  
FM SECSTATE WASHDC  
TO AMEMBASSY LIMA PRIORITY 2302  
BT  
UNCLAS FINAL SECTION OF 02 STATE 029215/02

AIDAC

5. EFFECTIVE DEMAND: THE PP SHOULD DESCRIBE THE DEMAND FOR BASIC INFRASTRUCTURE SERVICES AMONG THE TARGET GROUP AND INCLUDE AN ANALYSIS WHICH ENSURES THAT THESE SERVICES CAN BE AFFORDED BY THE FAMILIES IN THE PUEBLOS JOVENES TARGETED FOR ASSISTANCE UNDER THE HG.

6. GOP FINANCIAL COMMITMENT: IN LIGHT OF THE SUBSTANTIAL HG FINANCING, THE PP SHOULD DESCRIBE HOW A FORMAL COMMITMENT WILL BE OBTAINED FROM THE GOP FOR CONTINUING TO REIMBURSE BVP FOR ITS FOREIGN EXCHANGE LOSSES DUE TO THE PURCHASE OF DOLLARS TO REPAY U.S. INVESTORS.

7. ENVIRONMENTAL ASSESSMENT: LAC/DR ENVIRONMENTAL ADVISOR HAS REVIEWED AND APPROVED PROPOSED SCOPE OF WORK FOR EA SUBMITTED IN REVISED DRAFT OF IEE. VANCE  
BT  
#9215

BEST AVAILABLE COPY

UNCLASSIFIED

SOCIAL SOUNDNESS ANALYSIS

Introduction

The Annex assesses the project's contribution to the Mission's overall urban goal of improving the quality of life of the urban poor through the improved delivery of shelter-related services.

Methodology

The project assessment is based on a study of social needs and services in the pueblos jóvenes of metropolitan Lima which was carried out from mid-October to mid-November of 1979. That investigation included a review of primary and secondary sources of data on the pueblos jóvenes and inner-city tugurios (slums), study of the related activities of the Ministry of Housing and Construction (MOHC), and other relevant government and private institutions, including the BVP, as well as on-site visits to upwards of 35 pueblos jóvenes and tugurios. At least half of the community visits included one-on-one interviews with community leaders and residents.

Summary of Findings

The pueblos jóvenes, or squatter communities which ring Peruvian cities, represent a substantial portion of the country's urban population. The residents of the pueblos jóvenes are the poorest, least educated and most vulnerable segment of the cities, living in communities which offer primitive housing conditions, most of them lacking in one or more basic infrastructure services of electricity, water and waste systems. This contributes to serious health problems and limits possibilities for development, including that of electricity-based cottage industries which might create badly-needed employment and ease the financial crisis of many families in the squatter communities.

While acquisition of housing is a high priority in the pueblos jóvenes, the normal lending rates are beyond their financial means. Under the circumstances, AID's strategy has been to support loans through the BVP and S&Ls for basic infrastructure and home improvement projects in the pueblos jóvenes and similar low-income communities.

The pueblos jóvenes are organized into neighborhood councils, which originally received considerable support and technical assistance from SINAMOS. Many councils were instrumental in helping their communities to negotiate loans for basic services in the past and have experience in working with credit institutions. The councils still exist and continue to function, and will have a key role in negotiating sub-projects under the new loan. While many neighborhood councils work effectively, others show need for technical assistance in problem-solving and consensus-building skills required to participate in designing and implementing loan projects. There is promise of such assistance from a new promotion/technical unit of the BVP.

The program under analysis fills a void in credit resources for improvement of low income urban communities and uses a lending institution which has had long and successful experience in working with these communities. Implementation of sub-projects will have a positive impact on the health and general quality of life of the participating communities, with the possibility of important secondary effects of employment generation, reduction in cost of infrastructure and home improvement projects, increased coordination among public institutions which work with the urban poor, and an integrated approach to development of the pueblos juvenes.

### I. The Social Landscape

The pueblos juvenes are one of the most pervasive features of urban Peru. They are generally one of the first sights the visitor encounters approaching Peruvian cities. Located on the urban fringes, the settlements are usually unordered groupings of reed-mat or mud and wattle huts put up on unpaved dirt areas, lacking any basic infrastructure. As one moves closer to the urban center, these give way to more orderly but still rudimentary communities, mixtures of reed-mat huts and more solid construction, some of it only partially raised, with one or more of the basic amenities, some pueblos juvenes closest to the urban shell are almost indistinguishable from their neighboring communities within the formal city limits.

#### Demography

The squatter settlements are the result of more than forty years of increasing rural to urban migration in Peru, the pattern flowing from rural communities to small urban centers to larger cities and finally to Lima, which has become figuratively and literally the capital city of the nation. More than half of Peru's urban population lives in Lima, over 75% of that in the pueblos juvenes and inner-city tugurios. The pattern and percentages are similar in other major urban areas. The greatest impetus for the movement toward the urban centers is unquestionably economic opportunity, availability of education and health facilities, access to centralized government services (although the government is attempting to decentralize its operations), and the less tangible but still important factor of status which the cities, especially Lima, confer on those who have migrated from the hinterlands. Statistics alone make a stunning case for the economic motivation of the emigrants. The average per capita real expenditures of a person in the eighth decile of the rural highlands is below that of the average resident of Lima in the third decile (within the bottom 30%).<sup>1/</sup> Demographic projections indicate that at current fertility rates Peru's population will double by the end of the century. While there are development plans to relieve the economic stagnation of the rural sierra regions of Peru their hoped-for impact on migration to the cities cannot be expected for many years. The increasing growth in rural births will continue to swell the population of Peru's urban squatter settlements, through migration, for the foreseeable future.

---

<sup>1/</sup> Draft Paper, Peru: A Shelter Strategy (FY 80 - 84), AID/UDD/Lima, 5/9/79, Revision I, 12/12/79

### Employment

Those who come to the cities from the rural areas begin at the bottom of the socio-economic scale, although their relative position may be an improvement over their former condition. The emigrants arrive with poor education and few marketable skills which would permit them a successful economic transition to the urban environment. Only 48% of the rural population is literate; 67% of rural women and 42% of rural men are illiterate.<sup>1/</sup> The quality of rural education, when it is available, is often poor and rarely offers more than primary schooling. The severe economic recession which has afflicted Peru since 1977 has sharply reduced employment opportunities in areas of work which might normally be job entry points for rural emigrants to the cities. As a result, urban unemployment and under-employment are high, with particular impact on those with few skills or experience.

Employment opportunities open to job-seekers in the squatter settlements fall into such low-paying, low-skill jobs as street-vending and service work, the latter predominantly in domestic employment. A survey of 11 pueblos juvenes and similar low-income communities conducted by the Mutual Metropolitana of Lima in 1978 indicated that only 48.6% of workers had stable incomes. At the same time, inflation has eaten into real incomes, hitting hardest at those in the lower socio-economic strata. A study conducted by the Compañía Peruana de Investigaciones de Mercade in June 1978 indicated that the loss in real income for the average low-income Lima household from December 1975 to December 1978 was 29.5%. A low-income family had to spend 67.4% of its earnings on food, at then current prices, and a very low-income family spent up to 74.3% on food.<sup>2/</sup>

### Housing

Housing needs in the pueblos juvenes far outstrip the ability of the residents to obtain adequate shelter. The impact of inflation and high interest rates has brought home construction to a virtual standstill, exacerbating the housing shortage. The impact in the pueblos juvenes is particularly acute. The sizeable proportion of the population which lives in huts made of reed mats (esteras) or in partially built homes of more solid material, usually brick, have had to postpone acquiring more adequate shelter. Some housing construction is taking place in the squatter communities, although there is a question as to how it is being financed. There is no question that residents of the pueblos juvenes place a high priority on the acquisition of their own homes, and are prepared to make considerable sacrifices to obtain them. Status is probably as much involved as the need for shelter, as evidenced by their use of expensive material noble such as brick, over less costly but serviceable alternatives.

---

<sup>1/</sup> AID:PERU. CDSS. FY '82. January 1980

<sup>2/</sup> AID:PERU. Research on Malnutrition...A Quantitative Study on the Recent Situation in Lima. Mission Memorandum A-19, May 7, 1979.

The urban strategy of AID in Peru focuses on providing credit on terms which the target communities can afford in order to secure basic services. Their absence contributes to serious health and security problems, as well as increasing financial burdens. As installation projects are delayed, their costs rise, taking them still further from the reach of the target population, presenting the prospect of greater strain on their already fragile economic resources when the projects are finally begun.

It is difficult to generalize about pueblos jóvenes. Within each community there is a great disparity of social and economic situations, manifested by the diversity in the types and condition of shelter to be found within their confines. Family incomes vary sharply, and while community income averages can indicate something about the general affordability of projects, such figures do not take into account the real difficulty a proposed project may pose for individual families within that community. While the record shows that there have been relatively few defaults on infrastructure payments from low-income communities, the variance and instability in family incomes within the pueblos jóvenes should be taken into account in the design and financing of projects.

#### Health

Given the high incidence of unemployment, underemployment, poor housing, lack of basic infrastructure, and the disproportionate percentage of family income which must be spent on food, it is not surprising that serious health problems rank high on the list of descriptions of the squatter communities. Studies indicate that up to 26.1% of low-income families in metropolitan Lima suffered from severe nutritional inadequacy in 1979.<sup>1/</sup> The impact of these figures can be seen in related statistics of the Children's Hospital of Lima, where more than 69% of children admitted in 1976 were malnourished, with 29% of infants under one year of age showing symptoms of third-degree, or extreme malnutrition.<sup>2/</sup> Those figures are undoubtedly higher today in light of the considerably worsened economic situation since the data were taken. Medicines are almost totally outside the reach of the target population, having risen an aggregate of 366% between 1972 - 1976. While health posts sponsored by the Ministry of Health, some private voluntary organizations and some built by the communities themselves do exist, they do not begin to cover the need. Many remain empty shells, since neither the government nor other sponsors have the budget for personnel, equipment, and medicines to operate them.

The environment of many pueblos jóvenes themselves constitute health hazards. Garbage collection in the pueblos jóvenes is sporadic, and mounds of garbage, some of it burning, are a common sight in many of the low-income communities.

---

1/ See Research on Malnutrition..., op. cit.

2/ Instituto Nacional de Estadística (INE) del Peru, El Niño en el Peru, Lima, 1979.

### Education and Child Care

Public education facilities in the low-income communities do exist, but they are limited, and again, are not adequate to the need. Private programs, such as the schools of Fe y Alegria, a church-sponsored program, must supplement public resources. Pre-school and child care facilities are scarce, in spite of the efforts of public and private resources in this area. Figures show that in 1977, 1,970 infants were cared for in nurseries in metropolitan Lima. A 1979 study indicated that in 1975 only 5.5% of children eligible for the services were enrolled in pre-school centers in Peru.<sup>1/</sup>

### Women

The role and situation of women in the pueblos jovenes is an area in which few studies have been made. Much more needs to be known about their numbers, marital status, roles as mothers, heads of households, economic providers, as well as socio-political roles with the communities, their attitudes and needs. Informal observation and interviews, as well as such data as exist, indicate that in the move from the rural environment to the cities some factors in the women's lives remain constant, but other change, sometimes radically.

In the rural setting women have an important role in almost all phases of agricultural production and marketing, as well as the traditional responsibilities of child-rearing, housekeeping, sewing, cooking and tending to domestic animals such as cuyes (guinea pigs), which are sources of food. In Peru, rich in artisan talents, rural women also play an important economic role in producing handwork ranging from knitted alpaca sweaters and ponchos to woven rugs, baskets, ceramics, etc., in addition to making dairy products such as cheeses and manjar blanco, a milk-based sweet dessert. These are all important sources of family income in which the women not only engage in production, but sell the items in the regional markets. Few rural women, however, have formal jobs outside of the domestic setting. While schools are nominally open to boys and girls, few rural women complete their primary education. Literacy rates for rural women are considerably lower than those of rural men.

When these women come to the cities they are ill-prepared for the challenges of urban life. While many of their family responsibilities remain the same (child rearing, housekeeping, cooking), they are cut off from many other areas of their former lives which gave them standing in the family and some support. Their contribution to agricultural and commercial activities, extended family relationships which provided child-care services when needed, and age-old traditions which guided and buttressed their roles, attitudes and activities all change. Natural resources which contribute to housekeeping and economic support in rural areas are not available in urban areas. There is little data on the raising of domestic animals in

---

<sup>1/</sup> Overseas Education Fund of the League of Women Voters. Child Care Needs in Urban and Rural Peru. Washington, D.C., Aug. 1979.

the pueblos juvenes, although some of this does take place on a limited scale. There appear to be few cottage industries in the urban communities which might give women opportunities to supplement family income. Women's activities in one sense are therefore much more circumscribed to housekeeping and child rearing in the cities. On the other hand, economic realities have forced more and more women, particularly in the lower socio-economic strata, to seek employment outside of the home. Their poor educational background and almost total lack of vocational preparation, leave them few employment alternatives other than street-vending and domestic service, both low-paying and unstable occupations. Child care is becoming an increasingly important problem for these women. Little data is available on women heads of households in the urban barrios and slums, but all indications are that the phenomenon is much more prevalent in the cities than in the rural areas, and certainly more so than official notice would indicate. Since this has important implications for urban project development, data collection on this issue should be a priority component in social planning for Peruvian cities.

## II. Organizational Context

The pueblos juvenes of Peru are unique in that the Peruvian government has institutionalized what in many other developing countries are allowed to remain simply as chaotic by-products of the development process. Originally termed barriadas, the shanty-towns which began to spring up around Peruvian cities in the 1930's-40's, and continued with increasing rate and density, were later baptized as pueblos juvenes, or "young towns" by the Velasco administration in 1968, as part of a politically motivated effort to change the negative image of the barriadas and to gain their support for the reforms and socio-economic changes planned by the revolutionary government. In order to channel and mobilize that support the government created SINAMOS (Sistema Nacional de Apoyo a la Mobilizacion Social), a movement to create cadres at the grass-roots level to implement the proposed social and economic reforms. One of SINAMOS' principal responsibilities was to promote and control community organization in the politically volatile squatter communities. It offered the communities legal status as special proteges of the government under Decree Law 13517, which officially recognized all pueblos juvenes organized prior to 1960, and promised the residents eventual title to the lands they had invaded in return for their support of the government.

SINAMOS, through its ample staff of "promotores sociales," organized the pueblos juvenes along pyramidal lines which still constitute the basic organizational pattern of these communities. Each community block elected representatives to a comite vecinal, or neighborhood committee. This committee, consisting of a coordinator, treasurer, secretary and, optionally, a sports or recreation coordinator, women's committee representative, etc., in turn sent its coordinator to represent it on a central committee of the pueblo joven, or COPRODE (Comite Pro Desarrollo), which elected an executive committee, or junta directiva from among its members. The president of the executive committee was also the community's representative to a zonal association of pueblos juvenes, and this association was represented at a city-wide association of the communities.

The social promoters gave this structure considerable technical assistance in organizational techniques and leadership development, which enabled the communities, with SINAMOS frequently playing an ombudsman role, to gain access to the central government for assistance or solution of problems to a degree they had never known before. SINAMOS' backing was particularly helpful in moving many communities through the frequently tortuous remodeling-entitlement process which had been established to formalize the situation of the families living on invaded land, and to help the communities to obtain basic infrastructure.

Not all communities received the full range of SINAMOS' attention, since even SINAMOS' ample budget had its limitations; but at the minimum all communities recognized as pueblos jovenes under D.L. 13517 were organized along the lines described. It is important to note that D.L. 13517 only officially recognized squatter communities established prior to 1960. Many more came into being after that date and continue to do so. Their legal standing is in limbo, although in practice most of them are organized in the same way and receive some assistance from the MOHC, which took over many of the functions of SINAMOS when it was de-activated in 1978.

Those communities which received concentrated technical assistance from SINAMOS have maintained their cohesion and the advantages are apparent in the degree to which they have been able to move ahead in obtaining infrastructure, building permanent shelter, developing green areas and other community facilities. The MOHC, as a matter of policy as well as budgetary restrictions, provides only limited technical assistance to the pueblos jovenes, and this is focused on moving them through remodeling-entitlement. The MOHC's current resources cannot adequately meet the need for assistance even on this level.

As a result, many community organizations are experiencing varied degrees of disintegration, lack of confidence in their leadership, lack of member participation in meetings and community affairs, and inter-personal, intra-community dissension. This tends to weaken the effectiveness of community decision-making on important issues such as infrastructure projects and other joint community activities. Frustration and narrow interests sometime prevail and costly mistakes are made. Two instances illustrate this point. In one case a community was divided over the issue of whether to install both water and a sewerage system. One group wished to go ahead with the project, another group balked at the cost. Community leadership was not able to resolve the issue. As the debate went on for many months, costs rose, to the dismay of the group which wanted to go ahead with the project. Finally it decided to move on its own, and had the infrastructure installed for the half of the community it represented, leaving the other half without these services. At last report the situation had not changed, and the community's social fabric had been torn apart in terms of pulling together in the future resolution of other community needs. A second instance, in another smaller community, saw a similar controversy arise over the issue of electricity, with the same results.

It is important to note these examples in light of the proposed loan's assumption that neighborhood councils will have an important role in project development. They will be expected to help the communities discuss and reach

consensus on priorities for basic services and facilities, participate in project design, agree on costs, make decisions on saving for down payments as well as contributing labor to reduce the cost of these projects. In order to achieve the objective of meeting the needs of low-income urban communities, the proposed loan should factor in provisions for technical assistance to the communities involved.

In this regard, the projected creation of a technical/promotional unit within the BVP, which will use an outreach program staffed by "promoters" to assist communities in obtaining credit and using it more effectively, should be a useful development. It will be important for the BVP to staff this unit with persons who combine experience in working with low-income clients, knowledge of the community structure and problems of the pueblos jóvenes, and group and human relations skills. The work of this unit could be strengthened and its impact made broader through coordination with the local units of the MOHC responsible for technical assistance to the pueblos jóvenes. These functions reside principally in the Technical Units and Neighborhood Organization Units at the sub-region and zonal levels. The proposed loan program will succeed to the extent that client groups are prepared through effective technical assistance and are made to feel that the lending institution understands their situation and is sympathetic to their needs.

### III. Institutional Interface

The BVP has had considerable experience in dealing directly with low-income communities. Since 1969 the BVP has been instrumental in financing low-cost and self-help shelter as well as basic infrastructure programs benefitting a significant number of low-income urban communities in Peru. The BVP has shown sensitivity to the special requirements of the target group in its proposed creation of a new department to work with the low-income communities and their representatives in preparing sub-projects, and presumably in giving them further technical assistance as needed during project implementation. The creation of such a department may open the door to a variety of expanded roles for the BVP in the pueblos jóvenes and other low-income communities, not unlike the role of the Instituto de Crédito in Colombia, which has responsibility not only for housing and housing related credit programs but also for many community organization and development activities to improve the general quality of life in these communities. The possibility of financing facilities such as schools, health posts, markets, etc. in low-income communities, provides another interesting avenue by which the Bank might expand its contribution to the development of the pueblos jóvenes.

The utility concessionaires involved with the projects (ESAL, ESAR, Electro-Lima and Electro-Peru) have had considerable experience in working with the BVP, with low-income communities, and with private contractors in similar projects. There has, however, been a feeling expressed by some representatives of the pueblos jóvenes that the utility companies have not always been sensitive to their needs. It will be important for the representatives of thy companies, as well as those of the BVP and private contractors,

to establish a climate of mutual trust in negotiations with the communities, and to make certain that the terms and procedures of the proposed sub-projects are clearly understood during both the design and the implementation phases.

#### IV. Motivation

If past performance is indicative, there will be considerable interest on the part of individual families and communities who do not as yet have basic infrastructure to take advantage of the terms to be offered by the BVP for sub-projects. A significant number of urban homes are still without basic services, and loans of this type hold the only reasonable hope that residents of the pueblos jovenes and other low-income communities have to acquire them. Apart from the easily perceived benefits of electricity, water, and sewerage facilities, the installation of these facilities brings significant savings in expenditures for water bought from trucks, for candles, and for other sources of illumination, all of which cost considerably more than the installed services.

The likelihood that the target community will take advantage of the program is increased further by the prospect of promotion and technical assistance planned by the BVP. Those who may be expected not to participate are families and communities categorized as the very poor--those who must spend up to 74% of their income on food. Families in the next highest category, those who earn approximately S/.30,000 per month, may also find it difficult to meet the financial demands of loans, but evidence shows that many families in this bracket are prepared to make considerable sacrifices to acquire shelter and basic services.

#### VII. Obstacles

While the proposed loan follows in the steps of previous similar programs, several of which are still being implemented, it is nonetheless important to recapitulate here several areas of possible limitation to attaining the objectives of the current HG program, together with suggested approaches for mitigating their impact.

1. Disparities in income, particularly in a period of severe recession such as Peru is currently experiencing, may create problems in given communities in being able to agree on projects, leading to costly delays or even indefinite postponement of such projects, as has occurred in the past. These situations will require consideration of innovative solutions, such as modification of traditional designs for installation of services which would bring their costs to a more widely attainable level, creative financing arrangements, etc. Devising such solutions will require maximum use of the talents of the BVP's proposed promotional/technical teams as well as those of the utility concessionaires and the private contractors.

2. Much of the anticipated success of the current loan program is predicted on the effective functioning and participation of community councils. While many existing councils were formed under the tutelage of SINAMOS and continue to function well, others do not function as well for a variety of reasons, including less technical assistance from the Ministry of Housing, community factionalism, and the host of other problems which can afflict any organization, such as interpersonal friction, rivalries, poor leadership and problem-solving skills, replacement of individuals on committees, etc. With the de-activation of SINAMOS and the considerably restricted resources of the MOHC, a technical assistance vacuum exists, and the committees are largely left to shift for themselves. Given their central role in the loan program, it will be of particular importance to fill the vacuum. Coordination between the BVP and the relevant units of the MOHC is again stressed as a means of increasing the impact of technical assistance to the community organization. Such coordination can establish a useful precedent for wider coordination of activities between these institutions, both of which are essential to urban shelter development.

3. The project description includes the possibility of the BVP making part of the loan funds available for building schools, health posts, markets, etc. While such facilities are unquestionably needed, as some of the earlier cited statistics demonstrate, residents of the pueblos jovenes will place higher priority for use of their scarce funds on acquiring infrastructure. The concerned ministries should be brought into the planning process. This would have the advantage of promoting coordination with their ongoing and planned programs, as well as an integrated approach to development of the low-income urban communities.

4. Social and economic conditions in low-income communities outside of Lima vary considerably from those of the capital city. Income levels are lower. While the BVP has worked with such communities in the past, using comparable lending rates, it would be important to evaluate these experiences in the light of current economic conditions.

5. The level of sophistication and effectiveness of community organizations in cities outside of Lima similarly can be expected to be more limited, requiring particular sensitivity and skills on the part of Bank officials and others who will work with them in order to avoid problems due to breakdowns in the decision-making process, misunderstandings on design plans, terms of loan contracts, suspicion due to class differences, etc. Here again, previous experience of the BVP, utilities, and contractors should be evaluated in order to ensure the effectiveness of procedures under the new loan program.

#### VIII. Communication Strategies

In order for benefits to reach the desired target groups, information on the program must be made available to them. This will require an effort on the part of the BVP, using diverse channels of communication most likely to reach those living in the pueblos jovenes and similar communities. In this

regard, the technical assistance and community organization units of the Ministry of Housing could play a useful role in making known the availability of these loan funds and in helping to identify communities which could most appropriately apply for them. This represents another area for BVP-MOHC coordination to further mutual objectives.

IX. Spread Effects

There will be several important spread effects emanating from this loan program.

1. This loan supports the BVP's effort to develop and implement a new outreach promotion and technical assistance unit within its organizational structure, whose services will extend beyond the time and client boundaries of this program in benefit of a significantly wider segment of the urban poor.

2. The program provides opportunities for greater collaboration between relevant units of the BVP and the MOHC, which will result in improved service to the target population by both institutions.

3. While it is not yet clear what procedures will be used under this loan for financing community facilities such as schools, health posts, and markets in the pueblos jovenes, it is apparent that it will require and stimulate communities interested in acquiring these facilities to increased organizational activities to deal with the issues involved. The larger benefits accruing from such experiences, if they are supported by technical assistance as needed, are to increase community cohesion, sharpen group problem-solving skills, and to enable the communities to move into broader areas of community development.

4. The project offers further opportunities for the utilities, private contractors, and builders to accumulate experience in working with low-income populations, which should provide a good base for continuing to work with these groups outside of AID-sponsored programs.

5. The implementation of studies and the development of demonstration projects to increase the self-help component in community upgrading should promote use of the techniques developed in a wide range of other programs and thus benefit a far greater population than that contemplated under the proposed loan.

6. Implementation of the component of the loan program designed to provide health, education and other supplementary community facilities to the pueblos jovenes will strengthen needed collaboration and integrated planning between the communities and public institutions as well as among the institutions themselves.

7. Installation of electricity in the pueblos jovenes will provide opportunities for development of cottage industries and small businesses dependent on this resource.

## X. Social Consequences and Benefit Incidence

### 1. Beneficiaries of the loan program

Those most immediately benefitting from this program will be the individual families which participate in loan projects. The most tangible benefits will be in improved health, decreased costs for water and electricity, and increased security, often mentioned as a prime concern where electricity for illumination is lacking. The communities themselves will benefit from the upgrading of the general quality of life which accrues from availability of these basic facilities, as well as from an improvement in self-image which can act as a strong psychological stimulus to actively seek further improvements on an individual and community level. The communities will further benefit from strengthening of their organizational capabilities and indirectly from increased coordination among public and private institutions which may result as different components of the program are implemented, particularly those concerned with health, education, employment and reduction of construction costs.

Contractors, laborers and others involved in diverse segments of the construction industry will also reap economic benefits. A large percentage of the laborers employed in construction projects live in pueblos jovenes and similar communities.

Women will also experience a number of direct and indirect benefits. Women and girls will enjoy the benefits of installed basic infrastructure. Individual water connections and electricity will make the task of house-keeping considerably easier, and improved health will have positive impact for women as individuals and in their role as family nurse. Increased organizational activities in the community around various aspects of the sub-projects may provide new outlets, roles and status for women as they have opportunities to participate in planning for community development, particularly those activities related to health, education and child-care facilities. The potential is there and should be encouraged by those promoting these projects. Women could benefit economically through employment on various levels in health posts, schools and child care centers, as well as in community-based industries which may develop directly or indirectly as a result of the loan program.

### 1. Non-Beneficiaries

The poorest of the pueblos jovenes and other low-income communities whose income level puts them below the range of any credit program will not benefit directly from the current loan. The program does not positively impact the poorest of the poor except as it provides employment for construction laborers.

## XI. Changes in Power and Participation

The loan program stresses participation of neighborhood councils in the design and development of projects and makes technical assistance available to these councils to ensure that their participation is effective. The

important involvement in activities which will have considerable impact on their lives and on their communities should enhance the ability of the neighborhood councils to deal with public and private institutions in the future, giving the communities greater control over their development.

INITIAL ENVIRONMENTAL EXAMINATION

ENVIRONMENTAL THRESHOLD RECOMMENDATION

Project:	Peru 527-HG-011	
Project Title:	Upgrading Low-Income Settlements	
Funding:	HC:	US\$ 20.000 million
	Perú (BVP)	2.223
	Down Payments	<u>1.171</u>
Total:	US\$ 23.394 million	

IEE Prepared by: Peter A. Weber, Environmental Planner  
National Savings and Loan League  
for DS/Housing  
December 1979

ENVIRONMENTAL ACTION RECOMMENDED:

Based upon the findings of the IEE, a Positive Threshold Determination is recommended for Peru 527-HG-011. The specific environmental issues warranting further detailed investigation, and for which appropriate project design responses shall be prepared in the Project Paper, are outlined in the IEE.

Office of Housing: \_\_\_\_\_ Date: \_\_\_\_\_  
David McVoy  
Assistant Director for Operations

PERU HG-011

INITIAL ENVIRONMENTAL EXAMINATION

I. BACKGROUND INFORMATION

A. BASELINE ENVIRONMENTAL CONDITIONS

1. Natural Environment

Perú is a tropical country, located as it is between the Equator and 18° South Latitude. Despite the geographic location, the country has practically every type of climate, because of towering mountains, temperate valleys, cold ocean currents, and extreme desert habitats. For further information on the natural environment, the reader is referred to the IEE for Perú HG-010 (1979).

2. Human Environment

a. National Land Use and Urbanization

Perú has a harsh, demanding environment for most of its extent. As an indication of its inhospitality for human land use, less than 2% of the total land area was under cultivation in 1970 (Weil et al, p. 271). In addition, 21% of the country was in pasture land. At that time, fully two-thirds of the nation was in forest land. Rugged mountain ranges comprised the remaining 9% of Perú.

Human settlement patterns predominate in the mountain valleys and in the coastal desert; the jungle and the high mountains are not appreciably populated. The challenges offered by Perú's human environment stem from increased population growth rates, longer life expectancy from improved medical care, and the accelerating urbanization of the national population. In national terms, the population increased from 6.2 million in 1940 to 14.2 million in 1972 (Draft SSA, Annex 2). During that same period, the urban portion went from 35% to 61%. In 1970, the PID estimated that 75% of Lima's inhabitants resided in "pueblos jóvenes" and inner city slums (p. 1). As another example, Chiclayo had 60% of its population in low-income neighborhoods. The pattern is repeated to a greater or lesser degree throughout the country. It is this socio-economic group which has been the major factor in the urban surge.

b. Metropolitan Lima

The Peruvian capital has a higher population than double the sum of the next twelve cities. According to AID's SSA (Annex 5), the city is projected to contain 4.8 million people in 1980. Since the city is overwhelmingly inhabited by very poor people (75% of the total) and has grown so rapidly (from 630,000 people in 1940), there is a resulting lack of urban planning. Spontaneous, haphazard, inefficient growth has occurred, to the detriment of all concerned. One of the major shortfalls is in urban infrastructure, especially potable water and sewerage.

c. Secondary and Tertiary Urban Centers Throughout Perú

Most of the other major cities, besides Lima, are situated on the Pacific coast, in a comparable desert environment. In-migration from rural sierra areas has been the prime stimulus to their rapid growth. There are several smaller cities in the Andes, and a couple of river ports in the Amazonian region.

3. DESCRIPTION OF THE PROPOSED PROGRAM

1. Program Characterization

The proposed program would consist of a \$20 million HG loan, "to finance primarily water, sewerage, and electricity services in pueblos jóvenes and similar communities" (Draft PID, p. 4). Also potentially part of the program would be loans for home improvements in the same areas. The beneficiaries are to come from the lower half of the urban population. They are living in peripheral areas of each urban concentration. The program would not involve upgrading of inner-city tugurios (slums). Potential sites occur in all of the major cities of the country.

2. Institutional Organizations and Capabilities

For further information, the reader is referred to the PID and the FY 1979 IEE.

3. Environmental Planning Capability

There is no long-term well-developed national environmental policy. Urban environmental planning, as such, is not receiving major attention. Per se, there is no official environmental planning input into EVP's technical office. Rather, engineering practices, insofar as they touch upon the environmental ethos, are the standard operating procedures of EVP. Baseline data sources are presented in the 1979 IEE.

## II. EXAMINATION OF POTENTIAL ENVIRONMENTAL EFFECTS OF THE PROPOSED HG PROGRAM

### A. SUMMARY OF MAJOR CONCERNS

In an upgrading program, the major negative impacts should not be caused by that program itself but rather should be produced by the impact of the natural environment on the human environment. The history of Perú indicates that natural processes/disasters have caused much loss of life and destruction of man's works. In fact, the rate and amount of urbanization in the last several decades has been greatly augmented by earthquakes, landslides and floods, which displace great numbers of people. Once the people gather in ever increasing urban concentrations, the second phase of environmental impact begins. In this phase, the carrying capacity of the environment (to produce supplies of potable water, for example), is significantly strained.

The following are the major environmental concerns which need to be addressed in project development. Given the variety of Peruvian environmental conditions, not every concern is found at each site. These concerns, and proposed solutions to the difficulties they represent, will be discussed further under part B of this section.

- Potable water supply and distribution
- Sewage collection, treatment and disposal
- Earthquakes/landslides/tidal waves
- Moving sand dunes
- Flooding.

### B. DISCUSSION OF KEY ENVIRONMENTAL ISSUES TO BE CONSIDERED IN PROJECT PAPER

#### 1. Water Supply and Quality

As mentioned earlier, the Peruvian coast is a desert. But it is a heavily-populated desert. Five of the six largest cities of the country are located in this region, including Lima, the capital. Water supply is a particular concern in coastal cities. Ground water extraction is depleting coastal resources; water from the Andean streams is costly to obtain.

In order better to understand the urban water supply issue, Lima shall provide the main example. First, Lima's water supply in 1978 came from three sources. The Atarjea treatment plant of the Río Rimac provided 11.3 m<sup>3</sup>/second; wells throughout the metropolitan region provided 5.0 m<sup>3</sup>/second; and percolation galleries (galerías filtrantes) provided 2.7 m<sup>3</sup>/second, capturing sub-surface river flow even during the dry season. Second, ESAL estimates that demand has exceeded supply at the present time, so that average consumption has had to be reduced, particularly in the pueblos jóvenes. An indication of an associated problem was given by the Ministry of Agriculture in 1970, as quoted by ESAL, to the effect that the Lima water table was dropping by two meters a year because of the heavy water extraction. ESAL, recognizing this constraint, is trying to phase out its system of wells.

Water supply for the pueblos jóvenes is even more precarious than that for the city in general. At the present time, the majority of the pueblos jóvenes are outside the ISAL piped water system. In fact, the latest growth of these settlements is occurring in increasingly marginal land away from any river and higher up in the dry hills. Extension of existing lines would be difficult. No gravity-propelled water system is possible at this time. Thus pumping is required from surface storage sources. But surface water sources have fallen behind demand. A system of wells may thus prove to be the only feasible short-term way to serve these people. And there is no assurance yet that well water is available for all these areas.

The strategies of Lima to augment its water supply are worth noting both for themselves and as an indication of what coastal cities must do in order to get water. First, the main reservoir and treatment plant for Lima (Atarjea) is currently planned to be greatly expanded by means of a second reservoir and treatment plant system (expected to be functioning in 1982). Then, by 1986, the capture of the Rio Mantaro watershed (which drains to the Atlantic) is to be accomplished by a trans-Andean tunnel. Another 5 m<sup>3</sup>/second would be added to Lima's supply. Also planned are two reservoirs upstream from Atarjea, one at Otosica to serve (by new lines) the Canto Grande/La Molina area, and the other further down the river to serve the Omas Pueblo joven area by a ridge-crossing water line of 5 m<sup>3</sup>/second capacity.

Trujillo is faced with a situation in which its supply of water, through a network of wells, is increasingly inadequate. Stressed by high population growth (for which not enough wells exist) and a major earthquake in 1970 (during which a number of existing wells were put out of action, up to the present time, by earth movements which broke the tubing and filled in wells with sand and rock), the city is struggling to obtain water. In addition, it lacks a system of reservoirs throughout the system, so that pressure to distribute the water is low or non-existent.

Water quality is also generally a concern, both by contamination by human activity (sewage and garbage pathogens leaching into ground water reserves and into broken or leaky water pipes; mine spoils dumped into several of the sierra streams which contribute to potable water supply systems) and by natural phenomena (salt water intrusion into "sweet" water supplies along coastal areas when ground water is over-extracted, thus sucking salt water into the aquifers).

## 2. Sewage Collection, Treatment and Disposal:

Sewerage services for the cities of the country basically involve collection by sewer lines and treatment disposal in one step by discharging into the nearest natural body of water. In the pueblos jóvenes, this basic system has not existed. The proposed program would extend collector sewer lines to these communities. Still to be resolved would be the joint issues of treatment and disposal. And in some

cities, it may not be simple to extend existing sewer lines to the pueblos jóvenes.

An example of the recurring contemporary complex situation in sewerage systems is found in Trujillo, one of the bigger cities of the country. Trujillo has an old sewerage system, developed when the town was much smaller, which is now losing capacity since it is becoming overloaded and is becoming worn out. The town's system has been disrupted by earthquakes, which shift the earth and break the sewer lines. Therefore, the system has multiple problems: obsolete capacity in some of the lines, deteriorating lines, and periodic massive disruptions (earthquakes) to the entire system. With these points in mind, it is important to realize that there may be difficulties in tying in sewerage from the pueblos jóvenes to the municipal system. Also, the city does not provide for treatment of the raw sewage. Instead there are outfalls into the Pacific Ocean, close to the population. In these ways there are health and ecological hazards from off-site disposal of the wastes. The AID program should strive to minimize these hazards while it attempts to maximize the upgrading benefits.

In order to design the sewerage component of the program, detailed existing system capacity should be determined. The limits to additional sewage flow will shape the timing and scale of sewerage upgrading. In addition, opportunities present themselves concerning alternative sanitary systems. An existing AID project in Tacna is using oxidation lagoons for sewage treatment. The Ministry of Health's "Proyecto San Juan -CC," successful since 1967, has shown the way for alternative methods of sewage disposal besides outfalls in bodies of water. In the Ministry's project, lagoons 1.5 meters deep were excavated and raw sewage filled the lagoons. By means of natural oxidation, phytoplankton converted the sewage into more plants, non-toxic residues and purified water. The plants in essence cleaned the water, which then could be used for agriculture and forestry purposes. So instead of losing sewage into rivers and the ocean (and polluting them at the same time as leading to public health hazards), an economical natural process can convert waste into a useful product. Given the awesome need for expanding agriculture, particularly in the desert where most of the cities are located, this system of oxidation lagoons should be intensively evaluated for its applicability in the present program. Besides agricultural benefits, the effluent could be utilized to nourish the dune-stabilizing trees, shrubs and grasses. This process would help prevent the onslaught of shifting sands on houses, roads and other important components of the communities. These vegetation belts could also shelter cities from winds and help abate the severe problem of particulate matter in the air. With the pueblos jóvenes frequently located on the desert fringe, land should be available for this type of sewage treatment. In conjunction with oxidation lagoons, methods such as land application and community septic tanks should also be considered.

The proposed urban services program should diminish health hazards which are created from lack of potable water and sewerage facilities. Diarrheal and respiratory ailments should be reduced because

of this upgrading program. Mortality rates, especially of children up to age five, should fall.

### 3. Seismic Phenomena

Within the period from 1904 to 1968, there were twelve earthquakes with a force on the Richter seismic scale greater than 7.5, scattered throughout the nation (unpublished data from Instituto Geofísico). On May 30, 1970, another earthquake struck Perú with a force of 7.7 on the scale. An estimated 50,000 people perished. There is thus no doubt that the frequencies and intensities of earthquakes are high in Perú. At present, there is no sure method of predicting occurrence, location or intensity of seismic upheavals. At any time, apparently, the coastal and sierra parts of the country can be struck. Epicenters (surface location over the center of the internally-generated earthquake) have occurred throughout the length of the country (Benavides, map, p. 102). Lima was destroyed in "great part" in 1573 and 1586; "total destruction" occurred in 1687 (two earthquakes on the same day) and in 1746. A lapse of years or centuries does not erase the chance of violent earthquakes happening anywhere throughout the seismic zone.

Besides earthquakes, the related phenomena of tidal waves (or tsunamis) on the coast and avalanches in the mountains (of snow, ice, mud, rock) have caused much loss of life and extensive damage to property.

Special seismic planning is required. First, a proper site location needs to be selected. Those housing developments with evidently poor location should not be serviced; rather the housing should be relocated as soon as possible, given the nature of the environmental problem, instead of creating the possibility of a natural disaster by keeping the housing in a poor location. Although an entire region may be susceptible to damage, there should be micro-geological differences which permit a minimization of dangers. With detailed geological knowledge, including reading the landscape for past seismic activities, obvious mistakes can be avoided. The site should be away from any known active fault zones, away from landslide areas and out of reach of known maximum tidal wave height. Second, proper selection of materials (reinforced concrete materials) and proper design (for stress resistance) should be used. Third, site layout should facilitate an "absorption" of impact, such as streets with proper width to absorb partial or complete damage of housing units without cumulative "domino" effects.

### 4. Moving Sand Dunes/Wind Winds

Along the coast, such as in Piura, Chiclayo and Ica, a lack of precipitation, the presence of sand dunes, and the rising of a wind can cause a hazardous situation. In the south, around Ica, violent winds called the "garraza" are common in the month of August (Benavides, p. 32). In the north, Chiclayo and Piura are noted in regions where dunes (sometimes in clusters called garrazas) advance on the land.

Roads and housing and other structures are susceptible to being covered. Proper design features to mitigate these problems include: 1) correct site location, away from the path of prevailing sand motion and away from direct impact from winds, if at all possible; 2) planting of shrubs and trees in lines to break the force of the wind and stop the free movement of sand; and 3) appropriate site layout of streets and orientation of buildings, and so forth, in order to create barriers to moving sand and high winds.

#### 5. Flood Protection and Storm Water Drainage

The jungle, especially a place like Iquitos (which is on the Amazon), is a region with a surplus of water, in its manifestations as precipitation, as a river and as water on the land. Special difficulties are presented by heavy rains, flooding and a high water table. Design of projects should endeavor to keep away from flood plain location (requiring knowledge of previous flood reaches) and to ensure adequate storm water drainage (in association with water and sewerage installation).

The western side of the Andes is a region of high-velocity avalanches in the river valleys, triggered by sharp heavy rains on the mountain sides. These phenomena are called "huaycos" (Benavides, p. 98). They carry soil, rocks, plants, crops and anything else in their way in a torrent down towards the plains. It is uncertain at this point whether any potential site is located in this region. Once again, though, caution is needed to find sites which are out of the path of these forces.

### III. THRESHOLD RECOMMENDATION

Based upon the foregoing discussion, a Positive Threshold Decision is recommended for Perú 527-HQ-011, in accordance with Regulation 16 and the Office of Housing Environmental Policy and Actions (DS/H Manual Order 42-0, January 30, 1979, Part 3.B.) The potential for significant adverse impacts associated with the proposed program requires further environmental work during subsequent steps in program development.

APPENDIX A. PHOTOGRAPHIC SUPPLEMENT

Photograph 1. Aerial View of Amazonian Lowlands

2. Andean Region

3. Coastal Desert

4. Potable Water from a Well in the Desert

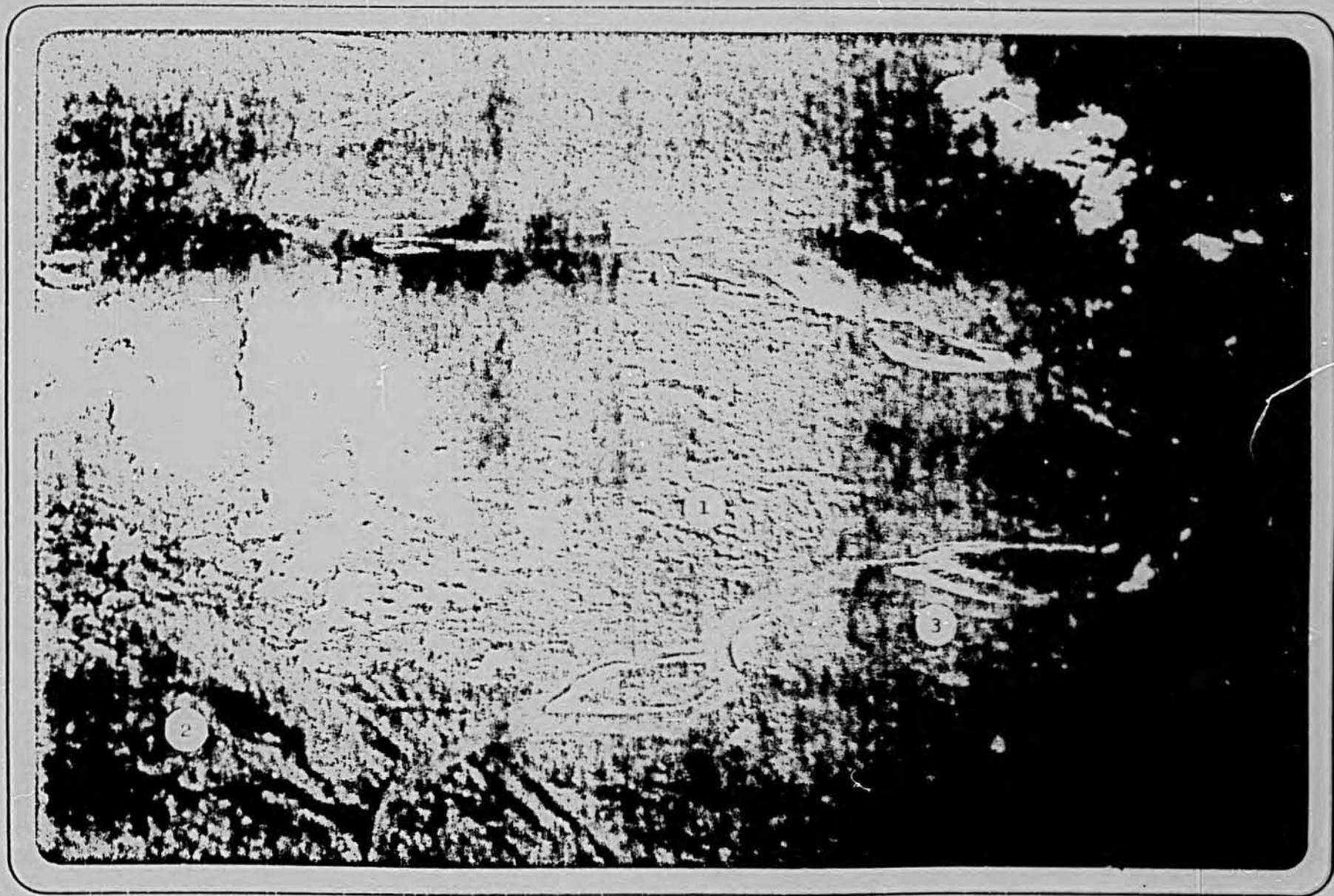
5. Existing Water Distribution System by Standpipe

6. Landslide Disaster

7. Dusty Housing Conditions

8. Urbanization in Valuable Irrigated Desert Valley

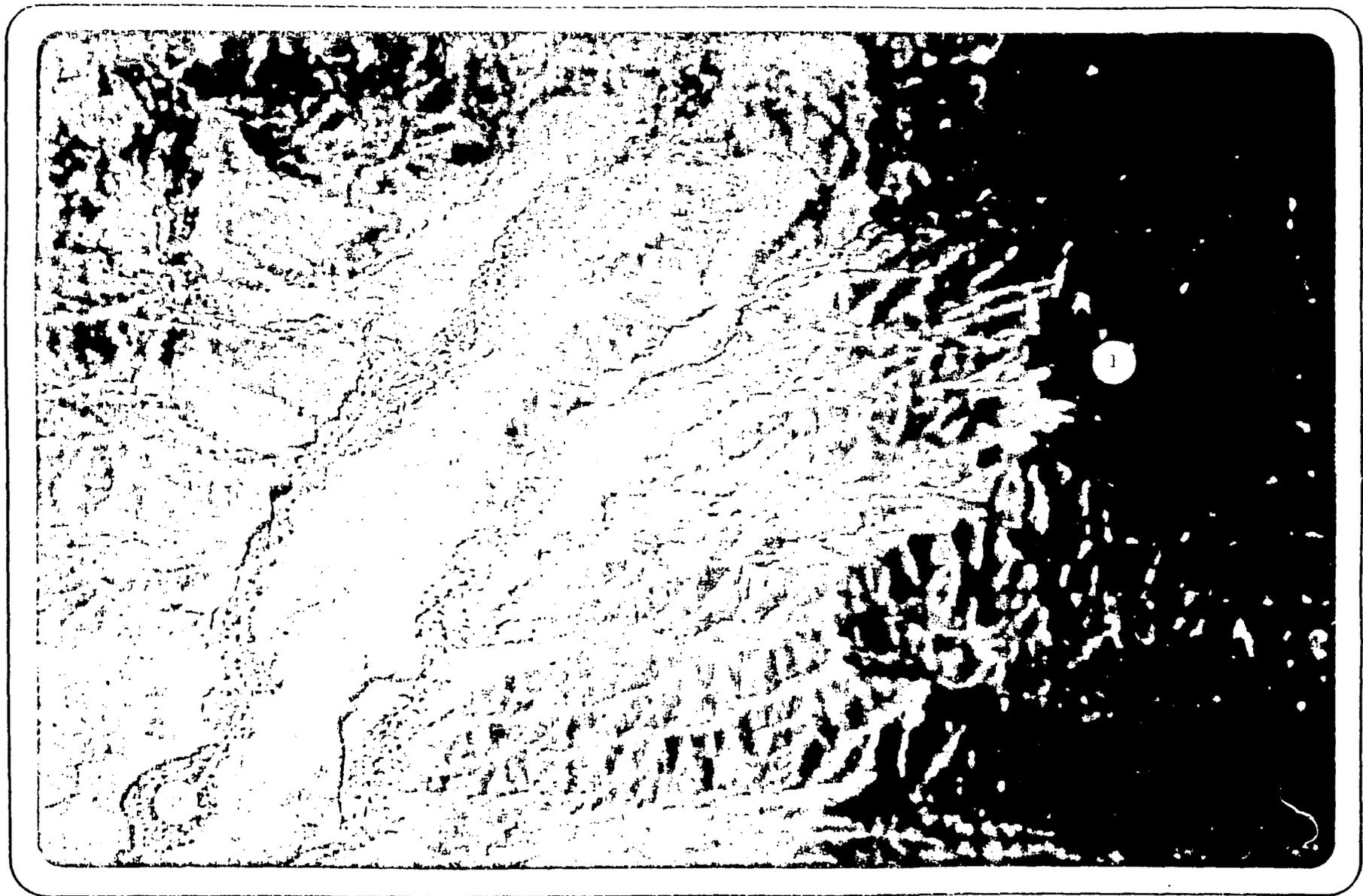
9. The Urban Dilemma in the Desert



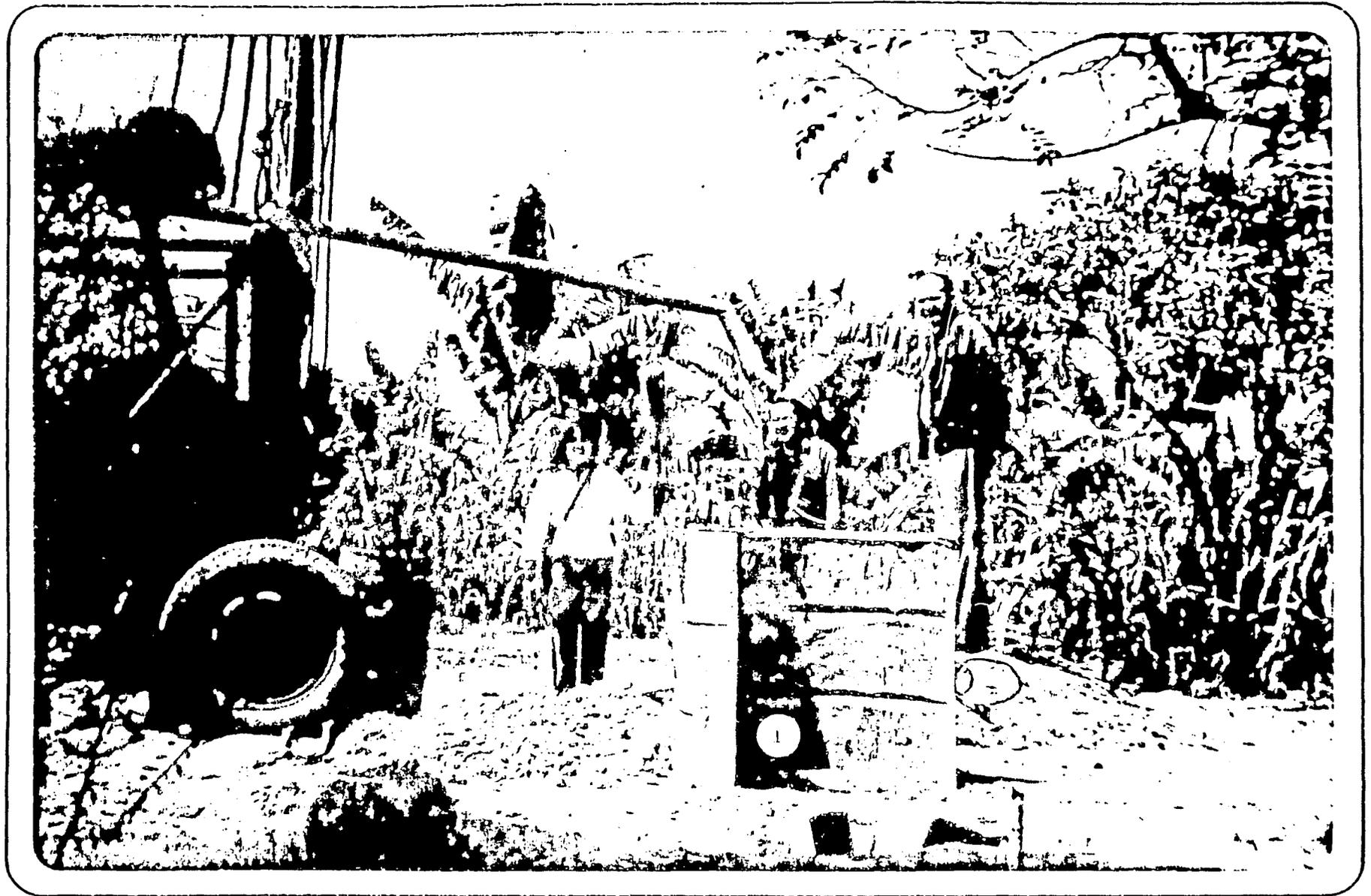
1. The Amazonian jungle represents 63% of Perú's area. The lowland part is heavily forested and flat (1). The upland area (2) consists of the foothills of the Andes. Rivers such as the one shown (3) annually flood the lowlands, and then recede, leaving sandbars in the channel.



2. The Andean montane region is 26% of Peru. The highest range of mountains, the Cordillera Blanca (1) reaches over 23,000 feet (6,700 meters). The valleys and slopes are predominantly semi-arid (2), except for the Amazonian side (3).



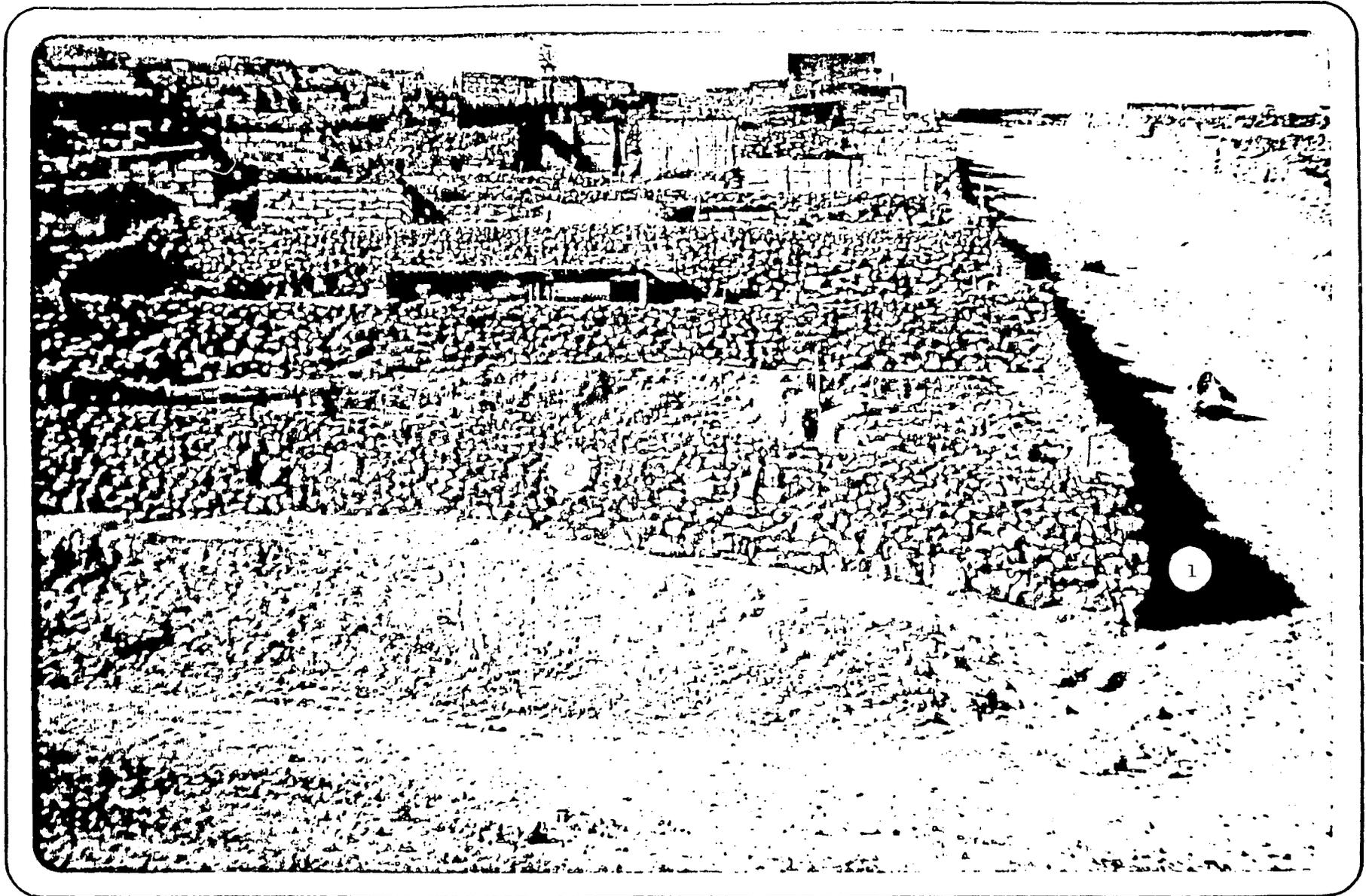
3. High aerial view of Peruvian coastal desert (1), which occupies 11% of the nation. No appreciable rainfall occurs, therefore no vegetation is found except in the infrequent river valleys (2) which drain the Pacific side of the Andes.



h. Potable water from the desert, by means of drilling a well, Chimbote. The well (1) must extend at least 40 meters (130 ft.) down. Redrilling is required after the periodic earthquakes snap the tube. Well water is an important source of potable water in the desert.



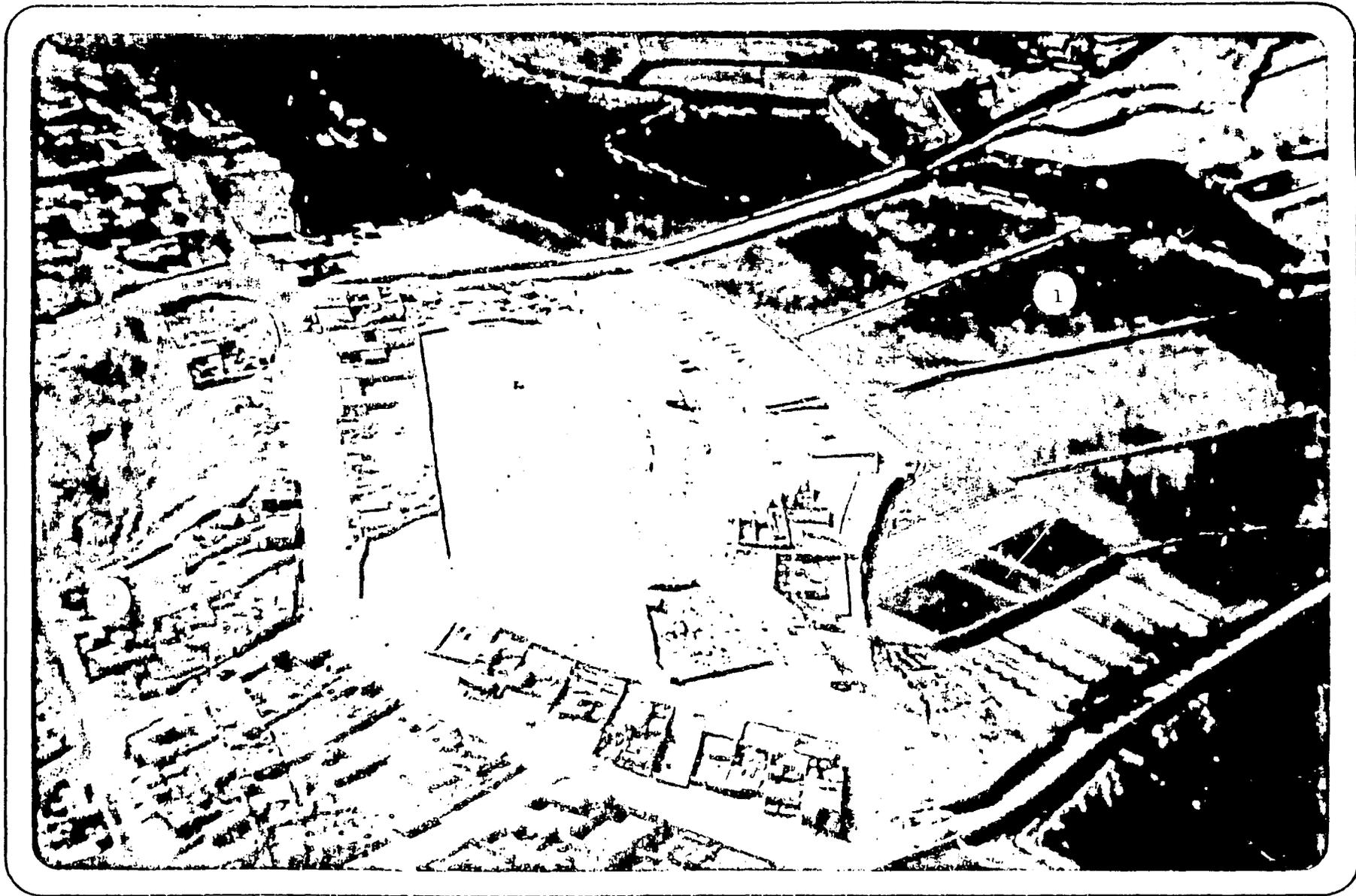
5. Potable water distribution system in Piura, by means of a communal standpipe (1). The children carry the water in tin cans. Consumption is lower than it would be should each home have individual on-lot service.



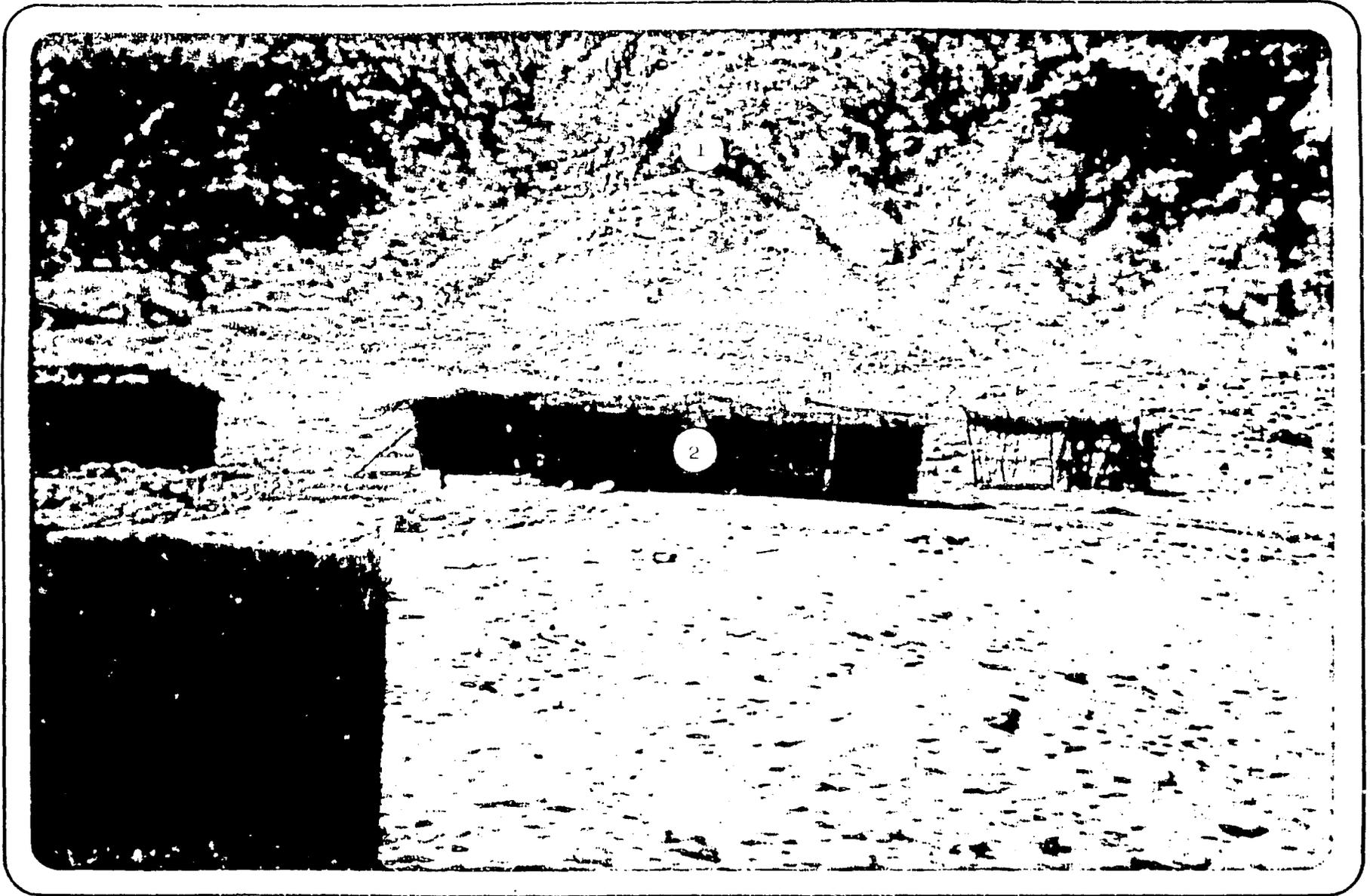
6. Dusty conditions found on the Pacific side of the Andes. This pueblo joven in Arequipa has sandy, dirty streets (1). Respiratory ailments are aided by these conditions. Rocks (2) are cleared from the land to serve as lot line markers.



7. Landslide disaster in Callejón de Huaylas, Ancash Department. A major earthquake located in the Pacific Ocean was so powerful it caused part of Mount Huascarán's glacier to split off, sending ice, snow and rubble down a narrow pass (2) to the populated valley below. Individual boulders (3) and other debris buried the town of Yungay, killing 20,000 people by earthquake and landslide.



8. Urbanization proceeding at the margin of irrigated land (1) in the desert, Arequipa. Spontaneous settlements (2) threaten existing agricultural land and preclude expansion of irrigated land. Increased food imports result, thereby draining the country of much needed currency.



9. Perú's urban dilemma: the desert (1) is inhospitable even to low-density housing (2) and yet ever-increasing numbers of people are moving to the coastal desert cities.

## APPENDIX B. REFERENCES

- AID. May 1972. Perú, Urban Reconstruction, Earthquake Area. Capital Assistance Paper, AID Loan No. 527-L-055.
- AID. Office of Housing. June 1979. Draft Shelter Sector Assessment, Perú. 93 pp. + 16 annexes.
- AID, Office of Housing. June 1979. Initial Environmental Examination, HG-010.
- AID/Peru. October 1979. Draft Project Identification Document, 527-HG-011.
- Benavides, J. Augusto. 1977. Mi Nueva Geografía. Lima: Editorial Universo. 287 pp. (My New Geography of Perú).
- Leon, Abelardo Sanchez et al. 1979. Tugurización en Lima Metropolitana. Lima: DESCO, Centro de Estudios y Promoción del Desarrollo. 190 pp. (Tugurization of Metropolitan Lima).
- Romero, Emilio. 1973. Perú, Una Nueva Geografía. Lima: Librería Studium. 2 volumes (376 pp. and 329 pp.). (Perú, A New Geography).
- Weil, Thomas E. et al. 1972. Area Handbook for Perú. 430 pp.
- World Bank (IBRD). October 1978. "Report and Recommendation...on a Proposed Loan to the Republic of Perú for a Water Supply and Power Engineering Project."

BVP ENVIRONMENTAL CHECKLIST FOR SELECTION  
AND DEVELOPMENT OF ENVIRONMENTALLY-  
SOUND PROJECTS

The use of this attached form will consist of first identifying the pertinent impacts by completion of the checklist. Then in the spaces entitled "Observations", measures will be indicated to minimize or avoid the negative impacts indicated in each section of the checklist. Should the project not prove amenable to design and locational measures, then the completed form would conclude with a rejection of the proposed project on these enunciated grounds.

This form shall guide the BVP in its sponsorship of environmentally-sound projects. When it receives a project for review, it will be asking for environmental information and analysis to be included in the Memoria Descriptiva (Background Report). Therefore environmental concerns will be channeled back to project initiators.

This form has been reviewed and approved by the Office of Housing. At the present time it is in the draft stage of preparation. Its format follows other technical forms and usages of the BVP.

ENVIRONMENTAL ANALYSIS OF THE PROJECT

Housing Bank of Peru  
Project Analysis Department

Project No.

Reference

Report:

Date:

Of:

For:

Name of Project:

City:

District:

Applicant:

1.0 Environmental Effects of the Project

2.0 Locational Factors Potentially Impacting Project

I. PROJECT IMPACTS ON THE ENVIRONMENT

A. In relation to the natural environment

1. The project will affect existing water resources:

- |  |     |    |
|--|-----|----|
| a. Surface (rivers, lakes, reservoirs) | YES | NO |
| b. Underground                         | YES | NO |
| c. Estuary                             | YES | NO |
| d. Ocean                               | YES | NO |

Observations:

2. The project will affect sensitive areas:

- |   |     |    |
|---|-----|----|
| a. Areas of resupply of underground water                         | YES | NO |
| b. Rare or endangered animal and plant species and their habitats | YES | NO |
| c. Historical, archeological, and cultural resources              | YES | NO |
| d. Unique natural areas   | YES | NO |

Observations:

3. The project will have an effect on existing or future land use and on development projects which may influence:

- |  |     |    |
|--|-----|----|
| a. Local wildlife reserves                                       | YES | NO |
| b. Agricultural lands  | YES | NO |
| c. Important natural resources (woods, wetlands, minerals, etc.) | YES | NO |
| d. Open space/recreation lands                                   | YES | NO |
| e. Ecological equilibrium of the area/region                     | YES | NO |
| f. Stability and preservation of human settlements               | YES | NO |

Observations:

4. New or different technology, related to infrastructure and community services, will provoke ecological consequences:

- |   |     |    |
|---|-----|----|
| a. Water consumption beyond the limitations of the supplies               | YES | NO |
| b. Energy Requirements  | YES | NO |
| c. Air quality  | YES | NO |
| d. Water quality  | YES | NO |
| e. Change in agricultural practices and use of human waste for fertilizer | YES | NO |

Observations:

B. In relation to the human environment

1. The project will affect traditional customs and sociocultural conditions:

- |   |     |    |
|---|-----|----|
| a. Community character and cohesion         | YES | NO |
| b. Social organization                      | YES | NO |
| c. Institutional structures                 | YES | NO |
| d. Lifestyle and cultural traditions        | YES | NO |
| e. Family organization and values           | YES | NO |
| f. Demographic or social profile            | YES | NO |
| g. Level of personal safety and convenience | YES | NO |

Observations:

2. The project will affect traditional concepts and housing techniques:

- |  |     |    |
|--|-----|----|
| a. Building materials                              | YES | NO |
| b. Construction techniques                         | YES | NO |
| c. Housing form and style                          | YES | NO |
| d. Interior design or space                        | YES | NO |
| e. Spatial relationship among the housing elements | YES | NO |
| f. Population density                              | YES | NO |
| g. Housing location                                | YES | NO |

Observations:

3. The project will affect public health and general well-being:

a. Contagious diseases and health conditions	YES	NO
b. Migratory movement	YES	NO
c. Employment centers/sources of income	YES	NO
d. Land tenure and/or human settlement stability	YES	NO
e. Form of use of income	YES	NO

Observations:

II. LOCATIONAL EFFECTS ON THE PROJECT

A. In relation to the natural environment

1. Sensitive areas will affect the project:

a. Wetlands, swamps, alluvial plains, and estuaries	YES	NO
b. Slides of land and rock, huaycos, unstable slopes	YES	NO
c. Soil stability: dunes, expansive clays, inconsistent soils, erosion, etc.	YES	NO
d. Unique or unstable geological formation	YES	NO
e. Floodplains	YES	NO
f. Saline soils	YES	NO

Observations:

2. Natural hazards will affect the project:

a. Seismic movements	YES	NO
b. Floods	YES	NO
c. Droughts	YES	NO
d. High winds, paracas	YES	NO
e. Fires	YES	NO

Observations:

**B. In relation to the human environment**

**1. Problems of environmental health will affect the project:**

- |  |     |    |
|--|-----|----|
| a. Water quality   | YES | NO |
| b. Air and climate quality   | YES | NO |
| c. Exposure to contagious diseases   | YES | NO |
| d. Impacts caused by the action of man:<br>noises, smells, toxic materials, etc. | YES | NO |

Observations:

**2. The lack or limited capacity of infrastructure and basic community services will affect the project:**

- |   |     |    |
|---|-----|----|
| a. Transportation: access to work, services, etc. | YES | NO |
| b. Provision and distribution of water            | YES | NO |
| c. Collection, treatment, and disposal of sewage  | YES | NO |
| d. Medical help                                   | YES | NO |
| e. Collection and disposal of solid waste         | YES | NO |

Observations:

**3. Urban/regional growth and land use considerations will affect the project:**

- |   |     |    |
|---|-----|----|
| a. Pressure on the capacity of the existing natural systems: food, production, provision of water, etc. | YES | NO |
| b. Pressure on public services: public transportation, electric service, schools, etc.                  | YES | NO |

Observations:

**III. CONCLUSION**

Appendix A. Selected References. (See the Project Paper 527-HG-010 for additional references).

1. AID/Lima. n.d. "Disaster Predictions, Peru". Black loose-leaf folder at Mission Engineer's Office.
2. AID, Office of Housing. Dec.1979. Project Identification Document 527-HG-011, Upgrading Low Income Settlements.
3. AID, Office of Housing. Dec.1979. Shortened Draft Initial Environmental Examination, 527-HG-011, FY-1980.
4. AID, Office of Foreign Disaster Assistance, June 1978. Peru, a country profile. 76pp.
5. Library of Congress. October 1979. Draft Environmental Report on Peru. 110pp + 2 appendices. Prepared for the Science and Technology Division of U.S. Man and the Biosphere Secretariat, Department of State.
6. ONERN. October 1975. Inventario y Evaluación de los recursos naturales de la zona del proyecto Marcapomacocha. Two volumes (Inventory and Evaluation of the natural resources of the zone of the Marcapomacocha project).
7. ONERN. In press. Diagnóstico de Impactos Ambientales, Departamentos de Ancash, Lima e Ica. (Analysis of Environmental Impacts, Departments of Ancash, Lima and Ica).

CURRENT ECONOMIC SETTING: MISSION ANALYSIS

During the past three years, 1977-79, the Peruvian economy has suffered severe recession--the most severe since World War II. Peru's estimated GDP for 1979 was 17% less than it would have been if the economy had grown by 5% annum from 1970. From 1977 on, per annum GDP growth has been about zero, reflecting the combined impact of substantial growth in mining sector output and an absolute decline of output for the urban-based manufacturing, construction, and related trade and finance sectors. Inflation accelerated from an annual pace of less than 10% in the early 1970s to 56% in 1978 and 68% in 1979 (on an average basis) due to monetized fiscal (and public sector) deficits and corrective devaluations. Simultaneously, decreased real credit to the private sector has reduced real demand, thereby eroding employment opportunities and real incomes in the urban sector. Since 1976, urban real wages and incomes have declined by about 30% for lower income households (and by even larger percentages for middle and upper income households), and unemployment and underemployment in the Lima metropolitan area has increased from a level of 26% in 1975 (April-May) to 47% in 1978 (July-August).

Set against present conditions, the medium term outlook is for moderate improvement of the economic welfare of most urban Peruvians. Real urban incomes should increase moderately in 1980--probably on the order of 4-7% and more impressively in 1981. The projected improvement derives fundamentally from the very good performance of Peru's external sector in 1979, which increased foreign exchange availability sufficiently to enable Peru to resume normal service on its large external debt (\$9.3 billion at year-end 1979) and to pay for an increased volume of imports. Export earnings in 1979 amounted to \$3,467 million--a 79% increase from the 1978 level of \$1,941 million. The increase in earnings derived from substantially higher export prices for petroleum, silver, and copper, generally buoyant market conditions for other traditional mineral and agricultural exports, as well as a \$342 million increase in non-traditional (generally industrial sector) exports. The increase in export earnings and a negotiated reduction of public sector external debt amortization produced a \$1,572.1 million increase in Peru's (banking system) net international reserve position in 1979, and freely disposable foreign exchange holdings of the Central Bank were at a record high of \$1,022 million at year end. The brisk recovery of external account solvency fulfills the indispensable condition of allowing near-term growth of imports. A sustained increase in urban real incomes also depends upon successive reductions in the rate of inflation (to increase real wages rapidly) and upon a revival of domestic investment activity (to increase employment opportunities). Due to normal lags in economic processes, a return to pre-recessionary or historical norms for urban incomes is not expected until 1983-84. It should also be noted that the expected resumption of prosperity could be choked off by inept domestic economic management and/or a deterioration of world economic conditions.

The roots of Peru's recent economic debacle stretch into the past. The Phase I military government which came to power in 1968 undertook structural reforms aimed at creation of a more equitable distribution of income and wealth. A sweeping land reform redistributed 45% of Peru's best farmlands to workers' cooperatives. Through nationalization and creation of new enterprises, the State took over direct control of 150 enterprises in key economic sectors. By 1973 the State had assumed the role previously held by foreign capital in electricity, telephones, and railways, and had taken over much of the mining sector and the banking system, virtually all export marketing, and the fishing sector. The State's role in capital formation rose (from less than one-fourth of total investment in 1968-70 to about one-half in 1974-78). The role previously played by foreign direct investment was replaced by sharply increased utilization of external credits, including medium-term credits from foreign commercial banks.

The favorable perception of Peru's external creditworthiness in the early 1970s was further enhanced by discoveries of petroleum in Peru's northeastern jungle region in 1971 and the subsequent participation by 16 foreign petroleum firms in exploration activities. By 1975 it became apparent that Peru's petroleum exports in the late 1970s would be less than had been expected because proven petroleum reserves amounted to only 550 million barrels. The fundamental base of Peru's external accounts was eroded during the first half of the 1970s by overall stagnation in export volume arising from the impact of uncertainties engendered by the revolutionary experiment on large scale private sector investment and from the long gestation periods typical of major mining sector expansion programs. (For example, the SPCC Cuajone copper mine initiated in 1971 came on stream in late 1976; and the PETROPERU trans-Andean oil pipeline and northern spur were not operating at near capacity until mid-1978 even though the project had been initiated in 1973.)

While export growth was stagnant, import volume was pushed upward after 1970 by domestic prosperity as the Phase I government followed clearly expansionary monetary and fiscal policies, particularly after 1973. Central government expenditures rose from 17.2% of GDP in 1973 to 20.6% in 1977 while domestic tax revenues remained at less than 14.0% of GDP and the domestically-financed fiscal deficit grew from less than 2% of GDP to about 4% of GDP. Prior to mid-1976 governmental policy on food pricing, interest rates, exchange rates, and foreign trade encouraged consumption and discouraged savings and tended to transfer real income from rural to urban sectors, and for a time (1970-73) urban real incomes rose above historic norms. Beginning in 1973 unfavorable exogenous factors eroded Peru's external accounts. The OPEC-induced 1973 petroleum price increase added at least \$200 million annually to Peru's import during the period 1974-78. Anchovies, the principal source of exported fishmeal, virtually disappeared in 1973, and the catch in 1974-78 averaged less than 25% of the 1968-71 level. After 1974 and up to 1979, the external terms of trade generally worsened, i.e. export prices of sugar, copper, and all minerals except silver declined as import prices increased. A pegged exchange rate and an excessive growth of aggregate demand--activated by an expansion of net domestic credit expansion running in excess of 50% in 1975--led to a rapid expansion of Peru's trade deficit (from

an annual surplus of \$106 million in 1972-73 to an annual deficit of \$920 million in 1975-76). Despite a substantial increase in Peru's net inflow of long-term capital (which averaged \$902 million in 1974-76 as compared with \$157 million annually in 1971-73), Peru's net international reserve position declined by \$1,444 million in the two-year period 1975-76.

By 1976 Peru threatened by the exhaustion of foreign exchange reserves (suggesting a possible disruption of imports) and an accelerating monetary expansion (suggesting the emergence of hyperinflation). The Phase II military government initiated a stabilization program in mid-1976 to arrest the growing balance of payments (B/P) and fiscal disequilibria and achieved initial success in terms of domestic policy implementation and of completion of a stabilization transaction, i.e. the external credits needed to close the B/P gap. This transaction broke down in mid-1977 due to the unwillingness of the government to maintain fiscal discipline, to abortive negotiations with the IMF, and to erosion of confidence of external creditors. By the second quarter of 1978, Peru was no longer able to service its short-term commercial credits on a timely basis and was also unable to comply with the terms of an IMF standby agreement signed in November 1977. Just what factors were most responsible for this debacle--untimely arms purchases, the heavy demands of the IMF, incorrect economic perceptions of governmental leadership--is open to debate. The economic medications administered from mid-1978 included a sharp effective devaluation of the Sol (from 117.03 sales per dollar at the end of November 1977 to 154.85 at the end of June 1978), maintenance of a fiscal deficit of substantial magnitude (about 4% of GDP), expansion of banking system credit to the public sector of 122% in 1977, and a decline of real banking system credit to the private sector. These policies worsened the recession and increased inflation.

A stabilization transaction composed of traditional elements (substantial external financing and fiscal austerity) was implemented by a new economic team in the second half of 1978. An IMF standby agreement was obtained in September 1978 (which runs through 1980) and a rescheduling (of 90%) of public sector debt amortization due in 1979 and 1980 was negotiated with major creditor governments and foreign commercial banks in 1978. The new economic team complied rigorously with the fiscally-austere quarterly targets established in the IMF standby. Due to increased foreign exchange availability, the GOP decided in late 1979 to forego a portion of the debt relief, and the plan presently being implemented includes: (1) non-utilization of the \$225 million obtained from bilateral creditors at the November 1978 Paris Club negotiations and (2) prepayment of \$376.6 million in debt relief obtained from some 267 foreign commercial banks for 1979 (but retaining the reduction in amortization for 1980 along with a reduction of the interest charge from 1 7/8% over LIBOR to 1 1/4%). Thus, the foregoing of debt relief serves to lower interest charges and the debt service ratio in future years.

Even though some aspects of Peru's recent severe recession can be linked to revolutionary experiments to achieve greater equity, strong evidence also points to inept economic management. From 1973 to 1976, government policymakers delayed undertaking policies to reduce real demand, and in 1977 they lacked the steadfastness necessary to maintain a stabilization transaction. Recession was thereby prolonged and made deeper than necessary. Exogenous forces, such as deterioration in external market conditions for Peru's exports after 1974, the increase in petroleum prices in 1974-77 (when imports were still necessary) and the anchovy decline (1973 and after) were also unfavorable.

In regard to the impact of the Phase I reforms, quantitative evidence clearly indicates reduced capital formation, which (with a lag) would also imply a reduced rate of growth for GDP. Specifically, Gross Domestic Investment (GDI) decreased by over 20% for the period 1970-78 as compared with 1960-69; the ratio of GDI to GDP decreased from 20.8% for 1961-69 to 16.2% for 1970-78. To some extent, this decline is related to losses due to decapitalization of physical and human capital in the foreign enterprise and agricultural sectors and to the loss of potential investment by wealthy emigrants. However, private sector managers who stayed in Peru generally adopted a "wait-and-see" attitude due to the increasingly strident pro-socialistic rhetoric of the Phase I government, and such private sector investment as took place was oriented principally to capital deepening of existing enterprises rather than to the creation of new enterprises (due to the peculiar mechanics of the Industrial Communities legislation). Moreover, and even apart from excessive military expenditures, certain public sector projects had low economic feasibility due to disjointed execution, cost overruns, or poor selection. In fairness, it must also be noted that the Phase II government took steps to restore private sector legitimacy and confidence, e.g. by restructuring Industrial Communities into a profit-sharing scheme with maximum equity ownership by workers set at one-third of share equity; reprivatization of the fishing fleet; elimination of foreign exchange controls; de-emphasis of social property enterprises; and adoption of measures to restore and maintain the profitability of state enterprises.

Perhaps the most important defect of the Phase I strategy to prevent long-term economic deterioration was the lack of a timely and low-risk program for export expansion. From the mid-1960s on, and up to 1977, Peru's exports experienced no growth in volume. Even though Peru's rich array of export products (nine principal products) dampens the impact of adverse secular price movements for particular products on overall export earnings, sooner or later a small country with stagnant export growth is forced into a situation of "stop-and-go" macroeconomic policies. That is, when export earnings are high due to a world commodity boom, policymakers can increase aggregate demand and imports and foreign borrowing can be increased. Thereafter, when the boom ends and export earnings decline, aggregate demand has to be reduced, household incomes and employment fall to socially explosive levels, and external debt service becomes onerous. With a 5% average annual growth in exports, this problem diminishes (unless the terms of trade are adverse, which has not

been Peru's situation). Therefore, the critical ingredient for a smoother and higher long-term growth path for output (GDP) is investment in the export sector (and this condition holds without regard to ownership rights and the financial modes employed for that purpose). A second consideration related to maximization of long term economic welfare is the linkage between strong economic growth and the economic welfare of the poor. Peru has already redistributed ownership rights as far as a strongly dualistic economic structure and the limits of altruism permit. This suggests that the poor can be provided with health, education, and urban services essential to their welfare by a fiscal system whose expenditures are underwritten and increased by strong economic growth and sound administration.

Looking forward through the 1980s and beyond, Peru's natural resource base and demographic factors are the principal forces facilitating and limiting economic welfare. Rich unexploited minerals ore bodies, abundant hydroelectric potential, and moderate petroleum reserves are obvious strengths; limited farmland and the high cost of expanding such land, limited availability of water in the coastal areas, and demographic pressure are obvious limitations. Population growth will place increasing pressure on agricultural land, the provision of basic public services, and food and energy supplies.

The Phase II government sponsored a constituent assembly which drafted a new constitution and elections are to be held in May, 1980 for a new civilian government to be installed in July. The new government will have to focus initially on economic policies promoting recovery. Barring a very adverse movement in terms of trade, the external account performance should pose no blockage to economic recovery for the next few years and GDP growth on the order of 6.5% per annum is possible through 1985. Even though near-term inflationary pressures impose significant problems for policymakers, barring gross errors, the pace of inflation should decline (but the official projection of 40% for 1980 may prove to be too low). There are several medium-term policy areas which demand attention. Four such issues are energy, external debt management, employment generation, and the allocation of public expenditures.

1. Unless Peru carries out an aggressive exploration program for petroleum in all areas with good possibilities or ceases shortly to export petroleum, Peru will have to resume importation of petroleum around 1984-85. The unfavorable impact of this development on external accounts is obvious. Development of Peru's abundant hydroelectric potential will entail high capital requirements and long pay-off periods. A low-risk strategy buttressing both endeavors would be accelerated development of minerals ore bodies which requires large and lumpy investments. Therefore, Peruvian economic welfare by the second half of the 1980s is critically dependent upon hammering out policies conducive to accelerated investment in mining and energy in the next 2-3 years.

2. The magnitude of Peru's external debt (nearly 80% of GDP) and the service of public sector debt (about 35% of 1980 export earnings), uncertain long-term petroleum prospects, and the need to offset public sector amortization approximating \$1.0 billion annually suggest the need for careful debt management, (i.e. contracting at long-term instead of short with a focus on productive investment) and for continued cooperation among the IFIs, major bilateral lenders, and the GOP to improve the term-structure of Peru's external debt.

3. Peru's labor force has been growing by about 150,000 annually and by 1990 this growth will accelerate--possibly to 227,000 annually. Recovery from recession, alone, will not provide sufficient new jobs. A World Bank study recommends labor subsidies to employ and train labor. Additional programs--credits linked to employment generating exports, expanded public employment to create urban and rural social infrastructure--should also be explored.

4. In regard to the management of public resources, the experience of the present decade, including waste of resources on projects of low productivity and excessive military expenditures, suggests the need for a better distribution of public expenditures both for the maximization of economic growth and for funding basic human needs. Taxation and spending are important mechanisms for improving the distribution of real income and for accelerating expansion of the modern sector. Although the fiscal mechanism cannot serve these purposes adequately without economic growth, and the bulk of revenue growth depends on growth, the recent rectification in tax administration and the distribution of expenditures should be continued.

ANNEX I

ESTIMADO DEL INGRESO FAMILIAR MEDIANO  
ESTIMATED MEDIAN FAMILY INCOME

(Soles per month)

<u>Ciudad</u> <u>C. ty</u>	<u>Reajuste a Dic.31,1978</u> <u>Adjustment as of Dec.31,1978</u>	<u>Reajuste a Dic.31,1979</u> <u>Adjustment as of Dec.31,1979</u>
1. Arequipa	20,939	38,995
2. Cajamarca	15,297	28,488
3. Cuzco	17,346	32,304
4. Chiclayo	18,576	34,594
5. Chimbote	13,648	25,417
6. Huancayo	18,583	34,607
7. Huanuco	14,118	26,292
8. Ica	21,224	39,526
9. Iquitos	19,847	36,961
10. Lima	32,751	60,993
11. Pasco	20,356	37,909
12. Piura	20,969	39,051
13. Pucallpa	16,790	31,268
14. Sullana	14,355	26,733
15. Tacna	24,289	45,234
16. Trujillo	21,037	39,177

ANNEX J

DEMAND AND THE AFFORDABILITY OF SUBPROJECTS

A. Demand as a function of population and new household formation

The population of Peru is estimated to be 18 million, and growing at an annual rate of 2.9%. If present fertility rates remain unchanged, the population will approach 32 million by the year 2,000. The 1972 Census reported 59.5% of the population to be urban, with urban areas growing at an annual rate of 5.02%.

While precise statistics are not available, GOP estimates put the number of households now in pueblos juvenes at approximately 600,000. These households divide approximately evenly between Lima and the provincial cities. The number of such households will increase by about 111,500 during the next 2 years. Given the very nature of the urbanization process represented by the growth of pueblos juvenes, these families will not have piped water, sewerage infrastructure, or electricity. The increase in need represented by the growth of these new households alone substantially outstrips the supply potential represented by the proposed \$20 million HG program.

B. Demand as a function of accumulated deficit

A 1977 survey updating data provided by the National Housing Census estimated urban infrastructure deficits to be:

- 56% of households without piped water
- 66% of households without sewerage infrastructure
- 45% of households without electricity.

Pueblos juvenes experience even larger deficits than those for the total urban configuration; but even applying the overall percentages to them, their demand as a function of the accumulated deficit is immense. Adding to this the investment required at current prices to satisfy the accumulated deficit produces the following estimates of potential effective demand:

	<u>Unit Cost</u>	<u>Deficit in Number of Households</u>	<u>Required Investment</u>
Water	776	336,000	\$261,000,000
Sewerage	352	396,000	\$340,000,000
Electricity	<u>576</u>	<u>270,000</u>	<u>\$155,000,000</u>
Total	<u>2,210</u>	<u>n.a.</u>	<u>\$756,000,000</u>

### C. Some Measures of Effective Demand

The HG 009 loan largely financed the same type of projects envisaged for this project. Its final sub-project implementation is just now winding down. Eligible sub-projects sufficient to cover the amount allotted for the first \$15 million tranche were identified and funding was earmarked by the BVP within 4 months of receipt of the letter of implementation.

The backlog of projects generated through the organizational and technical assistance efforts of SINAMOS combined with the lack of alternative financing for infrastructure services to lead many organized communities, many with plans already prepared, to make the rounds of BVP and the utilities in search of financing.

Although the austere economic climate of recent years may have eliminated some families from the market, the scale of the deficit and the strong effective demand encountered by the BVP in undertaking 009 clearly argue that effective demand is currently adequate to easily absorb the funds of 010 and 011.

The potential effective demand is many times in excess of the funding currently available. The decision to divide the funds equally between Lima and the provinces, and so approximate the actual division of pueblos jovenes households, addresses the need to support decentralization efforts by the GOP. It reflects the Mission's desire to support the development of more effective delivery systems for the basic urban infrastructure needs of secondary and tertiary cities. The combination of the S&L network brought to bear through HG 010 and the 5-city provincial coverage of BVP will make increased financing available for the urban poor outside Lima.

It is difficult to forecast the actual mix of infrastructure sub-projects. For illustrative purposes, the P.P. presents a breakdown based on the experience to date. Lower incomes in the provincial cities may well lead to more purchases of single services rather than combinations of infrastructure services. It may also be more difficult to reach as far down in the income distribution. Nevertheless, neither of these contingencies argues very strongly for an allocation of resources different from that proposed.

#### D. Affordability

Annex I shows the median family income of each of the potential project cities. In order to simplify the presentation, the cities have been grouped into 2 categories with the following December 1979 median monthly household income:

<u>Group</u>	<u>Median-Income</u>
Metropolitan Lima	\$243.97
Other Urban	121.78

a/ At an exchange rate of S/.250 = US\$1.00

The calculations below show the minimum income necessary to qualify for a loan for each service package and what percentage of the target group can afford each package.<sup>1/</sup> The loan amounts are net of a 5% down-payment. Twenty-five percent of income is used to qualify participants.

TABLE I

Monthly Qualifying Monthly Household Income (\$)  
(Loan at 21.5% p.a.)

	<u>10 years</u>	<u>15 years</u>
A. Sewerage	66	61
B. Water	60	55
C. Electricity	44	41
D. A + B	126	116
E. A + B + C	171	157

TABLE II

Percentage Affordability by Target Group Project Component  
(Loan at 21.5% p.a.)

<u>Repayment Period</u>	<u>A</u>	<u>B</u>	<u>C</u>	<u>D</u>	<u>E</u>
<u>10 years</u>					
Lima	77	81	91	28	10
Other urban	14	24	62	-	-
<u>15 years</u>					
Lima	30	34	92	27	12
Other urban	22	36	58	-	-

<sup>1/</sup> Construction costs are rather uniform throughout the country. Estimated unit costs as of 31 December 1979 were: water, \$776; sewerage infrastructure, \$858; electricity, \$576.

FONAVI: A NATIONAL HOUSING FUND FOR PERUIntroduction

1. Decree Law No. 22591 of 31 July 1979 established a new National Housing Fund (Fondo Nacional de Vivienda: FONAVI) in the BVP. FONAVI has the potential to be a dominant new factor in the housing sector, financing some 1.1 million houses over the next 30 years.<sup>1/</sup> Its impact will be immediate and nationwide; it will increase fivefold the volume of housing activity in the public sector, provide significant and needed support to the construction industry, increase employment, and make it possible for middle-income workers again to buy a home.

2. After briefly describing how FONAVI is structured, I shall examine some of its economic implications, compare it with an alternative system to capture forced savings for the housing sector which was under active consideration by the GOP, and suggest ways in which FONAVI should be modified during the next few years. It can and will be modified. AID should be prepared to encourage modifications which advance its own shelter sector strategy.

FONAVI

3. The principal source of FONAVI funds will be a new payroll tax, a tax equal to 4% of the payroll contributed by the employer and 1% by the employee. The GOP matches 20% of this amount. Construction firms and supplier firms for FONAVI projects each pay 3% of the value of the contract.<sup>2/</sup>

4. Projections by the MEF through the year 2008 foresee the following sources and amounts of funds:

<u>Source</u>	<u>Amount (\$ million equivalent)</u>	<u>Per Cent</u>
Employer tax	1,564.8	67.2
Worker tax	284.8	12.2
Government	370.0	15.9
Construction companies	66.4	2.8
Supplier companies	44.0	1.9
Total	2,330.0	100.0%

\* A report prepared by Donald E. Stout, FCH, in response to Work Order No. 65 dated 15 October 1979

<sup>1/</sup> This would make housing available to about 27% of the participating workers over the 30-year period, to about 1.2% of the eligible workers in the first year of FONAVI.

<sup>2/</sup> The BVP also is authorized to issue bonds Type A which must be purchased by the Social Security System and by insurance companies; and type B which can be placed in the open market. The BVP does not plan to issue bonds because there presently is no financial incentive to do so.

During the 30 years, FONAVI also expects to collect in rents and sales of housing units a total of \$2,344 million equivalent, bringing the total resources available to FONAVI up to nearly \$4.7 billion equivalent.

5. MEF projects that with these resources, FONAVI can finance about 500,000 housing units during the first 20 years. The Minister of Housing and Construction stated that the immediate level of effort will be the construction of 15-20,000 units per year, the creation of 45-60,000 new jobs directly in construction, and 125-180,000 new jobs indirectly in supplier activities. By any of these measures, FONAVI will be a major new force in the economy. The MEF, for example, projects 1980 FONAVI collections at US\$123 million equivalent. This would be 5 times the volume of public sector shelter activity in 1978. In the first two months after FONAVI was established, the MORC called for 37 bids. Five more will be issued momentarily. The 37 tenders total some \$32 million equivalent, one-third more than the total public sector shelter activity in the entire year of 1978. All of the 37 projects are to be completed by the end of 1980. FONAVI is off to a running start.

6. FONAVI has some particular attributes which should be noted before turning to an analysis of its operations.

- a. FONAVI efforts are to be concentrated outside the Lima-Callao area. The President of the BVP said that the goal was to direct 70% or more of FONAVI activity outside the Metropolitan area. (A list of 33 of the first 37 bids which have been tendered shows about 45% of the total value is in the Lima-Callao area. As the shelf of existing projects is financed, the pipeline of new projects presumably will present a lower proportion for Lima-Callao.)
- b. FONAVI loans will be at a nominal interest rate of zero; but loan balances will be indexed by (up to) the percentage change in the Lima minimum wage. This determines an implicit interest rate.
- c. Housing units will be allocated by lottery.
- d. EMADIPERU manages the renting, maintenance, and selling of units.
- e. The expected clientele will be middle-income and lower middle-income families with qualifying monthly incomes ranging from S/.12-60,000. The maximum unit cost is limited to 360 times the Lima minimum wage (a maximum cost of S/. 4.32 million, or \$18,000 equivalent.) <sup>1/</sup>
- f. The eligible income must be at least 90 times the cost of the unit. Amortization is spread even by over 240 months for purchases. Rental payments are equal to the monthly amortization charges over 400 months.

<sup>1/</sup> The minimum wage in Lima-Callao was revised from S/.12,000 to S/.15,000 (about \$50 to \$62.50 equivalent) on 23 September 1979. The minimum qualifying income presumably will be increased to S/. 15,000 and the maximum house price to \$22,500 equivalent.

- h. The MOHC determines how many of what types of units will be built and where they will be built.

7. Finally, it is FONAVI policy to sell no units in the early years. As units are completed, they will be rented with an 18-month option to buy. This will lessen the monthly payment initially required from the squeezed middle class.

#### Issues

8. Inflation. The inflationary impact of FONAVI is the most disputed aspect of the program. The Minister of Economy dismisses the issue by saying that a 4% increase in employers' wage costs could not justify more than a 2% increase in product prices. In the overall context of inflation running at an annual rate of 60 - 70%, this is insignificant. CAPECO goes farther and points out that the 4% tax is on labor payments only, attempts to calculate the value added by labor as a percentage of total costs in major industrial sectors, and concludes with an estimate of a possible 0.44% increase in prices. On the other hand, some economists foresee a much stronger inflationary effect. Paul Rosenstein-Rodin and Daniel Schydlawsky, both distinguished economists, criticize FONAVI strongly on this ground.<sup>1/</sup>

9. We will never be able to point to a number and assert with confidence that FONAVI added so many percentage points to the inflation rate. Although FONAVI looms large in the shelter sector, it is a modest proportion of total economic activity, probably too small to be able to be isolated among the hundreds of economic cross currents which induce inflation. Still, some specific potentially inflationary biases can be identified and, to some extent, countermanded. Two biases, in particular, can be anticipated: (1) the prices of land and shelter inputs; and (2) the prices of food and basic consumer goods.

10. A new system of supplier bidding (Concurso Oferta) has been established in order to get FONAVI-financed projects moving quickly. Promoters, land-owners, and builders can form consortia to present turn-key development packages to the MOHC. There are reports that land prices are being rapidly bid up by groups eager to use the same sites for projects. Other than land prices, however, there seems to be a consensus that the prospective supplies of building materials need not become bottlenecks which lead to price increases. Overall supply capacity is adequate. Spot shortages of particular materials could arise at times if deliveries are not programmed. It is encouraging to learn that the MOHC already has undertaken a canvass of supply capacities with a view to preparing a time and place matrix of building materials. This approach should enable FONAVI projects to avoid temporary shortages and price pressures on building materials.

11. Most of the direct employment generated by FONAVI will be for less skilled and lower paid workers. Savings from this additional income will be minimal. Nearly all of it will go immediately to the purchase of food and basic consumer goods -- food, clothing, medicine. The food supply is quite inelastic in the short run; consequently, some upward price pressure can be

<sup>1/</sup> Quoted in CAPECO, "FONAVI: Disposicion de Fuerzas," an internal document, F, 8.

expected to appear for food items. As with building materials, however, these pressures can be anticipated and mitigated by programming the temporary additional demand to be expected at project sites.

12. Subsidies and implicit interest rates. FONAVI has a strong subsidy element built into its operations. A family with a monthly income of \$50 equivalent would qualify to buy a unit costing \$4,500 equivalent, paying 37.5% of its income in monthly payments of \$18.75 equivalent over 25 years. If 25-year mortgages were available at market rates of interest, the monthly payment would be about \$144 equivalent. The \$125 a month difference can be thought of as a subsidy.<sup>1/</sup> At the limit, this implies a US\$41 million potential subsidy to the buyers of FONAVI houses in the first full year of operation.<sup>2/</sup> And this would be cumulative: \$41 million the first year, \$82 million in year 2: a mind-boggling implication for resource allocation within a very few years.<sup>3/</sup>

13. These subsidies stem only from the use of a zero interest rate in establishing amortization payments. Implicit subsidies actually will be still greater because of the indexing mechanism. Mortgage balances will be adjusted by a monetary correction factor no greater than the increase in the Lima minimum wage. In practice, the minimum wage has not fully compensated for inflation in recent years.

1/ Market interest rates still lag behind inflation and are negative in real terms. If market interest rates reflected current inflation plus a 6% real interest rate, the monthly payment would be about \$250 a month for a \$4,500 unit over 25 years. The unreality of these payments has pretty much eliminated effective demand for all except luxury housing and this facet of life underlies the rationale for FONAVI.

2/ S/.30.8 billion expenditure on units costing S/.1.08 million each.

3/ Actual subsidies could be even greater in the early years since all units will be rented at monthly rents equal to 0.6 of purchase payments.

This system would have produced heavily negative real interest rates as real wages declined since 1974.

<u>Date</u>	<u>Minimum Wage a/</u>	<u>Nominal Wage Index</u>	<u>Consumer Price Index a/</u>	<u>Real Wage Index</u>	<u>FONAVI Implicit Interest Rate b/</u>
2 April 1974	S/. 3,000	100.0	100.0	100.0	0
19 May 1975	3,540	118.0	124.1	95.1	(4.8)
1 July 1976	4,500	150.0	176.9	84.8	(15.2)
2 August 1977	5,400	180.0	250.7	71.8	(28.2)
10 October 1978	6,900	230.0	438.7	52.4	(47.6)
7 February 1979	8,970	299.0	510.0	58.6	(41.4)
30 June 1979	12,000	400.0	599.2	66.8	(33.2)
28 September 1979	15,000	500.0	693.2	72.1	(27.9)

a/ Lima-Callao area.

b/ If FONAVI had been in operation. Parentheses indicate negative percentage interest rates.

If, on the other hand, real wages rise, it is unlikely that loan balances would be indexed by the full increase in minimal wages. To do so would increase monthly payments to amounts exceeding the already high 37.5% of income. It is probable that real interest rates will be negative both when real wages are falling and when real wages are rising.

14. If the minimum wage were increased each year to reflect the past year's inflation in full and if the indexing were by the full percentage increase in the minimum wage, the real implicit interest rate still would be negative because of the lag effect of always catching up to last year's inflation. At a 20% annual inflation rate, the real interest rate would be minus 9%; at 60% inflation, minus 37.5%. Finally with zero inflation or if payments are fully adjusted for inflation (unlagged), the FONAVI schedule of payments reflects interest rates of 0.15% per month for sales, a minus 0.15% per month for rentals.

15. In short, the real subsidies to those who receive FONAVI-financed housing are quite substantial. The GOP may not "feel" the subsidies because they do not show up as a budget expenditure. They are nonetheless real in the sense that they represent a foregone expenditure for other GOP budget items. The GOP decision to establish FONAVI with this level of subsidy is consonant with its understandable concern with the deteriorating quality of life of its middle class. The subsidy probably is supportable indefinitely because the minimum wage cannot continue to fall forever in real terms; so the decapitalization of the FONAVI portfolio probably will never exceed the amount of new resources becoming available each year. It does suggest several questions, however: (1) Is the GOP aware of the full extent and implications of the subsidy? (2) Is there a better way of designing FONAVI to accomplish the same shelter-building goals with less "distortion" in the allocation of

resources? (3) Can AID's target group be benefited by FONAVI?

16. Income distribution. If the GOP consciously has opted for a policy to buffer its middle class with subsidized housing and if the GOP can afford the subsidy, FONAVI is a perfectly understandable mechanism to accomplish that policy objective. Housing, especially low-income housing, is universally subsidized in developed and developing countries alike. There is one perverse implication of FONAVI for income distribution in Peru, however, which should be foreseen. Under the HG infrastructure programs, there is every reason to believe that the real interest rates paid by borrowers will become positive within a year or so as inflation is reduced. We will then confront the anomaly that the lowest-income groups are paying more of the cost of its shelter-related services than higher income groups which have access to FONAVI. The government will be foregoing the opportunity to use the FONAVI subsidies for the lowest income groups. In a sense, the poorest will be indirectly subsidizing the higher-income households. This contradicts the GOP's principle of equity goals in income distribution.<sup>1/</sup>

17. SIFEVI. There is a proposed system better than FONAVI to accomplish the objectives of FONAVI (and more) and to do it more efficiently.<sup>2/</sup> Like FONAVI, the Sistema de Financiamiento Exclusivo para Vivienda (SIFEVI) is a proposal to capture forced savings for application in the shelter sector. The BVP sponsored the SIFEVI project and had received favorable reactions from the GOP before FONAVI was set up.

18. SIFEVI's major source of funds would be the indemnification funds which employers reserve for lump sum payments to workers who leave their employment. Since firms use the indemnification funds for working capital, SIFEVI would only ask to capture 10% of the addition to the funds during the first year, increasing the percentage to 20, 30, 40 and from the fifth year on, 50% of increases in the indemnification funds. Compared with FONAVI, this source of funds would not be inflationary and would not be a new tax.

19. Other sources of funds would be (1) key money deposits from the beneficiaries of SIFEVI financing, averaging 20% of the value of the property; (2) purchase of SIFEVI bonds by construction companies and suppliers equal to 5% of the value of the work contracted with SIFEVI; (3) GOP capital transfers equal initially to 10% of SIFEVI operations and also one-third of the government collections from the existing (before FONAVI) taxes on wages and salaries; and (4) Social Security funds which are supposed to be passed on to the BVP but which until now have not been.

---

<sup>1/</sup> I want to emphasize that I am not calling FONAVI into doubt. I strongly support this initiative on behalf of the straitened middle class. I am questioning only whether the GOP is aware of the income distribution implications and might be willing to share the pie in some way with AID's target group.

<sup>2/</sup> SIFEVI was described in the SSA. The following amplifies that description in the light of further discussions and the newly available text of the SIFEVI proposal.

20. The sources and costs of funds for SIFEVI can be summarized as follows:

<u>Source</u>	<u>Percent</u>	<u>Nominal Cost (%)</u>	<u>Finance Cost</u>
Indemnification Funds	50.7	12.0	6.08
Deposits	20.0	12.0	2.40
Bonds (Construction companies)	5.0	12.0	0.60
Social Security	2.0	12.0	0.24
Government capital transfers	10.0	0.0	0.0
Government payroll taxes	12.3	0.0	0.0
Total	100.0%		9.32%

The BVP calculated that the funds could be lent at 14.6%, the spread covering administrative costs and reserves. The real interest rate would, of course, be negative -- a deliberate policy decision. The total resources would exceed the new FONAVI annual resources by year 4 and, including portfolio collections, soon be capable of a substantially higher volume of activity than FONAVI.

21. The fundamental difference from FONAVI is that SIFEVI would work through and strengthen the existing housing finance system. SIFEVI also would provide an incentive for beneficiaries to save. FONAVI is based on the luck of the lottery draw. There is no incentive for individuals to save. While addressed primarily to the same client group as FONAVI, SIFEVI would make use of existing institutions and human motivations to sacrifice for a home.

22. SIFEVI contemplated using variable mortgage payments to broaden the group eligible for SIFEVI financing and indexing higher priced units to cross-subsidize non-indexed, lower-priced units. An important additional feature of SIFEVI is that, in strengthening the S&L system, the BVP intended that SIFEVI would be a secondary mortgage market.

23. SIFEVI is a well-conceived scheme to capture forced savings for middle-class housing. It has all of the good points that FONAVI has and has some additional creative financing ideas, strengthens the housing finance system, increases private savings for housing, and avoids some of the drawbacks of FONAVI relating to inflation and to the magnitude of the social cost of subsidies. The SIFEVI idea should be pursued either as a complement to FONAVI or else FONAVI should be modified to incorporate some of the SIFEVI features.

24. Possible modifications of FONAVI. FONAVI should make use of the existing housing finance system and of private promoters working through the S&Ls. Next to the (unknown) inflationary impetus which people fear from FONAVI, the most commonly cited criticism of FONAVI is that the implementation of the system will bring a big addition to the bureaucracy. The structure is complex: BVP is the banker, EMADIPERU manages and sells the properties, the Social Security Fund keeps track of collection accounts and passes the money

to the BVP, and the MOHC calls for bids and awards contracts.<sup>1/</sup> MEF stands in the background in a monitoring role. Making greater use of the private sector should be an early goal.<sup>2/</sup>

25. FONAVI coverage should be extended to groups now excluded and funds should be made available for purposes other than building houses alone. FONAVI, for example, in my view should finance cooperatives, infrastructure, and urban renovation. This extension would be a corollary of bringing the S&Ls into the system.<sup>3/</sup>

26. AID's target group. It is probable that the projections of FONAVI resources are overly sanguine.<sup>4/</sup> Nevertheless, it is clear that huge sums will be amassed. Although I do not expect major bottlenecks in the supply of building materials, I do foresee a shortage of well-conceived projects once this initial stock of projects has been exhausted. The constraint will be in the capacity of the MOHC to process projects rather than the capacity of the developers and builders to prepare projects. It would be a shame if large sums of idle funds should come into existence.

27. The combination of a prospect of idle funds and equity considerations suggests that the GOP should not discard the possibility of tapping FONAVI funds for the AID target group. The anomaly of the AID target group receiving less of the government's largess than higher income groups was discussed earlier. Making part of the FONAVI funds available for infrastructure projects in pueblos juvenes and similar communities would help to redress this imbalance. Huge draws on FONAVI would not be involved. An important principle of equity would be.

28. Miscellanea. Although some of the target group could qualify for FONAVI housing units on the basis of income eligibility, it is likely that most of those will be excluded by extra-income criteria. Two criteria for qualifying for a FONAVI lottery in particular will militate against the target group: (1) a requirement that 3 years of employment be documented; and (2) that a participant be competent to enter into legal contracts. This latter requirement could be interpreted to mean that an applicant be functionally literate. If these non-income criteria were waived for the target group, 73% of the target group in Lima-Callao would qualify to purchase FONAVI units. Outside Lima, 27% of the target group in cities with a median income of S/.25,000 (December 1978) would qualify; 11% of the target group in cities with a median income of S/.18,000. An effort should be made to qualify target group households for FONAVI lotteries if they meet the income eligibility criteria.

<sup>1/</sup> The delay in issuing the operating rules and regulations for FONAVI is due to the complexity of the multiparty negotiations involved between the agencies, not because someone is trying to block FONAVI.

<sup>2/</sup> CAPECO has prepared a project to this end. THE S&Ls support the idea. They will jointly sponsor an amendment to bring the S&Ls into the FONAVI system. Presumably the BVP would support the proposal. THE BVP would match S/.20 of S&L funds with S/.80 of FONAVI funds.

<sup>3/</sup> The management of the BVP agrees with this view.

<sup>4/</sup> Aside from delays in contributions by employers, worker contributions surely will not begin on schedule on 1 January 1980. The President has announced that worker contributions will not be collected until the economic condition of workers has improved significantly.

29. A similar comment is appropriate for SIFEVI. A shortcoming of SIFEVI as now designed is that it could only reach the top 12-19% of income households in the Lima-Callao area, fewer still outside Lima. This should be viewed within the context that less than 1% in the Lima-Callao area were able to afford the lowest-cost "economic house" by late 1978. That percentage has further declined in 1979. It should be possible to qualify some target group households for SIFEVI financing of lower-cost housing units and home improvement loans.

30. In summary, FONAVI is for real, is off to a fast start, and is the best thing to happen to the moribund housing industry in a long time. If a choice between FONAVI and SIFEVI were possible, one probably should choose SIFEVI as a superior system. They are not mutually exclusive options, however. FONAVI can be modified to incorporate some of the desirable features unique to SIFEVI or SIFEVI itself can be established as a complementary exercise to FONAVI. One could argue that FONAVI in effect is a housing stimulus which can impact immediately on the shelter sector and that SIFEVI is the longer-run institutional complement.

#### Indexing

31. The worst of the economic recession seems to be past. The 1979 external account performance was extraordinarily good. The economic team has had less success in controlling inflation -- in part because of the monetization of the increased foreign exchange reserves. Instead of the goal of a 40% annual inflation rate by the end of 1979, 60 - 70% now seems more likely. Still, this is less than during 1978. Inflation now is falling rather than accelerating; and the inflation rate should abate appreciably beginning in the first quarter of 1980.

32. In conditions of falling inflation and prospects for a continuing decline in the inflation rate, it would be intolerable to embrace a generalized system of indexing even if it were politically palatable (and it is not). Generalized monetary correction in these circumstances would only hamper the fight against inflation.

33. This does not mean, however, that partial indexing in the shelter sector is undesirable. FONAVI has an indexing system, albeit a bad one. SIFEVI would have indexed loan balances for higher income groups. Indexing is an alternative to the decapitalization of the S&Ls; so are government subsidies. The effects of the FONAVI system of indexing should be monitored. I believe that the system will have to be changed to a system based on the consumer price index, construction costs, or a combination of the two.

#### Conclusions and Recommendations

1. One can postulate that the GOP must view the shelter sector in relation to all of the people. The AID target group, by tradition and necessity, has built its own shelter. The government can and does attempt to provide the basic infrastructure services to enhance the quality of life possible in that shelter. Since AID is mandated to restrict its efforts to the below-median income families, this means basic infrastructure and community services in Peru. Middle-class housing is a proper concern for government and an understandable government concern if HG money can finance infrastructure only and if there is an effective budget constraint which

prevents the government from contributing to the cost of infrastructure as well as middle-class housing. I believe that this will prove not to be the case, that FONAVI will capture sufficient resources to finance infrastructure for AID's target group as well as to attend to middle-class housing. I recommend that USAID follow the progress of FONAVI operations in order to be able to judge whether this becomes an appropriate subject to broach to the GOP in the next HG loan. As a first step, it should be posed as an issue in the Project Paper.

2. As a continuation of its support for the S&L system, which AID was instrumental in establishing, USAID should encourage extending FONAVI resources to the S&L system. These funds would be used in part to continue financing infrastructure projects in pueblos jovenes and similar communities. USAID also should encourage any attempt to extend FONAVI coverage to cooperatives.

3. The Project Paper for the next HG should update an examination of the subsidies implicit in the FONAVI system with a view to avoiding a situation in which GOP subsidies discriminate against AID's target group. Generalized indexing should be adjured at this point; but some form of indexing for the next HG which could put the HG clientele on a par with the FONAVI clientele should be considered in the Project Paper.

4. Finally, USAID should support SIFEVI or an incorporation of much of the SIFEVI project into FONAVI.

BVP Financial Position  
(US\$ millions equivalent)

I. Summary Balance Sheet, 31 December 1979  
(US\$ millions of dollars equivalent)a/

<u>Assets</u>		<u>Liabilities</u>	
38.9	Available funds	76.7	Deposits
18.0	Receivables	9.9	Guarantee fund
100.8	Loans	16.1	Accounts due
26.0	Housing program	52.3	Central Bank line of credit
52.0	Investments	11.6	Mortgage development bonds
9.5	Fixed assets	88.9	Foreign loans
46.7	Other assets	0.9	Reserves
<u>291.8</u>	<u>Total</u>	<u>35.5</u>	<u>Capital</u>
		<u>291.8</u>	<u>Total</u>

II. Sources and Uses of Funds, 1979  
(US\$ millions equivalent)b/

<u>Sources</u>		<u>Uses</u>	
0.7	Operating profit	6.9	Required reserves
6.5	Increase in capital	42.6	Loans
16.4	S&L required reserves	9.9	Housing programs
3.2	Development bonds	7.5	Amortizations
20.8	External loans	1.2	Development bond redemptions
20.2	Collections	15.8	Investments
5.7	Deposits	6.8	Accounts due
13.4	FONAVI	7.4	Increase in cash/bank accounts
12.0	Other	0.8	Other
<u>98.9</u>	<u>Total</u>	<u>98.9</u>	<u>Total</u>

II. Financial Evolution (millions of dollars)

	<u>1970</u>	<u>1975</u>	<u>1976</u>	<u>1977</u>	<u>1978</u>	<u>1979</u>
Total assets	56.4	170.2	151.8	161.2	281.2	291.8
Capital	16.6	19.9	13.0	7.4	8.5	14.2
Loans, of which	25.6	110.5	87.6	58.6	48.8	61.8
Housing	26.6	98.8	73.4	50.0	43.6	55.2
Construction industry	-	11.7	14.2	8.6	5.2	6.6

IV. BVP Disbursements (millions of dollars)

<u>Source</u>	<u>1977</u>	<u>1978</u>	<u>1979</u>
BVP	64.3	39.4	31.5
GOP	0.8	2.0	8.1
External	3.1	7.8	26.0
Total	<u>73.2</u>	<u>49.2</u>	<u>65.7</u>

Source: BVP

a/ S/.250 = US\$1.00

b/ S/.250 = US\$1.00

## .V. Distribution of Loans, Cumulative through 31 December 1979

	<u>Amount</u>	<u>Families Benefitted</u>
<u>Housing Lines of Credit</u>	<u>119.2</u>	258,658
Electricity	8.4	108,664
Water and Sewerage	25.7	119,494
Sidewalks and Paths	1.1	642
Industrial Parks	2.2	n.a.
Urban Development	1.9	333
Housing Construction	40.6	29,525
<u>S&amp;L Lines of Credit</u>	<u>17.3</u>	<u>n.a.</u>
Total	<u>136.5</u>	<u>258,658</u>

ILLUSTRATIVE COST ESTIMATES FOR PUBLIC  
UTILITY PROJECTS

(As of March 1980, S/.260 U.S. \$1.00)

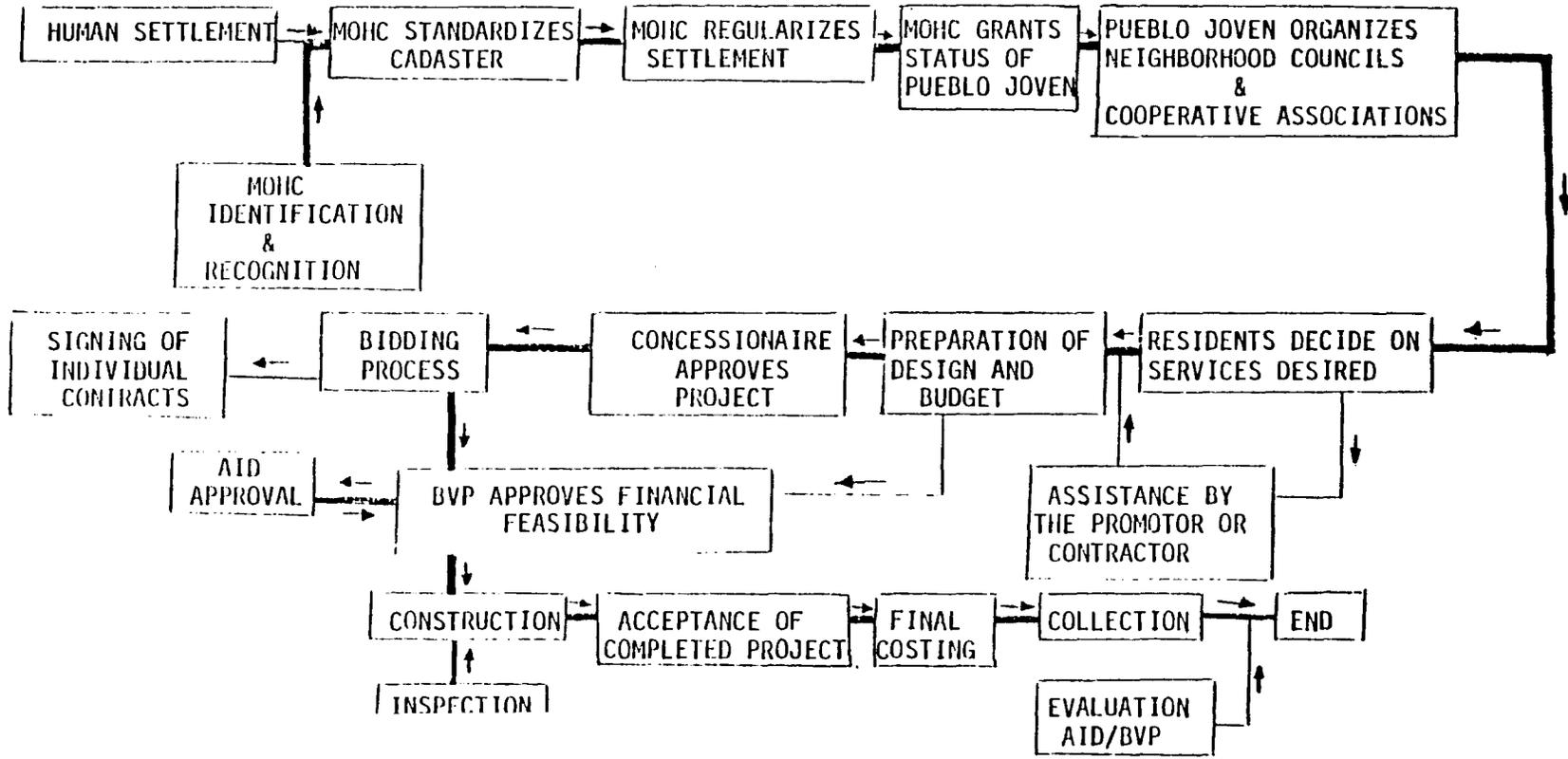
ITEM	ELECTRICITY		WATER		SEWERAGE	
	\$	S/.	\$	S/.	\$	S/.
Infrastructure (primary lines, transformers, reservoirs, wells, oxidation lagoons, etc.) <u>a/</u>	100	26,000	180	46,800	300	78,000
Secondary network	200	52,000	195	50,700	205	53,300
House connections (including meters \$100)	130	33,800	180	46,800	115	29,900
Canons, licenses	20	5,200	20	5,200	15	3,900
Supervision & administration	6	1,560	45	11,700	50	13,000
Construction financing (18% average) <u>b/</u>	77	20,000	100	26,000	111	28,860
Contingencies (10%) <u>c/</u>	43	11,120	56	14,560	62	16,120
<b>TOTAL:</b>	<b>576</b>	<b>149,760</b>	<b>776</b>	<b>201,760</b>	<b>858</b>	<b>223,080</b>

a/ Some sub-projects will not require this much infrastructure cost; others may require up to 50% more.

b/ Does not include interest charges on long-term financing.

c/ 10% is valid when computed in dollars.

FLOW CHART FOR IMPLEMENTATION OF A SERVICE PROGRAM



USAID/PERU'S URBAN STRATEGY (FY 80 - FY 84)

Background

The following briefly highlights the urbanization process in Peru. During the 1961-1972 period, Peru's total population grew at a rate of 2.9% per annum, rural population at 0.7% p.a., and urban population at 5.6% p.a. Official population growth projections are as follows: for 1980, 17.8 million (12.0 million urban); for 1990, 23.3 million (17.2 million urban); for 2000, 29.8 million (23.4 million urban). Population in urban areas (over 2,000 people) will nearly double in the next two decades and will approximate 78.5% of total population as compared with 26.9% in 1940; 40.1% in 1961; 53.0% in 1972 and an estimated 67.4% in 1980.

Peru's urbanization process involves: a movement to coastal areas, an increased concentration in larger cities, and the overwhelming primacy of Lima. Although Lima is still the primate city of Peru, medium sized cities are now growing at a faster rate than Lima.

Peru's urban explosion has been accompanied by an economic recession. The recession has had serious implications for the urban poor. The plight of an estimated 1.5 million below the median income families<sup>1/</sup>, always precarious, had by the mid seventies worsened due to lower real incomes and increased unemployment and underemployment. The middle class was also drastically hit by the recession; one indicator of the impact was a sharp decline in formal sector shelter construction starts by the beginning of 1978.

In the Lima Metropolitan area the proportion of the labor force which was underemployed<sup>2/</sup> had grown from 17.7% in March-April 1973 to 27.6% in February-March 1976 to 38.8 in July-August 1978.

The impact of urban growth and economic recession has been dramatic on the shelter needs of the poor; effective housing demand has been drastically reduced by high interest rates, and construction costs, and falling real incomes. Shelter and related services deficits are huge and are increasing. Peru's housing deficit<sup>3/</sup> in 1977 was estimated to be more than a million dwelling units. Seventy-two percent of existing housing units lacked piped water; 78% were without sewerage; and 65% did not have electricity. This translates into 1.1 million urban housing units without water, 1.3 million without sewerage and 0.9 million without electricity.

Inflation has forced the GOP to direct its limited shelter resources to safeguarding its housing finance institutions and the borrowers of the system through the injection of significant subsidies to cover, partially, losses associated with the effects of inflation. The GOP opted for subsidies in an effort to dampen the effects of inflation; it continues to strongly oppose a maintenance of value system which it views as inflationary. It is the Mission's view that these subsidies were the needed response to assisting the target group during the economic recovery period.

To stimulate a partial recovery of the construction industry in 1979, a new National Housing Fund (FONAVI) was created in the SVP. Its projected impact will be immediate and nationwide; it could increase fivefold the volume of housing

- <sup>1/</sup> Estimated median family income for Lima as of December 31, 1979 was \$270 per month with an average median income for the provinces \$153 per month.
- <sup>2/</sup> Workers who receive less than the minimum wage or work less than 35 hours per week and desire to work longer hours.
- <sup>3/</sup> Deficit as defined by the Census includes an evaluation of the number of people living per room and the type of building material used in the construction of the dwelling unit.

activity in the public sector (15-20,000 units in first year), provide significant and needed support to the construction industry, increase employment and make it possible for middle-income workers to again obtain new housing. FONAVI is funded by a new payroll tax, a tax equal to 4% of the payroll contributed by the employer and 1% by the employee. Investments are to be concentrated outside the Lima-Callao area; loans will be at a nominal interest rate of zero; but loan balances will be indexed by (up to) the percentage change in the Lima minimum wage. The units will be allocated by lottery. No units are to be sold in the early years. As units are completed, they will be rented with an 18-month option to buy.

Performance to Peru's external sector in 1979 was very good. Export earnings amounted to \$3,467 million as compared to \$1,941 million in 1978. Peru's (banking system) net international reserve position increased by \$1,486 million as a result of higher export prices and the negotiated reduction in external debt service. The current prospects for Peru's external accounts can be viewed as relatively normal for the early 1980s, particularly if export earnings do not decline. Even with the sharply increased export earnings, the Central Bank's present cash foreign exchange position (about \$1.0 billion) does not appear so substantial when set against a total external debt of \$8.8 billion (end of 1978) and a GDP of \$12-13 billion.

At present the outlook is for upward movement of real urban incomes. We expect a moderate increase in 1980 (4% to 7%) and probably a more impressive increase in 1981. However, we do not expect a return to pre-recession norms for real wages and employment until 1983-84. As the rate of inflation declines, urban finance institutions should also be able to return to a positive interest rate structure. When this occurs, GOP subsidies to shelter finance institutions which are now used to cover cash flow losses, can be reallocated to programs that impact on the needs of low income families.

Peru held a general election in May of 1980, and the new government is to take office July 28, 1980. This represents an opportunity for substantial changes in the GOP's longrange urban plans as well as inevitable changes in the way the sector is organized to respond to the growing urban pressures.

#### An Urban Strategy

The Mission does not anticipate new urban initiatives until a major consolidation has occurred in the leadership. But sometime in FY-80 it is anticipated that the new government will begin to articulate its urban strategy. In the meantime, the Mission's interim urban strategy is as follows:

- a. Emergency Measures: Assisting the urban poor through multisector Food for Work projects administered by PVO's and generating employment opportunities through infrastructure projects;
- b. Infrastructure Models: Continuing the financing of basic infrastructure projects to support the evolutionary upgrading of low-income urban settlements. When the revenue position of the government has improved, the HG infrastructure projects are seen as ways of providing models that can be replicated by both the public and private urban finance institutions;
- c. Absorptive Capacity: Increasing the number of institutions providing basic services to the poor, so as to increase the flow of resources into the sector and thus strengthen and expand the basic services delivery system;

d. Decentralization: Encouraging the GOP to continue the trend toward decentralized planning and improving project preparation capabilities of regional planning institutions; establishing a mechanism for financing productive market town and rural infrastructure in the sierra and high jungle; and serving as a pilot development effort for eventual replication in other areas of Peru;

e. Credit for the Urban Poor: Designing a credit project with an appropriate GOP entity to seek to increase income and generate new jobs for entrepreneurs located in low-income neighborhoods.

As soon as it is feasible, and in connection with the negotiation of 527-HG-011, the Mission will encourage the new government to organize a major review of its urban growth plans and programs so as to move from an emergency-type program to longer range development programs. The Mission is optimistic about the opportunity to work with the new government in developing ways to more effectively deliver basic services to the poor. Urban development policy will be a crucial area for the new government and for foreign assistance donors. Both AID and the IBRD support the convening of the Peru Consultative Group as soon as possible after the new government is formed. This body should encourage the GOP to develop a more comprehensive urban development policy, including the definition of investment programs to which aid donors can rapidly respond.

It is anticipated that several of the long-term shelter issues posited in the FY-80 HG PID guidance cable (e.g., the erosion of the financial base of the housing system; insufficient GOP budgetary allocations to the sector) will only be resolved with increases in urban sector real incomes that will accompany projected improvements in the overall economic conditions of the country. It is believed by the Mission that very little in the way of addressing long-term development issues can be accomplished without this recovery.

The Mission and IBRD are currently working on a complementary list of issues to be discussed with the new government. The outcome of the joint dialogue will set the stage for an international donors longrange loan and technical assistance program for the urban sector. The following briefly lists the Mission's list of initial issues to be discussed.

#### 1. Emphasis on Basic Services

Concern has been expressed over the lack of financing for low-cost housing. We view this problem in terms of the current lack of effective demand for such housing. The Mission has and will continue to discourage the financing of low-cost housing projects until real incomes permit the purchase of dwelling units on a cost recovery basis. In the meantime, the Mission will encourage the GOP to continue to finance basic communal services that are affordable to the target group as well as the provision of credit to facilitate self-help construction and/or improvement of dwellings.

#### 2. Reducing Standards

In connection with the neighborhood upgrading process, the Mission has established a Condition Precedent to 527-HG-011 (FY-80) that the BVP, with appropriate GOP entities, will conduct a study and make recommendations on construction standards and costs to ensure that the lowest cost appropriate technology is being employed in GOP supported shelter programs. HG loan funds will be utilized to finance a portion of this study. The intent of this exercise is to encourage a redefinition

of standards that will permit a greater participation of lower income people in the GOP's shelter programs.

### 3. Strengthening the Management Capability of the Sector

Recent evaluations of the shelter institutional performance have identified a series of management problems that need to be addressed by the Government. These include: (a) the need to develop an institutional outreach capability to deal directly with the needs of the target group; (b) the need to promote and improve coordination among project implementers; (c) the need to strengthen the cost recovery procedures of urban projects; and (d) the need to speed up project design and implementation process in order to reduce the impact of cost increases on project beneficiaries. The Mission through its on going and proposed shelter programs will be able to assist the Housing Bank and others address these issues.

### 4. Targeting Subsidies

The level of subsidies provided to the housing finance system is substantial. In CY-79, for example, the Bank and the S&Ls received \$8.0 million to cover losses associated with their frozen portfolios. Overtime, it is anticipated that improvements in the overall performance of the economy and the ability of the GOP to control inflation will lessen the need for the level of subsidy presently being injected into the housing finance system. It is also clear that the S&L system, for one, is aware of the danger of continued reliance on this form of subsidy and is anxiously awaiting to seek the new government's support in devising a maintenance of value system for the S&L's long-term investment portfolio.

Another form of GOP subsidy that is more directly impacting on the target group has been the extension of government guaranties to secure foreign credits and through the assumption of the exchange risk. To date, the GOP has paid out approximately \$6.9 million for exchange rate losses on external loans. The Bank projects that the GOP will need to contribute annually \$2.6 million in CY-80 and 81 to cover the exchange rate losses on the existing external loan portfolio. Through this allocation process, the GOP has been increasing its resource allocation to lower income families. The question that now must be addressed is the willingness and ability of the GOP to continue to cover the exchange losses for the proposed HG programs.

### 5. Solving the Deficit

Despite the budget austerity program of the Central Government, Peru's contribution beyond subsidies to the shelter sector has been on the rise. The Central Government allocated \$49.8 million in CY-79 and \$42.5 million in CY-80 for shelter related services. The Mission will work with the GOP to determine the extent to which this support can be utilized to meet present and projected shelter related deficits. Beyond budget allocation to the sector, what can the GOP do to solve the existing and projected deficits?

### Types of Projects Proposed for Perú

In FY-80, the Mission will continue to work with BVP given its thorough familiarity with the HG program, its extensive on going basic services program in pueblos jóvenes and the likelihood that its programs will be less impacted upon by changes in government than other institutions. It should be noted that although the BVP has \$10 million in escrow (527-HG-009(II)) and access to a new \$15 million

project involving the S&Ls (527-HG-010), the Mission is confident that BVP will be able to disburse funds in a timely fashion. In the first instances BVP has requested a \$3.0 million advance which should be ready for Mission approval shortly. In the meantime, it has advanced its own funds to undertake the construction financing of most projects proposed for 009(II) HG financing. 010 has been delayed pending the new government's review and approval of the new project. We anticipate rapid disbursement on this project given the projected local demand expressed by participating S&Ls.

A \$25 million FY-80 HG PID has been approved by the Bureau. It is understood by LAC and DS/H that the Mission wants a second \$25 million authorized for similar purposes in FY-82. The FY-80 PP, developed in the 3rd. quarter of FY-80, will permit the BVP to continue to provide a minimum level of financial assistance to low income people for water, sewerage and electricity services, plus the possibility of financing related community facilities such as schools, health posts, markets, etc., in pueblos jóvenes and similar communities. The BVP would also be permitted to lend for home improvements loans in low-income settlements.

In FY-80, the Mission will be implementing a multisector public works program in Lima. An OPG with CARE in conjunction with Title II food, and Title I local currency, will be used to support MVC, and the Ministries of Education and Health deliver services into the Pueblos Jóvenes. This combination of resources will finance the purchase of construction materials and provide food for work to build basic community facilities and services. The project is designed to deal with extensive unemployment and malnutrition found in low-income neighborhoods of Lima. DS/H's IIPUP resources are to be used to hire local consultants who will work with MVC in the development of studies and comprehensive plans for selected areas. IIPUP is also to provide short term US consultants to assist in development of the framework for these studies and plans.

In FY-81, the Mission is considering the possibility of another basic services HG Loan (012) for the S&L system, but this will depend on the outcome of an evaluation of the FY-79 HG program. It is possible that as the economic situation in Peru improves, S&Ls presently involved in our program may return to their traditional middle class clientele. This may be further facilitated by the proposed access of FONAVI funds by the S&L system to generate middle income housing.

The PP may consider, instead, the feasibility of channeling HG resources through BVP, and/or BANCOP to finance a credit union program of home improvement and home expansion loans. Credit unions identify 20% of their loan portfolio for home improvements. A number of these organizations know and deal with the lower income people and could be used to increase the level of credit assistance reaching low-income people. A Mission OPG (LOP\$575,000) will be used to support the implementation of this activity.

The Mission will also consider ways to develop a project idea that would provide a credit program for small businesses in Pueblos Jóvenes. The purpose of this activity would be to increase credit available to small entrepreneurs in an effort to increase incomes and generate new jobs for businesses located in low-income neighborhoods.

In FY-82, depending on the experiences of the Integrated Regional Development Loan Project, the Mission proposes to increase the percentage of HG resources supporting the GOP's decentralization programs. A HG Loan with BVP would address the deficits of basic services with an increased attention to the infrastructure needs of secondary urban centers throughout the country. The design of this

tranche will be based on an indepth evaluation of the BVP's decentralization experiences.

A related grant activity (LOP \$750,000) has been proposed to strengthen the responsibilities and capabilities of municipal government in the decentralization program.

#### Areas for Technical Assistance

FY-80. It is felt that only limited technical support to BVP will be required to implement the proposed basic services and facilities HG program (527-HG-011). The purpose of this technical support will be to further strengthen BVP's on-going efforts:

a. The Mission and BVP will work jointly in the installation of an evaluation system that will systematically review progress made on implementing the HG program;

b. With use of limited HG loan resources, BVP in close collaboration with implementing agencies and related normative ministries, will conduct a study on and make recommendations for construction standards and costs to ensure that the lowest cost appropriate technology is being employed in HG projects.

c. The Mission will work with BVP to ensure the inclusion of sound environmental planning for HG financed projects.

In addition, DS/UD is providing the Mission with consultant services to work with BVP and Ministry of Housing on a study to evaluate the role the construction industry (formal and informal) plays in the generation of employment opportunities for unskilled, low-income workers. This study will provide the basis for an employment generation component of a National Shelter Plan.

The Mission will also have access to a DS/H financed OPG resident technician who is completing his work with the BVP on the home improvement program.

DS/H IIPUP resources will also be available to the Mission in FY-80 to strengthen GOP's efforts to develop comprehensive plans and studies of the Pueblos Jóvenes, the low-income areas that surround Lima.

Development loan 063 will provide funding (through FY-83) for the following TA efforts related to implementing USAID's Integrated Regional Development Project:

a. Two Market Town Development Planners to assist the development committees of Junin and Cajamarca select and design basic urban infrastructure projects.

b. Various US and Peruvian advisors who will work with municipal governments to strengthen their role in the decentralized development process.

FY-81. The Mission has tentatively proposed resident technical (OPG) advisor to work with the BVP in the design and implementation of a home improvement program to be implemented by the credit union movement of Peru. (LOP \$575,000)

Depending on the outcome of the initial MWC planning efforts in the Pueblos Jóvenes, further IIPUP support may be requested. (LOP \$300,000)

In FY-81, the Mission has proposed a small business credit program that will include a technical assistance component. The terms of reference of this effort and its costs have yet to be defined.

FY-82. The proposed FY-82 527-HG-013 stress the importance of investing a greater share of HG resources in the secondary urban centers of Peru. The Mission has proposed a grant program (LOP \$750,000) that would complement this HG activity by strengthening the capability of Municipal government to design, implement and recover the costs of basic urban service projects.

Drafted by: Paul G. Vitale, Chief, UDD PA

Clearances: DR:Lee Twentymar \_\_\_\_\_ DD:Howard Lusk HLK

Approved by: Leonard Yaeger, Director LY

UDD:6/30/80

AID Support to Peru's Urban Sector

<u>Activity No.</u>	<u>Project Activity</u>	<u>Source</u>	<u>Amount (LOP)</u>	<u>Authorized Prior FY 80</u>	<u>FY 80</u>	<u>FY 81</u>	<u>FY 82</u>	<u>FY 83</u>	<u>FY 84</u>
009(I)	Low Income Housing	-- HG	15,000	15,000					
009(II)	Low Income Housing	-- HG	10,000	10,000					
1583	Home Improvement (TA)	DS/H DG	191	91	90				
063	Integrated Reg. Dev.	USAID DL	8,000	8,000					
0178	IRD (TA - urban)	USAID DG	523		48	227	228	20	
0186	Urban Feeding Program *	USAID DG	793		300	250	243		
0007	PPJJ Planning (TA)	DS/H DG	300		100	100	100		
010	Basic Services PPJJ	-- HG	15,000	15,000					
011	Upgrading Low Income Settlem.	-- HG	25,000		25,000				
012	Non traditional Credit <del>(TA)</del>	-- HG	25,000			25,000			
0218	Credit for Low Income Fam. (TA)	USAID DG	750			200	200	200	175
013	Decentralization of Services	-- HG	25,000				25,000		
0239	Municipal Development (TA)	USAID DG	750				200	200	200
0241	Urban Small Businesses	USAID DL	5,000				5,000		
014	HG to be defined	-- HG	25,000					25,000	
-	TA Support	USAID DG	750					200	200
015	HG to be defined	-- HG	25,000						25,000
-	TA Support	USAID DG	750						200

\* Plus PL 480 Title I + II