Evaluation of Loan No. 527-T-058

Centrales de Cooperatives

Office of Agriculture
and Rural Development
USAID/Peru
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INTRODUCTION

The Central Development loan was signed in September 1976. The project objective is to increase the capacity of the Centrals to provide economic services to their member cooperatives. The loan had three elements: technical assistance to the Ministry of Agriculture, the preparation of Development Plans for each Central by private consulting firms under the direction of the Ministry of Agriculture, and loans to the Central to finance projects identified in the Development Plans. Funding provided for $1.1 million for technical assistance and Development Plans and $5.9 million to finance projects.

Progress on the loan has not been satisfactory. The terminal commitment date passed July 25, 1979. No funds have been invested in projects. Less than twenty percent of the funds for technical assistance have been allocated. Drafts of fourteen of the Development Plans are being reviewed by the Ministry of Agriculture and six are uncompleted. The quality of the available Development Plans is not adequate for making investment decisions.

Faced with the lack of quantitative and qualitative progress on the loan and the approaching terminal commitment date, the USAID/Peru Office of Agriculture and Rural Development initiated a thorough evaluation of the loan. The evaluation focuses on two issues:

a) the viability (or potential viability) of the Centrals as an institution for providing agricultural services to affiliates; and

b) the general inadequacy of the Development Plans, both in terms of the slow progress and their quality.

Two Peruvian consultants and one U.S. consultant worked full time on the evaluation. A third Peruvian consultant worked part-time. Various AID/Peru employees also participated in the evaluation. The evaluating group visited each of the twenty Centrals in the project, as well as, affiliated cooperatives. At each site discussions with the Agrarian Bank, the Ministry of Agriculture, and competing suppliers of agricultural services were held. Representatives of the Agrarian Bank and the Ministry of Agriculture accompanied most of the field visits.

Communication with the Agrarian Bank was important, not only to exchange ideas and information, but to reach an understanding on the main points of the restructuring. The Ministry of Economy and Finance and the Ministry of Agriculture were also involved in these discussions. As yet, full agreement on two basic points have not been achieved: the proposed increased role of the Agrarian Bank and the use of a capital donation. Discussion of these issues is continuing.

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BACKGROUND AND GENERAL CONCLUSIONS

The Centrales de Cooperativas are secondary level cooperative organizations charged, by law, to provide a variety of social, technical, and economic services to member cooperatives. The purpose of the loan has been, and remains, to increase the capacity of the Centrales to provide services to their afiliates and, at the same time, to increase the financial viability of the Centrales. This objective implies the development of the Centrales as cooperative businesses, oriented towards the efficient provision of economic services to the primary level cooperatives. To achieve this end, the loan provides for technical and financial assistance to no more than twenty selected Centrales. The total amount of the loan is for $7 million. The loan is split into three parts in the following manner:

(a) up to $100,000 for contracting technical assistance in planning, implementation, and evaluation;

(b) up to $1,000,000 for the elaboration of "Development Plans" by private consulting firms;

(c) the remaining $5,900,000 establishes a Central Development Fund in the Banco Agrario to finance working capital, fixed assets for provision of services, and investments in agro-industrial projects.

The GOP counterpart is of $7 million for short-term lending to Centrales and to their affiliated cooperatives. Thus the total amount in the Central Development Fund is $12.9 million.

The present status of the different elements is shown in Table 1.

TABLE 1

Financial Status, Centrales Development Loan

as of May 29, 1979

	Amount	Committed
Technical Assistance	$100,000.00	11,288.00 *
Development Plans	$1,000,000.00	600,000.00
A.I.D.	$5,900,000.00	-.-
GOP	$7,000,000.00	-.-

* As of April 30, 1979.

The loan agreement was signed September 29, 1976. The terminal commitment date for expenditures is July 25, 1979 and the terminal disbursement date is six months later, January 25, 1980. It will not be possible to achieve the purposes of the loan in the remaining six months.

The lack of progress evident in the above figures is the principal reason for this evaluation. The alternatives that may be considered are essentially three:

(a) de-obligate the remaining portion of the loan, under items 8.03 and 8.04 of the loan agreement;

(b) continue operating under the existing structure and procedures with extended termination dates;

(c) incorporate changes in the existing structure of the program that would enable the objectives of the program to be realized as

rapidly as possible within an extended time period.

The selection of one of these alternatives depends upon a variety of factors. The case for de-obligation of the loan requires an analysis showing that (a) the Centrales are not a viable system for providing services to their members; (b) that the outputs achieved to date (i.e. the development plans and project studies) and the ongoing work is of little practical value; and (c) that neither a restructuring scheme nor the present structure can be expected to achieve the program results in a reasonable period of time. The case for continuing under the current procedures can be made, despite the actual lack of progress, if it can be shown that the lack of progress is not the result of the existing procedures, but is due to bad luck and/or unforeseen exogenous problems that are unlikely to be repeated. At the same time, it would have to be shown that (a) the Centrales are a potentially viable institution for providing services and (b) that the outputs of the completed and on-going work are satisfactory. Specifically, the worth of the completed studies must validate the existing procedures. The argument for restructuring the program would have to be made on the following grounds: (a) the Centrales are a potentially viable means of providing necessary services to the member cooperatives; (b) that the studies are of value; and (c) that the restructuring can be achieved at a relatively small cost in time and resources.

The general conclusion of the evaluation is that the Centrales de Cooperativas are worth support. Some Centrales, Chincha and Puno for

example, are providing a significant level of services to their members. Others, such as Tumbes and Tacna, have the potential to develop into strong cooperative businesses. On the basis of written reports and field visits to each of the Centrales there is strong reason to believe that a significant portion of the original twenty (20) Centrales can use the financial and technical assistance in a productive manner. Second, while the studies, in almost every case, are not adequate for making investment decisions, they can provide a basis for developing sound projects. Thirdly, a restructuring of the loan can eliminate the delays inherent in the current procedures and lead to the development and financing of sound projects in a relatively short period of time.

The strategy of the restructuring procedure is based on the following observations:

(1) a recognition that, with few exceptions, the Centrales are relatively weak organizations both managerially and financially, presently incapable of handling large agro-industrial projects;

(2) that the procedures for supervising and revising the work of the consulting groups by the Ministry of Agriculture have not been sufficient to ensure high quality project studies;

(3) that the basic problem of the studies is a failure to reflect realistically the situation of the Centrales and the cooperatives in their local economy.

(4) that the project is currently entering the implementation phase in which the crucial problems are those of revising the projects to reflect the local situation more adequately and developing the projects to a state where bank financing is possible;

(5) that some of the Centrales are not potentially viable institutions for providing services to their members.

These considerations suggest a restructuring on the following lines:

(1) A greater role for the local institutions (Banco Agrario and Central) in the revision of the completed studies and the supervision of the on-going studies. This capability will be made effective by providing technical assistance directly to selected Centrales;

(2) Lower the cost of human and financial resources available to selected Centrales by providing a capital donation to partially offset start-up costs in the provision of new or expanded services.

(3) Increased flexibility in the procedures for the evaluation and approval of projects, to move sound projects more quickly into the implementation stage.

(4) Increase the capitalization of the Centrales by linking the capital donation to increased financial support from the base level cooperatives.

These are the basic elements of the proposed program restructuring. A more detailed analysis of the reasons for these changes and a description of how they are expected to work is provided in the remainder of the evaluation.

The evaluation report is devided into three sections: (a) a general description of the current procedures and a presentation of the current state of the program; (b) a comparative evaluation of the Centrales; (c) recommendations for restructuring.

Project Description

The project involves three elements:

(a) increased technical capacity within the Ministry of Agriculture to assist in the supervision and direction of the Development Plans;

(b) contracting private consulting firms to supply Development Plans for each of the twenty (20) Centrales;

(c) a Central Development Fund to finance sound projects identified and elaborated in the Development Plans.

Three years after signing the loan agreement, only the studies portion of the project has been implemented. No projects have been approved or financed. As the figures in Table 1 show, the increase in technical capacity has been minimal.

The technical assistance funds have been used to hire one person during the development of the terms of reference for Development Plans. Presently, there are two persons working in the Ministry under these funds. The funds have also been used to cover operating expenses - gasoline and travel for example. Currently, six (6) persons in the Ministry (including the two contracted under technical assistance) are working full time on the project. An additional ten persons

have been approved for employment by the Banco Agrario and A.I.D., and are awaiting final approval within the Ministry. The initial tasks of those contracted under technical assistance were to assist in the preparation of the Development Plans and other activities related to project planning, implementation, and evaluation.

The work by the consulting groups on the studies is continuing. The twenty Centrales were divided into three groups, shown in Table II. The consultants are required to provide an evaluation ("diagnostico") of the Central and its affiliates based on field work, a Development Plan, and a set of six project studies. In the first two groups of studies, the consultants were required to develop two studies each to the levels of definitive, feasibility, and prefeasibility. The ranking was based on the desire of the Central rather than on expected feasibility. In the third group, a change was made to require a pre-feasibility study of six projects and to develop definitive studies from the expected most profitable projects. Payments to the consultants is based on the basis of approval of study documents in the following manner:

(a) on approval of the "Diagnostico" - 40% of the contract total.

(b) on approval of the first draft Plan de Desarrollo, 40%.

(c) on approval of the projects, 0

(d) on approval of the draft of the final Plan de Desarrollo, 10%.

(e) on approval of the final Plan de Desarrollo, 10%.

Advances made to the consulting groups have the effect of paying them 84% of the contract totals on the basis of the first two documents.

TABLE II

GROUPING OF CENTRALES

Group 1	Group 2	Group 3
Chiclayo	Pisco	Urubamba
Ica	Cajamarca	Guadalupe
Chira	San Lorenzo	Tarma
Chincha	Tumbes	Huancayo
Huaral	Tacna	Cerro de Pasco
Cañete	Puno	Medio Piura
	Andahuaylas	
	Majes	

While the Diagnóstico is self explanatory, the process of making the Development Plan requires explanation. The first draft Plan de Desarrollo (Estructuración del Plan) is relatively short document, bringing together from the diagnóstico the major problems of the Central and identifying, as project profiles, the projects and programs tentatively designed to solve those problems. Based on this, a ranking of projects is made and the projects are developed to the levels indicated previously. The final Plan de Desarrollo is based on the six projects developed.

At each step, the work of the consultants is subject to revision by the Ministry of Agriculture. This revision is based on comments received by the Ministry from the Comite Local (composed of the manager

of the Central, a technician from the regional or zonal office of the Ministry, and a technician from the local Banco Agrario), comments from the technical staff of the Lima office of the Banco Agrario, and comments from the project evaluators in the Ministry. The comments from the Comite Local and from the Banco Agrario are channeled to the Ministry in Lima. The Ministry enters into direct communications with the consulting firm to resolve any outstanding issues. Payment to the consulting firm is made when (a) all outstanding issues are resulved by the consultant, the Ministry authorizes payment and (b) the Comite Local expresses its agreement (conformidad) with the document. The Ministry's request for disbursement is sent to the Banco Agrario, and the Banco, as the implementing agency, requests the disbursement from AID.

CURRENT STATUS

Table II indicates how far along the Ministry is in revising the project documents of the first two groups of studies. To date, only the study for the Central of Chira has passed through the revision process in the Ministry.

The reasons for the slow progress are numerous. The principal problems are:

(1) lack of staff capacity in the Ministry to review the studies, because of the failure to contract technical assistance,

(2) concentration on architectural, agronomic, and engineering details in some projects;

(3) lack of knowledge about local potentials and constraints.

If, at the end of the revision process, there were an assurance of an adequate project study, it would be a relatively simple matter

Table II - STATUS OF DEFINITIVE LEVEL PROJECTS
AS OF June, 1979

Central	Date of Presentation of first document	Status
FIRST GROUP		
Chira/Piura		
Animal Feed Plant	10/10/78	M.A. approved 6/79
Marketing	10/ 2/78	M.A. Approved 6/79;
Huaral		
Marketing Inputs	9/15/78	Pending
Ag. Machinery	9/15/78	Lack of progress
Chiclayo		
Administrative Training	11/ 3/78	Lacks Economic-Financial Analysis*
Machine parts pool	11/ 3/78	Lacks Economic-Financial Analysis
Ica		
Agricultural Machinery	10/31/78	Lack of progress
Input Marketing	10/ 3/78	Pending
Cañete		
Ag Machinery	11/ 7/78	Lack of progress
Technical Assistance	9/ 7/78	MinAg approval
Chincha		
Technical Assistance	11/30/78	Pending
Input Marketing	12/ 6/78	Pending

* Approved by MinAg despite lack of significant documentation.

SECOND GROUP		
Tumbes		
Machinery Repair	2/15/79	Pending
Banana Marketing	3/15/79	Pending
San Lorenzo		
Technical Assistance	6/15/79	Pending
Input Marketing	4/15/79	Pending
Cajamarca		
Machinery Repair	3/15/79	Approved by MinAg
Input Marketing	3/15/79	Pending

Central	Date of Presentation of first document	Status
Pisco		
Machinery Services	6/15/79	Pending
Input Marketing	4/15/79	Pending
Majes		
Rice Processing	-	Lack of progress
Input Marketing	4/15/79	Pending
Tacna		
Olive Marketing/Processing	6/15/79	Lacks Economic-Financial Analysis
Input Marketing	-	Lack of progress
Puno		
Rehabilitate Slaughterhouse	4/15/79	Pending
Wool Marketing	-	Lack of progress
Andahuaylas		
Machinery Services	5/15/79	Lack of Progress
Marketing Services	5/15/79	Pending

to increase the staff capacity and quality to move projects along more quickly.

The evidence to support this is not encouraging. The studies for Chira, which are acceptable to the Ministry and are the most advanced, provide an example. A brief review of the two definitive studies suggests serious deficiencies. The first project is for the marketing of agricultural inputs. Both the manager of the local Banco Agrario and the head of the Zonal Office of the Ministry expressed doubts about the project. The demand projections are unsubstantiated and unlikely to be realized. They assume, without justification, that the Central will almost completely replace the existing private firms as input suppliers. Some of these firms, notably Romero, are unlikely to desappear. The main income producing activity is fertilizer sales, but the margin is misrepresented as six percent when in reality it is at most two percent. The required reduction in the demand estimate together with a reduction in the profit margin forces a thorough revision of the project. The second project is for the production of animal feeds. Discussions with existing feed producers raise the likelihood that there is an underutilized capacity in the region. As the study does not explore the reasons why current capacity is not fully utilized, the proposed investment should be considered doubtful. In short, it has been one year since the basic data for the projects were collected. After eight months of review, basic questions remain unresolved. The revision process, despite the length of time taken, has failed to produce projects that withstand a brief economic-financial analysis. Further, a page by page comparison of the final document with the original draft document does not indicate any substantive changes in the project document. The Comite Local communicated to the Ministry that the demand

projections for the marketing project seemed inflated. This is not reflected in the final document. This suggests that the Ministry has not been able to effectively direct or control the work of the consultants. Further evidence of this failure is that, while the consultants were required to establish and maintain a staff capacity in the area, this requirement has not been enforced by the Ministry. The consultants, with few exceptions, have maintained minimal staff in the areas studied. The two definitive project studies submitted by the consultant for the Central in Chiclayo lack an enconomic-financial analysis. This deficiency has not been corrected during the seven months of revision.

The revision process is being undertaken in a somewhat unreal or abstract manner, in which projects are being reviewed without reference to the actual conditions of the Central that is going to implement the project. For example, the Ministry has indicated that the agricultural machinery project for the Central in Cajamarca is well advanced. Yet the Central there is in disarray, largely because of its inability to handle a large infrastructure of donated agricultural machinery. The analysis of the project cannot, or should not, be divorced from an understanding of the current situation of the Central.

The three significant problems in the revision phase are, then:

(1) the time required to revise the studies in the Ministry;

(2) the failure of the revision process to produce adequate project studies;

(3) the apparent inability of the Ministry to enforce its control over the consulting groups.

With increased staff capacity in the Ministry it is possible that the review procedure could move more quickly. But this also depends on the ability of the Ministry to control the work of the consultants (set and enforced completion dates, for example). The general control mechanism that the Ministry has over the consultants to enforce compliance is to withhold payment. However, the consultants have already been paid eighty-four percent of the contract total. The ability of the Ministry to enforce compliance is therefore greatly limited. Also, perhaps more important, the Ministry has not demonstrated the will to exercise control over the consultants. Simply increasing the capacity of the Ministry is unlikely to speed up the revision process or improve the quality of the studies.

In short, despite the time taken in to revise the project studies, the revision process has not resulted in sound plans and project feasibility studies. This process is the cause of the lack of progress in the loan. The revision process in the Ministry of Agriculture should be terminated in a rapid, orderly fashion to allow the Centrales to redo and make adequate specific projects for bank financing. Annex 1 provides a suggested procedure for accomplishing this objective.

EVALUATION OF THE CENTRALS

Members of the evaluation team visited each of the twenty Centrals in the program. Generally, at least two members of the group went to each site for two days. In the majority of the cases, representatives of the Banco Agrario/Lima and the MinAg/Lima accompanied the evaluators. In the course of the two days, the evaluators interviewed local representatives of the Banco Agrario and of the Ministry, the Central manager and technicians, administrators of some of the member cooperatives, and managers of private firms that compete with the Central. The inverviews focused on three related issues:

(1) to what extent did the consultants work with the local representatives and Central in the various project steps: analysis of problems, identification of projects, design of projects;

(2) what are the current problems and potentials of the Central -- what is it doing, how well is it managed, its relation to the base level cooperatives, etc.

(3) are the projects, as designed by the consultant, feasible and within the capacity of the Central to manage?

The responses to each of these lines of questions tend to fall into similar patterns from which the following generalizations are not misleading:

(a) the consultants worked in the local area and in collaboration with the Central during the phase of problem identification and data gathering for the "Diagnostico". Once completed this phase, the presence of the consultant in the local area has been minimal. The participation of the local groups in the design of the projects has been practically nil. In most cases, the manager of the Central has only come to know the size and scope of the projects after the project study had been largely complted. Having the MinAg contract consultants to do a study for the Central distorts the client-consultant relationship and has led to the consultant ignoring the Central and working directly with the Ministry. This is the reason why many of the Centrales have been unsatisfied with the projects.

(b) the base level cooperatives know very little about the proposed projects. The consultants prepared questionnaires to get quantitative information from the cooperatives, but did not, in most cases, spend much time with the affiliated cooperatives.

(c) the Centrales, local Agrarian Bank, and Ministry officials continue to have important reservations about many of the projects. These reservations concentrate on two issues: the scope of the projects are too large and the ability of the Central to get the support of the base cooperatives is overestimated.

(d) the Cetrales are relatively weak organizations. They are presently offering few services, generating little profit, and are woefully undercapitalized.

FACTORS LIMITING THE DEVELOPMENT OF THE CENTRALS

The factors constraining the growth of the Centrals can be broken into external and internal constraints. The internal constraints can be affected by the kind and quantities of investments made under the loan. The external factors are largely unaffected by the loan. The two are, of course, related: better management (an internal factor) may allow the Central to meet the private competition (an external factor) more effectively. At the same time, it must be recognized that strong private competition in the area is not going to disappear.

The external factors are of various types, of which the following are most important:

(1) Competition within the local economy from the private sector. This appears particularly strong on the coast where private sector activity in the marketing and distribution of the principal inputs and outputs has developed strong ties with the cooperatives and with the financial institutions. Private firms handle most of the sales of pesticides used in cotton production for example.

(2) Competition within the local economy from state institutions. ENCI and its agents handle all fertilizer sales; ENCI purchases all the cotton production; EPSA purchases all rice production; the sugar cooperatives purchase and process all sugar production. As these are the principal inputs and outputs of coastal agriculture, the activities the Central can undertake are greatly reduced.

(3) State regulated fixed margins on processing and resales of commodities reduces the profitability of many activities. Fixed margins are established on the resale of molasses, the resale of fertilizers, and on rice milling. In the case of fertilizers, the joint effect of state competition and fixed margins results in Centrals receiving a net margin of less than two percent on sales, not including the administrative costs of managing the activity. For the activity to be profitable with this margin requires a large volume of business. Existing competition makes it difficult for the Central to achieve this volume. Discussions with rice millers indicate tha the current margin is not sufficient to generate profits, but black market sales are profitable due to the current shortage of rice. The state has established a variety of institutions and policies designed to reduce or eliminate supposedly excessive middleman profits. The Central is a middleman and its profitability is affected by those policies.

(4) The maintenance and repair, of agricultural machinery is one unregulated area of activityfor a Central. Machinery is widely used in coastal agriculture and observation suggests that much of the machinery is in a state of disrepair. The problem, however, appears to be a lack of replacement parts rather than maintenance problems. The lack of parts is the result of import controls and lack of foreign exchange.

(5) The diversity in the size of the affiliated cooperatives also affects the development of the Central. Some large cooperatives have the infrastructure and sales volume to act as a Central in their own right. Cooperaties such as Mallares in Piura and Sta. Margarita in Ica quite simply have little need for an intermediary in sales, machinery repair, or commodity processing. Evidence of the inability of coastal Centrals to integrate their functions with the cooperatives is given by considering the services they presently offer. In Chira, Ica, Huaral, Cañete, Chincha, and Pisco a major portion of their commercial business is tied, not to the cooperatives, but to small and medium sized private producers. Huaral, Chincha, Ica and Cañete collect cotton from the private producers. The largest part of consumers of machine services from the Central in Pisco are small producers. Huaral, Chincha, and Ica sell production inputs to small private producers. The elimination of middleman profits has been designed for the large production cooperatives. The coastal Centrals, unable to find economic activities within this system, have encountered a lack of services provided to the small producers and have developed commercial ties with this sector.

(6) The lack of profitability of the cooperatives until recently has constrained their demand for the services of the Central. The well managed cooperatives view the Central as one of many alternative service suppliers. The cooperatives generally stated that they would utilize the services of the Central as long as the service was a timely and less expensive than alternative suppliers. A number of Centrals have attempted to secure input marketing arrangements with the cooperatives. None has been successful, because the cooperatives prefer to have a variety of alternative service suppliers. This makes economic sense. Also the

cooperatives experience with state monopolies (ENCI, EPCHAP, EPSA) has not always been satisfactory and they maintain doubts about the Central. Further, the competition among alternative suppliers leaves room for bribery, which many knowledgeable persons suggest as an important constraint on the ability of the Central to begin marketing activities.

(7) The economic potential of the local economy constrains the type and volume of activities the Central can develop. In the sierra areas of Tarma and Huancayo small and medium sized independent producers are the mainstay of the agricultural sector. The cooperatives are less important. In those areas, the Central is linked to the cooperatives while the private producers are serviced by private firms (Huancayo) and a "Cooperativa Agraria de Servicios" (Tarma). As the base cooperatives are weak, so the potential of the Central is low. This presents an interesting phenomena: When the base cooperatives are relatively strong, the Central is weak; similarly when the base cooperatives are weak, the Central is also weak.

The internal constraints on the Central center on a lack of capitalization, in the broad sense of the terms "Capital". The following factors appear important:

(1) The lack of financial resources required to provide timely, efficient services. Few Centrales have received bank loans to finance marketing services. They lack the resources to carry out the activities fromtheir own sources or lack the assets on which to borrow the money.

(2) A lack of technically capable persons to manage the Central. Generally, the Centrals are one or two man operations. In most cases we found the managers to be competent, but there are limits to what one person can accomplish. Support from the local Ministry and Agrarian Bank

is limited.

(3) Provision of services at a financial loss to the cooperatives. This is particularly true where the Central is engaged in supplying agricultural machinery services -- Medio Piura, Cajamarca, and Pisco are clear examples. These Centrales are decapitalizing the little capital they own.

(4) A number of the Centrales suffer from a bad image. The Centrales were imposed on the cooperatives with, in some cases, considerable fanfare about what they were supposed to accomplish. Given few resources, they have been unable to accomplish the original objectives. Second, they have made some notable mistakes. Both factors have made the cooperatives doubtful about new ventures.

There are , then serious constraints on the development of the system of Centrals. At the same time, the evaluation identified a number of Centrales that had overcome many of the constraints and offered productive investment potential. To more systematically identify those Centrales and offer a guide to placing priorities on the Centrales a comparative evaluation of the group was conducted. The evaluation is in large part subjective, based on the field visits and augmented by information taken from the "Diagnosticos". As the visits were short, the evaluators may have missed some factors -- internal rifts among the administration, problems between the Ministry and the Central, etc. There are important differences among the Centrals, however, and the summary evaluation is an attempt to sort those differences out.

The results of the evaluation are presented in Table 4. The evaluation is divided into three basic areas of comparison: organization, integration, and investment potential. Each is given equal weight.

Organization is divided into two sub-categories: administrative organization and cooperative organization. Administrative organization reflects the capacity of the Central to manage increased activities stemming from new investments. Cerro de Pasco, Chincha, and San Lorenzo receive high marks in this category. Cerro de Pasco has a dynamic manager, along with six to seven professionals working in specific areas; accounting, marketing, technical assistance (veterinary), and social services. San Lorenzo, in addition to a manager, has five professionals including an economist and three agronomists. On the other hand, Tarma and Majes are managed by part-time officials from the Ministry of Agriculture.

Cooperative organization attempts to indicate the degree of administrative integration between the Central and the cooperatives. This is manifest in a functioning Consejo de Administracion, Comite de Vigilancia, and the Asamblea de Delegados.

Integration attempts to identify the level and kind of relation between the Central and primary producers. Three types of interaction are considered: social integration, economic integration with affiliates, and economic integration with non-affiliates. A number of Centrales offer social services, such as health services. This activity is, in part, a means of capturing the goodwill of the cooperatives and may make it easier for the Central to gain the cooperatives support for economic projects. The Central, at least, has established a presence in the cooperatives. A high mark indicates an on-going social service project. An intermediate mark indicates an incipient project, a low mark indicates a lack of service project. The degree of economic integration is measured by the volume of business done by the Central with affiliates or non-affiliates.

An example of a high degree of economic integration with affiliates is the Central in Puno, which markets 90 percent of the wool production in the area. Other Centrales, such as Majes, Tarma, and Guadalupe have little or no ecommercial ties with local producers.

The final category is Investment Potential. This reflects a largely subjective judgment of the evaluators, taking into account the projects identified by the consultant and the capacity of the Central. The basic question considered is whether the Central has the potential to be linked economically to the principal growth activities in the region, either as suppliers of inputs or in marketing outputs. Puno is again an example of a high potential Central, because of its actual and proposed linkages to wool, alpaca, and meat production. San Lorenzo is linked to the rice and cotton production in the area, but because the area is small and not highly productive its potential is more limited. It is somewhat surprising that many of the coastal Centrals in highly productive valleys (Chira, Ica, Cañete, Pisco) receive relatively low marks. This is due to the importance of the external constraints imposed by the state on coastal agriculture and to the lack of integration between the Central and the cooperatives.

The results suggest the Centrals can be roughly divided in four groups. The first group of seven represent Centrals with relatively high potential for development. These Centrals could make productive use of loan funds to expand their activities. The second group of five has less potential, but appear to represent Centrals with a reasonable expectation of growth. The last two groups, of four and four, must be considere to be of low potential. The primary difference between the third and fourth groups is with respect to organization. Organization by itself, however, is not sufficient to support economic growth. Both groups should be given low priority for receiving loan funds.

CUADRO DE CALIFICACION COMPARATIVA

DE CENTRALES

CENTRAL	ORGANIZACION			INTEGRACION				POTENCIAL		PUNTAJE
	Administrativa	Cooperativa	Sub-Total	Social	Económico			Inversión		
					Afiliados	No Afiliados	Sub-Total		Sub-Total	
Chincha	A	B	9	C+	B	B	5	B+	9	23
C. Pasco	A	B	9	A	C+	C	5	B+	9	23
Puno	B	B	6	C+	A	C+	6	A	12	21
Huaral	B	B	6	C	B	B+	5	B+	9	20
S. Lorenzo	A	B+	10.5	A	B	C+	7	C+	3	19.5
Tacna	B	C+	4.5	C+	C+	C+	3	A	12	19.5
Tumbes	B	A	9	C	B	C+	3	B	6	18
Andahuaylas	C+	B	4.5	B	B	C+	5	B	6	15.5
Urubamba	C+	B+	6	C	B	C+	3	B	6	15
Chira	B	C+	4.5	C	B	B	4	B	6	14.5
Canete	B	C+	4.5	C	B	B	4	B	6	14.5
Chiclayo	B	C+	4.5	C	C+	B	3	B	6	13.5
Medio Piura	B	B	6	C+	C+	C	2	C+	3	11
Ica	B	C+	4.5	C	C+	B	3	C+	3	10.5
Pisco	B	C	3	C	C+	C+	2	C+	3	8
Cajamarca	C	B	3	C	C+	C	1	C+	3	7
Huancayo	C+	B	4.5	C	C+	C	1	C+	3	5.5
Majes	C	C	0	C	C	C	0	C+	3	3
Tarma	C	C+	1.5	C	C	C	0	C	0	1.5
Guadalupe	C	C	0	C	C	C+	1	C	0	1

Para el puntaje: A = 2; B = 1; C = 0; + indica medio punto adicional

Los pesos que se han dado son:

- Organización administrativa 3
- " cooperativa 3
- Integración social 2
- Integración económica con afiliados 2
- Integración económica con no afiliados 2
- Potencial inversión 6

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FINANCIAL STATUS OF THE CENTRALS

The major internal constraints on the Centrals are the problems of capitalization and the profitability of activities. To describe the magnitude of these constraints, a simple financial analysis of each Central was made, based on the most recent accouting information. The information available does not support a sophisticated analysis: the statements are not standardized, are not audited, and some of the convertions and definitions are elusive. The indexes utilized are the following:

(1) Profitability, defined as net profit/sales and net profit/assets.

(2) Solvency, defined as liabilities/assets. Because the Centrals lack measurable equity, total assets were used as the divisor.

(3) Liquidity, defined as current assets/current liabilities.

(4) Activity, defined as sales/assets.

The two important indexes are profitability and solvency. The rankings and calculations are shown in Annex 2. The Centrals generally have not generated profits. The solvency index indicates the extremely low levels of capitalization within the Centrals. The three highest ranked Centrals, Cajamarca, Chiclayo and San Lorenzo have relatively adequate indexes because of external donations of capital assets. Neither Cajamarca nor Chiclayo has generated profits from these donations. In Cajamarca, the donation of agricultural machinery has simple been ill used. In Chiclayo, the capital is just now entering into operation. Recent observation suggests that once operating, the Central in Chiclayo will begin to generate profits. The problem of lack of capital is acute. Special loans from state banking institutions generally require at least twenty percent equity for financing a project. The Centrals in fact are

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not yet in a financial state sufficiently strong to receive loans. Some of the Centrals will likely never be in such a state.

To place those Centrals with economic potential on a sound financial basis requires that a process of capitalization be initiated. This process can be indirect or direct. An indirect procedure would be to subsidize the interest rate charged on project investments. By lowering the interest rate charges, financial profits are increased which, over time, form the basis for capitalization within the firm. A direct approach would be a capital donation tied to specific project investment.

There are a variety of reasons for not recommending that the interest rate be raduced. First, the indirect method is a lengthy process. SEcond, a reduction in the rate of interest for many projects, particularly marketing projects is not of a magnitude sufficient to make much of a difference. Third, a lowered rate of interest is likely to be used to justify projects that in economic terms are not feasible. A consequence of using a reduced rate will be to favor projects that utilize capital at the expense of labor. The agricultural machinery projects will tend to look financially viable when, in fact, they are largely unjustifiable.

The donation approach has fewer drawbacks and several strengths. First, it attacks the two basic problems of the Centrals -- integration with the affiliated cooperatives and the low level of capitalization. As outlined in the recommendations, the base cooperatives are required to match, on a proportional basis, the amount of the donation. By requiring the cooperatives to invest in the Central, there is a greater likelihood that the cooperatives will utilize the services stemming from the project. The donation enables the Centrals to achieve a sound

capital basis in a short period of time. Further, by reducing the acmount of the investment that must be financed by the loan it also generates financial profits. The donation can also be used to cover operating losses in the initial phases of the projects, whereas it is difficult to use loan funds for this purpose. The basic point, however, is this: without a direct increment to the equity position of the Central, it will not have the capital basis on which tooperate as a business. Red ucing the interest rate on project investments leaves unchanged the capital structure of the firms.

RECOMMENDATIONS

The general conclusion of the evaluation is that the "Centrales de Cooperativas", in some areas, have the potential to become important agricultural service institutions for both member cooperatives and private producers. Therefore, the basic recommendation is that the loan be extended and restructured to assist those Centrals with the greatest potential. The restructuring must proceed on two lines: (1) changing the procedures which have the program bogged down in studies and (2) changing the orientation of the loan to deal realistically with the problems confronting the Centrals.

STRATEGY

The factors which appear to be the major limitations on the development of the Centrals are the lack of integration between the Central and its members and the low level of capitalization within the Centrals. These two problems are related, for it is the members who can potentially raise the level of capitalization of the Central. However, because the Centrales were formed without an adequate financial base and unable to offer services, the member cooperatives have had little incentive to increase their financial support to the Central. Lacking a significant financial interest in the Central, integration remains at the conceptual level. The restructuring attempts to break this cycle by providing a capital donation from the loan funds, to those Centrales with the greatest development potential.

In order to receive a donation, a Central must meet the criteria indicated in Annex 1. The criteria are designed to ensure that only those Centrals with potential receive a donation. The most important requirement is that the member cooperatives increase their financial

support to the Central. The amount of the donation is tied to financial support from the cooperatives. The matching arrangement between donation and capitalization from the member cooperatives is shown in Table

The justification and feasibility of these amounts and proportions is provided in Annex 2. The donation reflects a complete change in the orientation of the loan. The assumption at the beginning of the project appears to have been that the Centrales were reasonably well-functioning institutions, that only lacked technical assistance and easily accessible credit to implement projects. We believe this is mistaken. The centrals, even the relatively strong ones, such as Puno and Cerro de Pasco, are marginal enterprises, formed without an adequate financial base. The objective of the restructuring is to begin by placing a selected number of the original twenty Centrals on a sound financial base. Without this, even the better Centrals are likely to remain marginal businesses. The donation serves to capitalize the Centrals with potential and tie them more closely to their member cooperatives.

The donation can be used to help finance project investments and cover projected operating cost deficits for project activities.

Operating Cost Deficit. An economically justified project that is projected to run deficits in the first years can be considered for a donation. The amount of the donation cannot exceed the amounts indicated in Table and must be matched by financial support from the cooperatives. The maximum period of the donation is three years and the maximum amount over that period is $35,000.

TABLE Proportional Relation between Donated Capital and Capital from Member Organizations

Objective	Cooperative	Donation	Condition
Investment and fixed assets	1	2	Up to a limit of $50,000 donation per Central
	1	1	Up to a limit of an additional $100,000 per Central
Operating Costs	1	2	For the first year, up to $20,000 per Central
	1	1	For the second year, up to $10,000 per Central
	3	1	For the third year, up to $5,00 per Central

Investment in Projects. In the financing of investments a capital structure of 50 percent loan and 50 percent own resources is recommended. The donation and matching funds can be used to build up equity to achieve this proportion for most projects. For large agroindustrial projects a ratio of 20 percent own resources and 80 percent loan may be considered.

Fixed Assets for Service Programs. Marketing and production service programs for which fixed assets are required to establish the program may utilize donation funds. This may include office equipment, vehicles, and some agricultural machinery. Agricultural machinery with a per unit cost in excess of $7,000 however cannot be purchased with donation funds.

Centrals that receive donation funds must agree that they will not distribute profits until they have capitalized an amount equal to the amount of the donation received. The Agrarian Bank will monitor this.

Based on the evaluation, it appears unlikely that more than ten of the Centrals can meet the conditions for receiving donation. The maximum amount of donation from the loan fund is, then, on the order of $1,850,000.

The remainder of the loan funds ($4,050,000) may be used in the following ways:

a. Medium and long term credits to finance up to 50 percent of the investment cost of fixed assets required to provide marketing and production services.

b. Medium and long term credits to finance up to 50 percent of the investment cost of agroindustrial projects. In exceptional cases, loan funds may be used to finance up to 80 percent of the investment cost.

c. Short-term credits for working capital to finance start up costs and/or operating costs of service activities.

All funds used for donation, purchase of agricultural machinery, and the construction of administrative offices must have the approval of the Agrarian Bank in Lima and A.I.D. Other uses will be handled by the normal procedures established by the Agrarian Bank. Projects whose costs require approval by the Lima office of the B.A. will also require the approval of A.I.D.

As in the original loan agreement, the counterpart from the Government of Peru will be used to provide short-term operating and production credit to the Central and its affiliates. Because of the financial

crisis currently facing the GOP, it is allowed minimum counterpart obligations. While a reduction in the counterpart has not been requested, the counterpart obligation may be reduced to the minimum of 25 percent.

The total amount of donation for investment purposes is $1,500,000. In order for the total amount to be realized, the member cooperatives would be required to provide $1,250,000. If this equity is used to finance 50 percent of investment costs, credits for $2,750,000 would be drawn upon. An additional $350,000 is available for operating cost deficits. This gives a total for donation and medium and long term investments from the loan of $4,600,000. This is a rough estimate -- more than ten Centrals may meet the conditions for financing or the cooperatives may not provide complete financial support. At any rate, it appears unlikely that all the loan funds can be utilized if we restrict the scope of the loan to the best of the pre-selected twenty Centrals. In the course of the evaluation, however, numerous cases of strong secondary level cooperative organizations were identified, often in areas served by a weak Central. These other institutions include both Centrals and "Cooperativas Agrarias de Servicio", (CAS). The CAS provide marketing services for private producers. It is reasonable to assume that the remaining $1.3 million could easily be utilized by opening the scope ofthe project to finance sound projects for any secondary level cooperative organization that meets the loan eligibility criteria.

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BREAKING THE STUDIES BOTTLENECK

The development plans for the first fourteen Centrales are under revision in the Ministry of Agriculture. The plans for the last six are still in the hand of the consultants. The revision process has no end in sight and is not producing studies of satisfactory quality. Almost without exception, the projects elaborated by the consultants will require a more thorough revision before financing can be considered. This revision cannot be done by the Ministry of Agriculture in Lima, for the faults of the studies stem largely from a lack of detailed local knowledge, a failure to appreciate the local constraints and potentials. These factors will only be included by making the Central responsible for revising the studies and providing the technical assistance and guidance at the local level to the Central. A general plan for implementing this recommendation is provided in Annex

The basic points of this plan are the following:

(1) A.I.D. will contract two to three Peruvian technicians to assist in the management of the project as well as to assist in the evaluation and revision of the project studies. The contract period will be for one year for a maximum time of three years.

(2) The remaining technical assistance funds in the project will be used to contract four to six technicians to work in the Agrarian Bank unit that is in charge of implementating this project. These persons will form T.A. teams to work with individual Centrals in the revision of the projects and the preparation of the loan applications.

(3) The Ministry of Agriculture will form working groups at the local level of at least two persons who will assist the Bank and A.I.D. specialists in revising the studies.

(4) The project documents are to be turned over to the Centrals in a rapid and orderly fashion, as outlined in Annex . Those Centrals with the highest potential are to be given first priority.

(5) Payment to the consultants will be made on a case by case evaluation of the documents. The consultant may be asked to return to the site to assist in the revision if the work to date is deemed unsatisfactory.

(6) As the studies are turned over to the Centrals, the technical assistance teams will work directly with the management of the Centrals to develop the projects and the loan applications. They will begin with the Centrals of highest priority and complete that work before moving to another Central. There will be two to three teams working simultaneously in the field to develop the projects to a level that justifies financing. The technical assistance teams will move from Central to Central, following the priorities outlined below.

(7) The Agrarian Bank with the advice of the Ministry will establish whether or not a Central qualifies for receiving donation funds.

(8) Following the outlined plan, it is anticipated that it will take 9-12 months to get the studies and loan applications for the ten priority Centrals. Because it is a staged procedure, commitments for the highest priority Centrals will likely be made before this. At any rate, the project is practically beginning anew, and the same length of project that was initially anticipated remains the most reasonable

expectation: 36 months for terminal disbursement and 30 months for terminal commitment.

(9) An evaluation by the Bank and AID will be made at the end of 18 months. If at this time, committed funds are less than 50 percent but more than 30 percent of the total loan, the funding will be reduced proportionally. If commitments total less than 30 percent, no further commitments under this loan will be made.

SUMMARY OF RECOMMENDATIONS

The recommendations for the restructuring are fairly simple: (a) provide a capital donation to establish some selected Centrals as viable business operations, and (b) set up a procedure to move the studies to the local level and provide technical assistance for their revision. The overridding problem with this loan has been the incapacity of the Ministry to manage the study phase. The breaking of this dead end in as short a period as possible eliminates this difficulty.

The capital donation component of the loan is designed to overcome the two major internal constraints on the development of the Centrals: their lack of owned capital and the lack of integration with their members. If these dual problems are not resolved, it is doubtful that the Centrals will develop into viable agricultural service institutions. The evaluation suggests that about half of the twenty selected Centrals are viable or potentially viable. The new procedures are designed to provide the technical expertise to get their projects funded and a funding mechanism that will give those Centrals an adequate financial base for their operations.

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ANNEX 1

Requirements for Receiving Capital Donation

1. The Central must have a full time manager paid by the Central.
2. The Central must currently be offering at least two economic services to the member cooperatives and more than half of the affiliates must be utilizing the services.
3. The project and loan solicited must be approved by the "Asamblea de Delegados" and the cooperatives agree in an effective manner to use the services of the project.
4. To receive a donation, it must also be shown that the cooperatives, through the assembly, will provide the financial support necessary to receive the donation and that they have the resources to do so.
5. In receiving a donation, the Central commits itself to not distribute profits until an amount equal to the amount of the donation is achieved.

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A N E X O Nº 2

1. El análisis de los estados financieros de las Centrales muestra que la generalidad de ellos tienen un escaso patrimonio que se traduce en bajos índices de solvencia (Pasivo total/Activo total) que fluctua generalmente alrededor de 0.85.

2. De acuerdo a esta realidad se estima que en esta etapa de consolidación de las centrales, la relación deuda-capital deseable sería 1 : 1 a fin de tender a un índice de solvencia de 0.5.

3. Dentro de este planteamiento, las inversiones que realicen las Centrales deberían financiarse 50% con recursos propiros y 50% con endeudamiento. Tratar de tener un palanqueo financiero mayor sería contribuir al deterioro de la empresa y dificultar la adecuada capitalización de la misma y solo podría justificarse en casos excepcionales.

4. Si se considera que en promedio las inversiones en proyectos agroindustriales previstos por las Centrales, pueden tener un orden de magnitud de 100 millones de soles (US$400,000.00), se requeriría que las cooperativas de base aportaran el 50%, es decir 50 millones de soles.

5. Para poder apreciar la capacidad de aportar estos montos, analizaremos 2 ejemplos que podrían representar posiciones opuestas:

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a) Central de Chincha, cuenta con 19 cooperativas alifiadas, de las cuales 1 esta en proceso de disolución. La situación económica de las mismas en su mayor parte es buena. Si tuvieran que invertir los 50 millones a que hemos hecho referencia, cada una de ellas tendría que aportar, alrededor de 2.8 millones de soles. Se estima que este monto no lo podrían aportar en su integridad, pero si podrían llegar al 50% sin dificultad.

b) Central de San Lorenzo, cuenta con 17 cooperativas de producción y 16 grupos campesinos afiliados. La situación económica de la mayor parte de los afiliados es precaria y recien se ha iniciado su proceso de capitalización. Considerando la inversión de 50 millones, correspondería a cada una de las afiliadas 1.5 millones. Este monto dificilmente podría ser aportado y se estima que con dificultad podrían estar aportando alrededor de S/.400,000.00

6. De acuerdo a lo analizado se puede estimar que la capacidad de aporte de las cooperativas estaría entre un límite superior de 1 sol por cada sol de donación y un límite inferior de 1 sol por cada 3 de donación.

Estos límites nos sirven de base para considerar que una relación aceptable a las Centrales sería de 1 sol de aporte propio por 2 soles de donación. Esto significará que en casos como San

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Lorenzo se vera obligado a optar por inversiones de menor envergadura y Centrales como Chincha podrán aspirar a proyectos de mayor magnitud.

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