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PROSPECTUS  
FOR A STUDY OF  
PRIVATE INDUSTRIAL DEVELOPMENT  
IN  
NICARAGUA

Submitted to the  
Agency for International Development

By -

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PROSPECTUS FOR A STUDY OF  
PRIVATE INDUSTRIAL DEVELOPMENT IN NICARAGUA

Nature of Study

This is an evaluation study of private sector industrial development in Nicaragua. Primary emphasis is on credit programs to which AID has given financial support. Such support includes 1964 and 1967 loans to the National Development Institute (INFONAC), 1965 and 1966 loans to the Nicaraguan Investment Corporation (CNI) and the 1967 loan to the National Bank of Nicaragua (BNN). These credit programs are to be evaluated as contributors to sectoral and national development objectives in conjunction with other measures which either encourage or place constraints on industrial development.

This study will be concerned mainly with processing and fabrication in establishments with a minimum of five employees. Such industry accounts for about 90 percent of value of output in the sector. Since this sector has recently experienced a period of significant growth it provides scope for evaluating the results of this growth and of the contribution of the above-named institutions. The institutions have received financial support from other external as well as domestic sources. This will permit relating the AID capital contribution to total availabilities from all sources and the aggregate availabilities to opportunities for effective use of such capital.

The three criteria that INFONAC professes to use in establishing priorities are: (a) foreign exchange earnings and savings, (b) use of domestic raw materials and (c) new job creation.

These appear to be appropriate for this study, and the conventional criterion of rate of return on investment may be added. Some system of balancing the criteria will be necessary as the simultaneous application of several criteria may give rise to internal contradictions which will have to be resolved.

Consideration will be given to possibilities of and limitations of future expansion of different types of industrial production. This will include new types of industry, particularly those that increase the value added in the case of goods exported. This phase of the study is intended to provide guidance in establishing future priorities for loans by type of industry which are not based solely on past experience.

In the earlier years of the CACM, for example, there was a great deal of import substitution within the market area, inspired by the high tariff walls around it. As these opportunities have been exploited, further expansion has proceeded at a more modest pace and future developments may be still more heavily dependent upon growth of the CACM market. Similarly, Nicaragua's application of the 30 percent import duty surcharge on selected non-CACM imports (pursuant to the 1968 San Jose Protocol) may have important consequences which should be measured against development objectives.

Another relevant matter concerns the effect on Nicaragua of competition among the CACM nations to induce foreign investment. There is some evidence that Nicaragua's efforts to attract foreign capital and enterprise may have included excessive concessionary inducements. The prospects for different kinds of industry will be importantly influenced by laws, regulations and administrative

practices with respect to business taxes, imports of capital goods and supplies, employment practices and the like. Therefore, consideration will be given to these matters as they may either encourage or discourage developments essential to the purposes of the credit program.

### Specific Methodology

Time constraints prevent the extensive use of quantitative analytical data, and the study will depend heavily upon probative questions in interviews with selected informants. These questions will be formulated to provide information necessary for (a) an economic evaluation of recent industrial developments, (b) relating the contribution of INFONAC and the other institutions in which AID has an interest to this overall industrial expansion, (c) prospects for further development, and (d) the choice and effectiveness of measures to achieve the development objectives, with particular attention given to important institutional or policy obstacles encountered. A partial list of such questions for each of the principal phases of the study follows:

#### A. Evaluation of Recent Industrial Development

Growth in number and volume of output of plants producing different types of goods for the past decade will be examined. For each major industrial category an approximate determination will be made of its balance of payments impact, its benefits to suppliers of raw materials, volume of employment created and rate of return on invested capital. This will be done insofar as practicable from readily available official statistical sources. The results will be verified as necessary or appropriate with some of the informants interviewed. The data will mainly serve

to provide a framework for the interviews which would seek answers to the following questions:

1. What kinds of industrial production have grown most rapidly and how does this growth compare with ratings according to the criteria listed above?

2. Has lack of capital limited financing priority types of enterprises?

3. Are there other constraints such as tax and trade policies?

B. Relation of Institutional Lending to Industrial Development

Loans of INFONAC, CNI and BNN will be categorized by kind of industry and size and characteristics of borrower. The results, when compared with the industrial profiles developed above, will provide the basis for determining the extent to which these institutions have furthered the development of the types of industry which best fulfill the relevant criteria. The consequences of large loans for purposes clearly divergent from the stated criteria will be determined. Throughout, the team's findings will be checked against inquiries made of appropriate informants.

Particular attention will be given to the following questions:

1. Do these institutions consciously or systematically provide priorities to influence the direction of investments?

2. What form do such priorities take?

3. What advantages are received by clients from these institutions as compared with those available elsewhere? Are these advantages decisive in businessmen's choices?

C. Future Directions and Potential Volume of Industrial Growth

Based on the team's evaluation of the issues discussed above, and again working from interviews, an appraisal will be made of the probable future direction of, and growth opportunities for, Nicaraguan private industry. Key points in this appraisal include the following:

1. Which industries have greater economic potential for expansion, taking account of foreign and/or domestic demand for the product and the characteristics of the supply function?

2. What should be the future role of INFONAC and CNI in relation to other credit institutions?

3. What improvements are needed in the policies and operating methods of these institutions?

4. What role might AID play?

5. What changes are needed in tax, trade and other public policies?

D. Adapting Credit and Related Programs to Future Needs

Finally, an inquiry will be made into appropriate measures to further optimum industrial development.

1. Are significant changes needed in priorities in granting loans? In terms of loans?
2. Is the technical assistance available to potential borrowers adequate so as to assure the needed quality of loan applications? Is the technical assistance available to both borrowers and lenders adequate to help assure the successful implementation of the loan-financed projects?
3. Are credit availabilities adequate to meet needs?
4. Could the credit programs be managed so as to offer possibilities for participation in loans by wider segments of the population than at present?
5. Are there external constraints upon success of credit programs?

#### Source Information and Data

INFONAC has played an important central role in private sector industrial development, and AID has long been deeply involved. The Capital Assistance Paper, Nicaragua: Industrial Development - INFONAC II provides a comprehensive description and analysis of these developments through 1966. This document also describes the INFONAC program for the 5-year periods 1966-71 and 1972-75 and its relationship to projections of the National Planning Office for the Nicaraguan industrial sector. The role to be played by the \$5 million loan is indicated.

The data used in this paper evidently came from INFONAC and other official published or unpublished sources. This is

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indicative of the kinds of data that presumably are available for studying developments since 1966 in relation to the targets chosen at that time.

The Audit Report (No. 68-37-N4) on the first AID loan to INFONAC provides additional information on industrial projects financed by INFONAC with AID funds.

The Capital Assistance Paper, Nicaragua: Corporacion Nicaraguense de Inversiones (CNI) parallels the INFONAC paper cited above by describing the industrial financing activities of CNI since it was chartered in 1964. This includes the use of the first AID loan of \$3 million.

This document provides a useful description of the credit system of Nicaragua and shows how the function of institutional financing of industrial growth is shared by CNI, INFONAC, the National Bank of Nicaragua, the four private commercial banks of substantial size and the Central American Bank for Economic Integration. A list of project proposals that were under active consideration at that time and which might be candidates for AID loan financing is presented. Their total cost would be about \$48 million.

The Capital Assistance Paper, Nicaragua: Small Enterprise concerns a \$2 million AID loan in 1967 to the National Bank of Nicaragua (BNN) for the purpose of providing short- and medium-term credit together with technical assistance to small industries, artisans and small merchants. It provides considerable insight into the role of industry in the economy, including rate of growth of the industrial sector, number of small enterprises, productivity of labor employed therein, volume of output and industrial expansion in relation to the balance of payments position.

The documents discussed above as data sources are valuable with reference to private sector industrial development and the AID role during the period to which they relate. It so happens that this was a period in which the economic effects of CACM arrangements were strong. This favored growth in those industries

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SCHEDULE FOR ITEM V, TRAVEL AND TRANSPORTATION

U.S. Travel: Non-D.C. Residents from Miami	\$ 138
D.C. Per Diem (14 days @ \$25)	350
International Travel:	
(4) trips to Managua	1,256
Excess Baggage	104
Field Per Diem	2,394
International Travel Per Diem	<u>24</u>
<b>Total</b>	<b>\$4,266</b>
	<u>                    </u>

SCHEDULE FOR ITEM VII, OTHER DIRECT COSTS

Preparatory Costs	\$ 300
Communications	250
Materials	100
Printing and Reproduction	800
Miscellaneous	<u>100</u>
<b>Total</b>	<b>\$1,550</b>
	<u>                    </u>

Logistic Support (Article VII, B., Contract AID/1a-650)

"The Contractor shall be provided with logistic support overseas, either by the mission or the Cooperating Country. If not provided in kind, Contractor will be reimbursed for such costs in U.S. dollars."

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SCHEDULE FOR ITEM I, SALARIES

	<u>Man Weeks</u>	<u>\$</u>
Jacobson (Principal)	1	\$ 769
Allen (Project Supervisor)	3	1,846
Statistical, Research, and Editorial	1	183
Technical Specialists and Evaluation Generalists:		
Bramble	10	5,096
Joel	6-1/2	<u>2,625</u>
	(Sub-total)	\$10,519 (1)
Artamanoff	<u>7</u>	<u>3,500</u> (2)
	Total	<u>\$14,019</u>
	<u>          </u>	<u>          </u>

(1) Subject to 120% Overhead Rate

(2) Subject to 30% Overhead Rate

which were in a position to take advantage of the opportunities offered by the enlarged and protected market within the member countries as a group. Nicaragua did not benefit as much as some of the other members as evidenced by her CACM trade deficit. Even in the countries which benefitted more there has been a tendency toward a slackening in industrial growth rates, presumably because a number of particularly attractive opportunities for CACM import substitution have been exploited. In any event there have been major changes in the economic climate for industrial growth since 1966 and 1967. It is on this period and the future that this study will be mainly focussed. These reference papers will provide a historical base to build upon and will also be suggestive as to the kinds of data available from official sources and types of analysis possible with these data.

A number of other documents have been perused during the course of our research, and will prove to be of value in appraising the development of the private industrial sector in Nicaragua.

Certain key organization problems of INFONAC are outlined in a paper prepared in 1963 by John F. White for INFONAC and AID, entitled Organizing a Nicaraguan Office of Industrial Investment Promotion. Mr. White's recommended solutions to some of these problems also bear examination.

Some valuable industry profiles are to be found in the 1961 report of International Economic Consultants, entitled Incentives for Private Enterprise in Nicaragua. This report also contains some useful data on the number of enterprises classified under the Law for Protection and Stimulation of Industrial Development. Much of this information is now obsolete, though some of the material assembled by IEC appears to be of some use even today.

A thoughtful view into the Nicaraguan Planning functions and operations is contained in the Continental-Allied report entitled Nicaragua's Planning Office, though here also the material was gathered in mid-1963.

Another interesting report which affords insight into the views of Nicaraguan small businessmen toward attracting joint venture capital is the 1967 Report on a short-term study tour of area development for PRODECA of Nicaragua, prepared by Conway Research for AID, which discusses a listing of enterprises possibly suitable for development in Nicaragua.

Still other reports have been examined, though they appear to bear only peripherally on the present effort. These include:

W. V. Patten, A Report on Industrial Development Promotion, 1965

R. Deschamps, Proposed Supervised Credit Program for Nicaragua, 1965

Additionally, the material in the latest CIAP INFORME FINAL DEL SUBCOMITE DEL CIPA SOBRE NICARAGUA will be beneficial in providing perspective into the general development of the Nicaraguan economy. Particularly useful in this regard are the prepared statements of the IBRD and the IMF representatives.

#### Time Schedule

Within two weeks of AID approval of this prospectus, a senior member or principal of the contractor will go to Nicaragua to perform the tasks listed in Article IB3 of the contract. For

planning purposes one week is allotted to this, and another week to followup in Washington in case any changes in plans or budget need to be agreed upon. The sector study team would then be organized, briefed and prepared to go to Nicaragua. Tentatively, it is planned that the team should go to Nicaragua about one week after approval of the plan and budget. This would be approximately five weeks after AID acceptance of the prospectus.

The three RRNA team members would spend a total of sixteen man-weeks in the country. This would include drafting a report which could be discussed with the Mission Director and/or members of his staff before departure of the team.

The team leader would work with home office staff of the consultant and the other members of his team for two weeks if necessary in the final revision and editing of the report. An additional week must be allowed for its reproduction as required for submission to AID/W.

Taken together, a total elapsed time of up to fourteen weeks will be required from the initial AID approval of the prospectus until the submission of the final report to AID/W.

#### Team Composition and Areas of Specialization

The field survey team is proposed to consist of three members from the contractor's firm and one participant from AID/W. In addition, it may be desirable to engage a Nicaraguan national to provide special insight into the local conditions and problems with which the team will be confronted.

From the contractor's firm, the following team members are proposed:

Team leader and evaluation generalist: Harlan Bramble  
Development economist: Clark Joel  
Industrial specialist: George Artamanoff

R. H. Allen will serve as the project director and Jerome Jacobson will be the contractor principal.

The team members proposed have been chosen to cover the most important areas of technical specialization combined with experience in developing countries working with governments on industrial development programs and with US agencies on programs for assisting governments to achieve mutually agreed objectives.

The team leader has been with the firm for over 5 years during which time his assignments which are relevant to this project included a study of the possibilities of economic integration between Colombia and Venezuela, and an investigation into increasing industrial development opportunities along the Mexico-US border. He recently returned from participation in a three-sector planning study for the Government of Ghana. Mr. Bramble is an economist with a long background in trade and economic development of LDC's, especially those that are heavily dependent on exports of primary commodities. He is coauthor of an RRNA report of the effects of European regional preferences on the exports of Latin America. Other services have included economic consultation for the Banco Central, Dominican Republic, and on development of a ferro-nickel project. Prior to joining Nathan Associates he was Counselor for Economic Affairs with the US Embassy in the Dominican Republic and later was Deputy Chief

of the Economic Section in Mexico. Formerly he had been Counselor of Economic Affairs in the US Embassy in Venezuela. From 1959-62 he was Deputy Director and Acting Director, Office of International Materials, (OR), Department of State.

Mr. Joel is a development and fiscal economist. He recently returned to the United States from El Salvador where he had worked for 3 years as a member of RRNA's economic development advisory team. His work there specialized in the analysis of balance of payments and monetary problems and the preparation of a tax reform program. His earlier overseas experience included two years as US/AID Program Economist in Laos (1963-65), where he advised on problems related to the economic stabilization program, projected resources required for the stabilization fund and commodity import programs, analyzed the demand for foreign exchange and prices and helped to develop an agricultural incentive program to stimulate rice production. In addition, he worked for two-and-a-half years as Program Officer for the UN Korean Reconstruction Agency (1953-55), during which time he assisted in the RRNA survey of the Korean economy and preparation of an economic program for Korean reconstruction.

Mr. Artamanoff is an experienced industrial economist who has held senior positions in both industry and government. He had principal responsibility for a study of state-owned enterprises in Thailand, a project financed by USAID. A wide variety of industries were studied, including sugar, paper, gunnybags and Hessian cloth, preserved foods, textiles, tanning forest products, and pharmaceuticals. In a study of industrial growth possibilities in Morocco, Mr. Artamanoff once again studied a wide range of industries, including fruit and vegetable processing, fish processing, fish meal and fertilizers, and the development of an industrial complex.

All three team members are fluent in Spanish.

The selection and appointment of the AID/W participant are of course matters which must ultimately rest with the Agency. We have discussed this question with various people in the Latin American Bureau and it has been suggested that Mr. Charles Johnson, the Central American Program Officer in LA/DP would be well qualified to participate in the study. Mr. Johnson has considerable AID experience, both in Washington and abroad. He has been recommended as being able to translate the concepts employed in the evaluation process into program or operation teams. Someone with Mr. Johnson's skills and experience should be able to make a significant contribution to the effectiveness of the team.

The general division of work will be as follows. Clark Joel will concentrate on analyses of the role of the industrial sector and various types of industry in contributing to national economic objectives. This will include balance of payments considerations, employment effects and intersector effects.

Mr. Artananoff will be responsible for the more technical aspects of industry organization and industrial processes which have a bearing on the competitive position of Nicaraguan goods both within and outside the CACM.

Harlan Bramble, in addition to his general supervisory role, will be concerned directly with the economic viability of different types of industry and priorities for investment in industry.

The AID team member will have specific responsibility for institutional and organizational matters. This will embrace the government agencies administering credit and related programs and public policies which have a bearing on the effectiveness of these programs.

BUDGET SUMMARY<sup>1/</sup>

	<u>Total estimated costs, including overhead</u>
Reconnaissance field trip and team briefing (6.5 man-weeks)	
Field evaluation (16 man-weeks)	
Report completion, review and editing (6 man-weeks)	
	\$27,692
 Total transportation and travel costs, other direct costs, contractor's fee.....	 8,364
 Total (28.5 man-weeks following submission of prospectus).....	 \$36,056

<sup>1/</sup> Excludes cost of AID participant, locally hired Nicaraguan and any local logistical expenses.