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— LOAN

FORM No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

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WBG ARCHIVES

September 10, 1971

LC/M/71-11

Minutes of Loan Committee Meeting held on Tuesday, August 31, 1971 at 3:30 p.m. in the Board Room.

A. Present:

J. Burke Knapp (Chairman)	D.J. Fontein
S.R. Cope	D. Gustafson
G. Alter	J.P. Hayes
A. Broches	C.G. Melmoth
B. Chadenet	D. Richardson
V.C. Chang	A. Stevenson
R. Chaufournier	J.H. Williams
R.H. Demuth	E.P. Wright
L.J.C. Evans	Dag F. Wittusen (Secretary)

Attending:

G. Aithnard	C.R. Poncia
B.A. de Vries	R.E. Rowe
D. Elz	R. Wadsworth
P.T. Grosjean	M.J. Walden
H.J. Nissenbaum	

B. Ghana - Sugar Rehabilitation Project

1. The Committee considered a memorandum dated August 27, 1971 from the Western Africa Department entitled "Ghana - Proposed Sugar Rehabilitation Project" and the accompanying appraisal report. The memorandum recommended that the Government be invited to negotiate a $7 million loan and a $8 million credit to finance the foreign exchange component of a project to rehabilitate the Ghanaian sugar industry.

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
Controller

Copies for Information:

President
The Economic Adviser to the President
Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

C. Disoussion

3. The Chairman, in opening the discussion, asked the Committee to consider whether a good case had been made for Bank Group investment in a sensitive and generally believed "surplus" crop. The project, providing a high return in foreign exchange, would improve Ghana's precarious balance of payment position, but it required substantial nominal protection against imported sugar, and the project's justification relied heavily on the use of a shadow rate of exchange. The Chairman felt that a closer look should be taken at Ghana's comparative efficiency in sugar production as a justification for the proposed investment.

4. In reply, Agriculture Projects Department said, first, that the past world sugar surplus was disappearing. Second, a standard economic analysis relating Ghana's comparative efficiency to the world market price of sugar was inappropriate. Most of world sugar production was sold at preferential rates according to special producer-consumer arrangements and did not enter the "free" world market. The marginal supply that entered the free market and determined the world price was often "dumped," making the world price largely irrelevant as a yardstick of efficiency. Other tests of efficiency, however, indicated that Ghana was potentially as efficient as other sugar producing developing countries. Regarding the shadow rate of exchange, it was appropriate on account of the overvaluation of the cedi and Ghana's shortage of foreign exchange. It was agreed that Ghana's exchange rate and the world sugar market situation would be treated more extensively during Board presentation.

5. Further substantive discussion focussed on (i) the protection of the sugar industry, and (ii) financing of the expatriate management firm.

6. Protection of the Sugar Industry. The Committee noted that:

(i) Some protection of the local sugar industry, via import duties on foreign sugar, was necessary and legitimate because of the absence of a truly competitive world market and the over-valued exchange rate of the cedi. At the same time, the system of protection should be flexible in order to avoid overprotection and should in particular be responsive to changes in the exchange rate.

(ii) There was some criticism of the proposal to obtain assurance that the Government would take the measures necessary to enable Ghana Sugar Company (GSC) to earn a return of at least 7% on capital employed (Appraisal Report, 9.02(r)). While a nominal protection against imported sugar was acceptable on economic grounds, it was questionable how far the Bank should insist on maintaining the financial viability of GSC. Several speakers maintained that the proposed rate-of-return covenant would compromise one of the prime objectives of the project, viz. to increase the technical and managerial efficiency of the sugar factories, by removing market pressure for reform and in effect guaranteeing a certain level of profits.

7. Financing of Expatriate Management Firm. The Committee noted that:

(i) The Area Memorandum recommended that the cost of the expatriate management team be capitalized and be eligible for Bank financing for four years until the financial break-even point of the project was reached. In response to questions of why this cost was not treated as recurrent, the Area Department stated that since there was a constraint on Bank financing of recurrent costs a broader definition of capital cost had been sought. It was argued that, according to Projects Departments Director's Memorandum No. 2.5, recurrent cost which contributed to the creation of capital assets could be capitalized and thus made eligible for Bank financing. Regarding the period for financing these costs, it had been set at four years on the assumption that after the financial break-even point of the project the cost of management should be considered operating costs and hence no longer eligible for Bank financing, according to D.M. No. 2.5.

(ii) The Chairman thought the financial break-even point of the project an arbitrary cut-off point for determining the amount of Bank financing. The Bank was fully accustomed to financing the foreign exchange component of management services for the entire period of disbursement of the loan (in this case, six years). The fact that the foreign exchange cost of management services in this project was an unusually large element of total financing should not prevent the Bank from following this guideline, particularly in view of Ghana's shortage of foreign exchange and great need for managerial assistance.

(iii) It was agreed that Projects Departments Director's Memorandum No. 2.5[1], entitled "Definition of Capital and Current Expenditures," should be circulated for review and further discussion.

1/ Attached

D. Conclusion

8. The Committee concluded that:

(i) The system of protection for the sugar industry should be flexible in order to avoid exclusion of competition with foreign sugar and the possible fostering of an inefficiently managed industry;

(ii) the Bank should finance the foreign exchange component of the expatriate management team for the full length of the disbursement period;

and further concluded that:

(iii) the Bank loan should be for 30 years, including 10 years of grace;

(iv) the Government-to-GSC relending rates on loan and credit proceeds should both by 7 1/4%;

(v) should some bilateral financing become available for the project, the Bank loan would be reduced accordingly;

and, subject to the modification in (i)-(v) above, approved the Western Africa Department's recommendation that negotiators be invited for the proposed loan and credit

E. Adjournment

9. The meeting adjourned at 4:40 p.m.

Dag F. Wittusen
Secretary

Cleared by: Messrs. Knapp
Broches
Chadenet
Chaufournier
Wadsworth/Evans

Secretary's Department
September 10, 1971

PROJECTS DEPARTMENTS

DIRECTOR'S MEMORANDUM No. 2.5

DEFINITION OF CAPITAL AND CURRENT EXPENDITURES

Introduction

1. The distinction between capital and current (sometimes referred to as recurrent) expenditure is important in determining the eligibility of items for Bank/IDA financing. While Article I of the Bank's Articles of Agreement refers to "facilitating the investment of capital for productive purposes" and to "the encouragement of the development of productive facilities and resources in less developed countries", there is no requirement that the projects financed by the Bank be capital in nature, provided that they come within the general purposes of the Bank set out in Article I. The Articles of IDA refer only to "providing financing to meet their [developing countries] important development requirements." There is therefore no legal requirement that the Bank should finance only capital expenditures, and whether or not it should do so is a policy question. This memorandum takes for granted that Bank finance should normally be limited to capital expenditures, but does consider whether in special or exceptional circumstances other kinds of expenditure should be financed.

2. While economic literature has dealt extensively with the subjects of capital, investment and consumption, and on the distinction between capital and current expenditures, considerable ambiguities remain and any set of definitions is arbitrary to some extent. Similarly, national accounting and budgeting practices in this field vary widely from country to country and time to time. The following attempts to give a practical definition of the concepts and to indicate how this definition applies to some of the principal types of Bank/IDA projects to which it is relevant.

Definitions

3. Capital expenditures are those which result in the creation of an asset which gives rise to a stream of benefits over a number of years. The number of years may vary, but in practice it must be at least 5 to 10 years as an average for the assets created under a Bank project in order to make the project suitable for Bank lending. This does not, of course, preclude the financing under the project of some capital assets with a shorter economic life.

4. Current expenditures are those giving rise to benefits which terminate within a short period of time, generally one year or less. Current expenditures must therefore be repeated at short, periodic intervals.

5. Capital expenditures may be for the purchase of the physical assets themselves (plant, machinery and equipment) which, since they give benefits over a number of years, are by definition capital in nature. In the case of labor, materials, and services, their classification for Bank projects depends on the use to which they are put. If they are used to create an asset which produces a stream of goods and services over a period, they are capital expenditures; otherwise they are current. For example, the labor, steel and other materials and services used by a borrower to manufacture its own railway locomotives are capital expenditures, as is the outright purchase by the borrower of the locomotive. The labor and materials used, in conjunction with the asset (locomotive) which has been created or purchased, to provide current railway services (the movement of passengers and goods) are current expenditures. Similarly, the wages of laborers and expenditures on gasoline and asphalt as well as depreciation of the contractor's equipment, are capital if they are used to build a new road or upgrade an existing road, since they create or add to the value of a long-lived asset (the road); the same expenditures are current if they are used to maintain an existing road since they must be repeated periodically to keep the road in its present condition. If road maintenance is neglected over a number of years, the capital invested in the road has been consumed, and the expenditures to reconstruct the road may be classified as capital since they create a new asset.

6. To continue with the case of highway maintenance, which illustrates some of the conceptual issues involved, the purchase of assets such as maintenance equipment (tractors, graders, rollers) is a capital expenditure; the labor, gasoline, asphalt and other materials used with the equipment to maintain the road in its present condition are current expenditures. The depreciation of the maintenance equipment and expenditures on its maintenance are current expenditures. This does not, of course, preclude the financing of the actual replacement of the equipment by external borrowing (including, if appropriate on other grounds, further Bank loans) rather than internally-generated funds; what source of finance is used for replacement depends on the overall financial position of the entity in question.

Other Illustrations

7. Other examples may be given. The salary of an engineer designing or supervising new road construction is a capital expenditure; the salary of an engineer [illegible] current [illegible]

8. A permanent increase in the inventory of materials, goods and supplies required to reach an initial level of operations, or to expand to a higher level, may also be classified as a capital expenditure; thereafter, such expenditures are considered as current. Thus, the incremental expenditures to build up a permanently higher inventory of asphalt and gasoline necessary for a higher level of road maintenance are a capital expenditure, as is the initial stock of textbooks and supplies for a new school. In the case of agricultural credit, short term credit to farmers for the purchase of seasonal inputs is a current expenditure to the farmer, but funds used to initiate such a credit program, or to expand its level, on a long term basis may be classified as capital expenditures.

9. The starting-up expenses of a project, covering the period until income from the assets created under the project is sufficient to meet expenses, are sometimes classified as capital and have been financed by the Bank, although the same types of expenditure are later treated as current; in effect, the development period for defining capital expenditures is taken as the time necessary to reach financial equilibrium. This would be the case, for example, of the expenditures for feed, etc. under a livestock breeding project until the new ranches were in full production.

10. Similar considerations may apply in the case of non-revenue earning projects. Thus, the Bank has, in exceptional cases, financed a declining proportion of the additional current expenditures for an expanded highway maintenance program, until such time as the Government's financial position would enable it to cover them.

11. The foregoing illustrations have all dealt with actual cash expenditures rather than economic costs. In the case of livestock projects, the withholding of cattle from markets during the herd build-up period is a capital cost, involving the foregoing of possible revenue over a period of years, although not a cash outlay to the farmer. It may also have a foreign exchange cost, since the withholding may result either in the loss of foreign exchange revenue or in an actual foreign exchange outlay for additional imports to supply the domestic market. It may be appropriate in some cases to take such costs into account in measuring the size of the farmer's contribution, the (indirect) foreign exchange cost of the project, and the amount of Bank financing. However, they should not be shown in the cost estimate table of the appraisal report, which is based on cash expenditures.

12. The classification of technical services such as those of consultants and advisers likewise depends on the use to which the services are put. Most of these services are likely to be capital in nature since they are used to prepare studies, train local personnel, give advice on the reorganization of institutions, etc. which yield benefits over a number of years. On the other hand, while the salary of the expatriate manager of a construction project may be a capital expenditure, the salary of the expatriate manager of an on-going enterprise is generally considered a current expenditure although conceivably it may involve elements of both.

13. Education projects are financed by the Bank on the grounds that they are an investment in human capital which contributes to the economic development of the country. Expenditures on school buildings, training equipment, facilities, and an initial stock of supplies, are all investments to create a capital asset (the educational system) which produces an output of trained manpower. The salaries of the staff of a project unit would also be a capital expenditure. On the other hand, from one point of view, teachers' salaries are not an element in creating the asset, but a current expenditure made in conjunction with the school system towards the annual output of students. From another point of view, however, the trained manpower which is the output of the school system is itself an asset, yielding a stream of benefits over the productive life of each graduate. In this sense, teachers' salaries would also be a capital expenditure. However this issue is viewed, there are practical objections to the Bank's financing teachers' salaries. If they were made eligible for financing they would be a very large element of total project costs, involving largely local currency expenditure. It is desirable that the Government be in a position to finance these expenditures from its regular budget over the life of the project. It would be appropriate, however, to finance the salaries of expatriate teachers used to train local teaching staff, for the reasons indicated in paragraph 12.

14. In Family Planning, expenditures on building a clinic, on transport equipment, and on an initial inventory of medical supplies are capital; they create an asset (the family planning service) which produces a stream of benefits over time. The expenses of operating the clinic, including salaries of doctors and nurses, and pills for current consumption are generally considered to be current. It could, on the other hand, be argued that each pill for example is an asset, albeit a small one, producing a stream of benefits over a number of years (the costs saved by the prevention of a birth for one day). A further argument could be that, given the importance of family planning in certain countries and the need to start or expand a family planning program on the right basis, there may be instances in which the Bank could make a contribution, on a declining basis, to the initial or incremental cost of running a family planning program. The Bank has not yet made any loans for population purposes, and its policy in this field is still under consideration.

Presentation in Appraisal Reports

15. In the preparation of appraisal reports, the table on the cost estimate of the project should contain only capital expenditures, on a cash basis. In projects where there are important related expenditures of a current nature (education, highway maintenance, family planning) these should be presented separately in the text, and the two sets of

figures should not be added together. In the cost-benefit analysis, both capital and current expenditure are taken into account since both are necessary to achieve the benefits being measured.

Warren C. Baum
Associate Director, Projects

July 3, 1969

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

September 10, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Central African Republic - Education Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated September 10, 1971 from the Western Africa Department, entitled "Central African Republic - Proposed IDA Credit for an Education Project" (LC/0/71-100).

2. Comments, if any, should be sent to reach Mr. Fall (ext. 4744) by 5:00 p.m. on Wednesday, September 15.

3. It is planned then, if the Committee approves, to inform the Government that the Association is prepared to begin negotiations for the proposed credit on the terms and conditions referred to in the attached memorandum.

Dag F. Wittusen
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
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Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

CONFIDENTIAL

LC/O/71-100

September 10, 1971

LOAN COMMITTEE

Memorandum from the Western Africa Department

Central African Republic: Proposed IDA Credit for an education project

1. In June 1970, a UNESCO mission reviewed the educational objectives of the Central African Republic (CAR) following a Bank reconnaissance mission in December 1969. In February 1971, the Government requested IDA financial assistance for an education project prepared with the assistance from UNESCO. The attached Appraisal Report (PE 34) dated August 31, 1971, proposes a $3.2 million development credit to the Central African Republic. I propose to increase the credit to $3.5 million for the reasons set out in paragraph 8.

2. The proposed project would be our third operation in the CAR. A $4.2 million credit for the Bangui-M'Baïki road construction and a $4.3 million for highway maintenance were respectively signed in April 1969 and June 1970. On both projects execution has been slow at the beginning. However, the closing dates of March 31, 1973 and June 30, 1975 for respectively the road construction and the highway maintenance can still be met.

3. The five-year lending program is attached. A cotton development program has been prepared and could possibly be considered for IDA financing in FY 1973. No other project is scheduled for FY 1973, but preparation work is under way in transportation and livestock.

The Economy

4. An economic report (AW-16-a) dated May 27, 1970 distributed to the Executive Directors in June 1970 is being updated by an economic mission which visited the CAR in May 1971. The updated version will be issued before Board presentation of this credit.

5. The CAR economy has good economic potential based on diamonds, cotton, coffee, and uranium. Although coffee production has stagnated, cotton production had increased by 18 percent in 1968/69, and diamond production by 17 percent in 1968. Exports in the period 1966/70 had been higher than in any earlier period. They were expected to increase during 1971-73 because of the expected continued increase in cotton production and the export of over 500 tons of uranium ore per year, starting at the end of 1972. A CFAF 8 billion ($29 million) investment program to be spread over four years (1969-72) was under way for the uranium mining and processing plant. This investment of CFAF 2 billion annually, which was not included in the four-year Plan, corresponds to about 25 percent of the annual investments, public and private, under the Plan.

6. The CAR Government,however,faces increasingly serious financial difficulties. The budget which until 1966 had been in surplus, is showing growing deficits. This deterioration is largely due to a rapid increase of expenditures for administration, education and defense and to a slower growth of the economy since 1966. The need for corrective action was discussed during the negotiations of the Highway maintenance Credit in May 1970, and again during the economic updating mission in May 1971. There are indications that the Government recognizes the need for remedial action. Some measures to restrain current expenditures introduced during the preparation of the 1970 and 1971 budgets were a step in the right direction; restriction on all new recruitment and enforced retirement of civil servants at retirement age, withdrawal of government vehicles from ministers and senior officials, reduction both in number of students sent abroad and in the amount of scholarships given at home, and reduction of travel abroad and embassy personnel were timely taken. The Government also demonstrated its willingness to increase development expenditures by earmarking $1.6 million in the Road Fund in 1970 and committing itself for the same amount in 1971, in order to be able to meet recurrent maintenance cost generated by the $4.3 million IDA credit for highway maintenance.

7. However,the cumulative effect of the above mentioned measures, will prove insufficient in 1971 to further improve the budgetary situation. They will not be sufficient either because cotton, coffee and diamond productions will remain below previously attained levels, and because the production of uranium which was expected early 1972 will be delayed because of technical difficulties encountered during project implementation. In a letter dated July 12, 1971 we drew again the Government' attention to that situation. During negotiations of the project and discussions during the Annual Meeting, we will seek agreement to a program of financial

reform. While financial difficulties have not so far affected progress of our past operations as the Government has assigned the required funds to what they consider to be high priority projects, continued deterioration would clearly limit our ability to proceed with our longer term program; we will make it clear to the Government that the amount of finance we can provide will depend on their own performance.

8. Even with improved performance in public finance, it can hardly be expected that significant budget savings can be developed during the 1971 and 1972 budgets. Therefore, IDA must be prepared to finance a large part of the project costs including, inevitably, a considerable proportion of local expenditures. In the past IDA financed up to 88 percent of total project, net of taxes, but only covering the foreign exchange component. For the proposed educational project, in which the foreign exchange cost represents 65 percent of the project cost net of taxes, we propose financing of 87.5 percent of capital costs exclusive of import duties and local taxes, or about 50% of total cost, including the additional recurrent expenditures required during the implementation period. (see para. 14)

The Project

9. The proposed project would assist in the implementation of the government educational policy by (a) providing lower secondary facilities for the teaching of a broader curriculum; (b) adding science and practical subject rooms to four existing lycées; (c) improving the facilities for technical and commercial courses; (d) establishing a Teacher College, ENS, to train secondary school teachers; (e) helping with the preparation of a long-term educational development plan.

10. The project would consist of:

(a) Construction of and furniture and equipment for:

(i) four new lower secondary schools and extension of an existing one;

(ii) additional facilities for science and practical subjects in four lycées;

(iii) extension to the technical lycée;

(iv) a new secondary teacher training college;

(b) A unit for the implementation and overall supervision of the project.

(c) The preparation and implementation of plans for:

(i) Cost-saving devices in the framework of a long-term plan for the education and training system.

(ii) Training of secondary school teachers for practical subjects;

(iii) Scheme for the training of technical and commercial teachers.

11. To assist in the preparation of a long-term educational plan, the project would establish an education project unit and provide the services of an educational economist for one year to advise on educational finance and cost-saving devices. To ensure proper implementation, the project would include the services of an educator-administrator as adviser to the project director (three may-years), and a project architect (three man-years). Qualified counterparts should be assigned to work with all foreign experts.

12. The proposed credit would finance:

(a) 65 percent of the cost of civil works

(b) 80 percent of cost of the furniture and equipment if procured abroad or 65 percent of the cost if procured locally and

(c) 80 percent of the cost of the project administration and technical assistance.

13. Contracts for civil works and procurement of furniture and equipment would conform to the Bank/IDA guidelines on international competitive bidding. Domestic manufacturers would be allowed a preferential margin equal to the existing rate of import duty or 15 percent of the c.i.f. cost of competing imports, whichever is lower. The preferential treatment would be applied also to manufacturers from other countries of the Economic and Customs Union for Central Africa (UDEAC).

14. The total project cost is estimated at about $5.0 million of which $2.6 million would be foreign exchange and $1.0 million, or 20 percent, import duties. The proposed credit of $3.5 million would cover the foreign exchange costs plus about $0.9 million of local costs i.e. 87.5 percent of total cost, exclusive of import duties and other local taxes. The Government's contribution of 30 percent of total cost, of which 20 percent will be in the form of releasing taxes, constitues an adequate domestic effort, together with the increased recurrent costs of about $0.7 million annually which will be required by the proposed project.

Issues for the attention of the Loan Committee

15. The CAR Government has undertaken a series of nationalizations on which the status of settlement is as follows:

(a) In 1967 Société Equatoriale d'Energie Electrique (SEEE); agreement has been reached;

(b) In 1967 Union Electrique d'Outre Mer (UNELCO). The Government recognized the principle of compensation, but settlement has not been reached on the evaluation of the assets; since April 1970, we have received no information on this issue;

(c) The Agence Transéquatoriale des Communications (ATEC). In 1969 the Government withdrew from the convention establishing the Agence Transéquatoriale des Communications (ATEC), a multi-national transport agency jointly established with the Congo (B), Gabon, and Chad. The Government took over ATEC's transport facilities located on its territory and set up a national agency, Agence Centrafricaine des Communications fluviales (ACCF), to run them. ACCF is continuing transport services to the former ATEC partners under a series of bilateral agreements which have led to satisfactory cooperation.

(d) While withdrawing from ATEC, the Governments of the CAR and Congo(B) nationalized the Compagnie Générale des Transports en Afrique Equatoriale (CGTAE). Both Governments have reached a common position on the outstanding issue concerning the valuation of the assets of the company. Discussions between C. A. R., Congo (B), and the Company resumed in February 1971 and then broke off. In March 1971 the Company made a compromise proposal and in May informed us about the lack of response from the Congo Government. We have received no subsequent information.

(e) Mining Companies: In 1969, the three diamond mines in the CAR were closed by the Government in a dispute over mining rights. The discussions between the Government and the Diamond Distributors, Inc. (DDI) broken off in November 1970, started again in March 1971. An agreement was reached upon, resuming the activities of DDI as soon as a suitable mining code now under preparation is available and the DDI is able to raise $600,000, the necessary sum for reopening of the mines.

27. From the above, it is evident that there has been some progress in the settlement of nationalization disputes. The others are still too recent to consider the lack of final agreement. We propose, however, to press the delegation to speed up negotiations and reach an agreement. The influence we have had in bringing about solution in the diamond disputes justifies this course of action.

28. Aside from the nationalization disputes, an other issue is the budgetary situation. In a letter dated July 12, 1971, we drew the attention of the Government to the fact that a continued budgetary deficit would endanger our operations in the country. During negotiations of the proposed credit, if no decisive commitment on the control of recurrent expenditures is reached, we might have to consider reducing the pace of our operations after FY72, pending evidence of improvement in economic policy-making.

Recommendations

30. I recommend that the CAR Government be invited to send representatives to Washington to negotiate a credit of \$3.5 million for this project otherwise on the terms and conditions outlined in paragraphs 6.01, 6.02, and 6.03 of the attached Appraisal Report.

Roger Chaufournier
Director

Attachment.

Attachment

CAR - PAST LENDING OPERATIONS AND PROPOSED LENDING PROGRAM THROUGH FY1977

Population: 1.6 m
Per Cap. inc.: $127

		($ million)										
		Through 1969	1970	1971	1972	1973	1974	1975	1976	1977	1969-73	1973-77
Agriculture I Cotton	IDA					5.8						
Agriculture II Livestock	IDA						2.0					
Agriculture III Unid..	IDA									2.0		
Education I	IDA				3.5							
Education II	IDA									3.0		
Road I Bangui M'Baiki	IDA	4.2										
Road II Highway Maint.	IDA		4.3									
Road III Bangui Bossembele	IDA						4.0					
Road IV Sibut Bambari	IDA								3.0			
Operations Program	IDA				3.5	5.8	6.0	-	3.0	5.0	17.8	19.8
	No				1	1	2	-	1	2	4	6
Lending Program	IDA	4.2	4.3	-	3.5	4.0	4.0	2.0	-	3.0	16.0	13.0
	No	1	1	-	1	1	1	1	-	1	4	4
FED		40.7	0.5	6.0	6.0	6.0	6.0	6.0	n.a.	n.a.		
FAC		40.6	1.5	8.1	6.0	6.0	6.0	6.0	n.a.	n.a.		
IDA Gross Disbursements		-	-	1.6	2.6	3.5	1.9	3.8	5.3	4.5		
Net "		-	-	1.6	2.6	3.5	1.9	3.8	5.3	4.5		
Net Transfers		-	-	1.6	2.5	3.4	1.8	3.7	5.2	4.3		

Western Africa Department
September 8, 1971

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

September 9, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Mauritania - Proposed Livestock Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated September 9, 1971 from the Western Africa Department, entitled "Mauritania - Proposed Livestock Project" (LC/O/71-99).

2. Comments, if any, should be sent to reach Mr. Adams (ext. 4736) by 5:00 p.m. on Tuesday, September 14.

3. It is planned then, if the Committee approves, to inform the Government that the Association is prepared to begin negotiations for the proposed credit on the terms and conditions referred to in the attached memorandum.

Dag F. Wittusen
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
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Executive Vice President (IFC)
Vice President (IFC)

CONFIDENTIAL

LC/O/71-99

September 9, 1971

LOAN COMMITTEE

Memorandum from the Western Africa Department

MAURITANIA: Proposed Livestock Project

I. BACKGROUND

1. Attached is an appraisal report (PA-102), dated August 31, 1971, recommending an IDA credit of US$ 3.4 million equivalent to the Islamic Republic of Mauritania.

2. The proposed credit would be the Bank Group's fifth operation in Mauritania. In 1960 the Bank made a loan (249-FR) of US$ 66 million, to Mines de Fer de Mauritanie (MIFERMA), for the exploitation of iron ore; in 1964 an IDA credit (69-MAU) of $ 6.7 million was granted for a road construction project in which FED also participated; in 1968 IFC invested US$ 20.0 million in Société Minière de Mauritanie (SOMIMA), a company that is operating a copper mine; and in 1969 an IDA credit (159-MAU) of US$ 2.5 million equivalent was made for a highway maintenance project.

3. The five-year lending program (copy attached) calls for financing of small projects in agriculture, livestock, fisheries, education and transport. The next project is likely to be for improvement of the Nouadhibou fishing port.

II. THE ECONOMY

4. An economic report was circulated in July 1971. It concluded that Mauritania, being an extreme case of dual economy, has three major economic potentials: mining, livestock and fishing. However, rapid growth of the mining sector has only limited impact on economic development, since nearly half of its value added is transferred abroad, and since the privately-owned mining companies employ a limited number of Mauritanians. Economic growth will therefore be greatly determined by what actions will be taken to better exploit the growth potential in fishing and livestock. To allow implementation of a public development program of a size judged necessary, without creating budgetary problems, external aid should continue to be on concessional terms, except for projects that will create no demand on Government resources. The share which Mauritania would be able to contribute towards the cost of foreign-financed projects is on average well below the local cost component, particularly for projects in the rural sector. The Bank Group - together with other providers of foreign loan aid - should therefore be prepared to cover a substantial part of local expenditures and in certain cases of operating costs.

III. THE PROJECT

5. The proposed project, covering a four-year disbursement period, would comprise three main components as follows:

(a) Wells: including (i) reconstruction and/or repair of approximately 300 pastoral wells; (ii) establishment of two well-maintenance teams; and (iii) exploratory drilling for water at 10 sites within a sector of the Project area where there is inadequate information on ground water supply.

(b) Animal Health: involving the strengthening of the Livestock Service of the Ministry of Rural Development to enable it to carry on a campaign to vaccinate animals in the Project area against the important endemic diseases.

(c) Firebreaks: involving provision for equipment and organization for regular maintenance of approximately 6,500 km. of firebreaks within the Project area.

6. The repair and reconstruction of the proposed 300 wells would provide an adequate network for optimum use of pasture in the project area, in which over 40 percent of the country's cattle population is concentrated. The continuation of vaccination of cattle against endemic diseases will prevent recrudescence of rinderpest, which can cause mortalities of up to 50 percent of individual herds, and of contagious bovine pleuropneumonia. The rehabilitation and maintenance of the network of firebreaks will substantially reduce the present 40 percent average annual grass fire destruction of available pastures in the project area.

7. The project would be the responsibility of the Ministry of Rural Development. The Ministry of Civil Works and Labor and the Hydrological Services within the Ministry of Equipment would be concerned with some aspects of the Project. A Project Coordinating Commission would be appointed to advise on certain aspects of the wells and firebreaks component of the project, as well as on terms and conditions of engagement of well consultants. The legal arrangements for establishing interministerial cooperation will be discussed during negotiations.

8. Total costs of the project are estimated at about $US 4.8 million equivalent, comprising US$ 3.1 million capital costs and US$ 1.7 million operating costs during the four years of project execution. The IDA credit would cover the foreign exchange component of the investment costs (US$ 2.5 million equivalent) and an annually declining proportion of operating costs (from 80 percent in the first year to 20 percent in the fourth year) totalling about US$ 0.9 million equivalent over the disburse-

ment period. The combined Government contribution to investment costs and operating costs would reach a peak of $492,000 during the fourth year of project execution.

9. Contracts for well repair, reconstruction and purchase of vehicles would be subject to international competitive bidding. Vaccines are likely to be purchased from a veterinary laboratory in Dakar.

10. French bilateral aid agencies are contemplating financing animal health programs in the Project area. Discussions with a view to coordination between the FAC and IDA-financed project would be held prior to presentation of the proposed credit to the Executive Directors.

11. The appraisal report recommends that additional taxes be levied and collected on livestock within the Project area to cover services provided to livestock owners under the Project. The Agriculture Projects Department argues that inadequate budget provisions since independence led to the deterioration of these services in the first place and therefore would like to see the incremental taxes to be levied and collected by local authorities earmarked for the sustained operation of the well and firebreaks maintenance services.

I propose to seek from the Government an understanding that the yearly budget shall provide for adequate resources to cover the cost of these services, in accordance with an estimate agreed jointly between the Government and the Association. I do not favor an earmarking of resources limited to a given project area because:

(i) a tax confined to the Project area could jeopardize project implementation because it might incite cattle owners to avoid the area;

(ii) collection would be difficult;

(iii) the livestock sector is already heavily taxed in relation to the Government services it has been receiving. In addition, it is felt that this project aims at restoring and developing a major traditional activity. It therefore is more akin to extension actions than to provision of public services;

(iv) the Legal Department has advised that a tax (a) confined in its application to a portion of the territory of the Borrower and (b) the proceeds of which are to be earmarked for specific purposes, would require the adoption of special legislation.

Questions regarding grazing and watering rights will also have to be explored during negotiations.

12. Creation of the Project Coordinating Committee (see para. 7) would be a condition of effectiveness of the IDA credit, while disbursement of funds under the animal health component would be subject to employment of a veterinary officer acceptable to IDA.

13. The economic rate of return of the project is estimated at about 20 percent. This assumes that, without the project, the number of wells in the Project area would decrease to about 200, that the animal health component will reduce cattle mortality rates and increase calving rates, and that, as a result of protection of pastures from destruction by fire, livestock carried in the area could be increased by about 20 percent. However, achievement of the return is dependent on maintenance of the vaccination campaign for at least ten years and of the wells and firebreaks for at least thirty years. If these activities are not maintained beyond the disbursement period of the credit, the rate of return would be reduced to 14 percent.

IV. RECOMMENDATION

14. I recommend that the Association invite the Government of Mauritania to negotiate a credit of US$ 3.4 million for a Livestock Project substantially in accordance with recommendations set forth in Section VI of the Appraisal Report, except for the amendment proposed in paragraph 11 of this memorandum.

Roger Chaufournier
Director

Attachments

Population: 1.1 m
GNP Per Cap: $130

Attachment 1

IVa. MAURITANIA - 5 YEAR OPERATIONS AND LENDING PROGRAMS
(By Fiscal Year - Amounts in $ millions)

OPERATIONS PROGRAM			1971	1972	1973	1974	1975	1976
7-MTA-AX-01	Agricultural Unidentified	IDA					2.0	
7-MTA-AL-01	Livestock	IDA		3.4				
7-MTA-AI-01	Irrigation - Gorgol I	IDA			2.0			
7-MTA-EE-01	Education	IDA				2.0		
7-MTA-TH-03	Road Construction	IDA				3.0		
7-MTA-TP-01	Port Extension - Nouadhibou	IDA			3.0			
		IDA		3.4	5.0	5.0	2.0	
		No.		1	2	1	1	

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LM/M/71-36

September 3, 1971

Minutes of Special Loan Meeting to consider "Iraq - Telecommunications Project" held at 3:00 p.m. on Friday, August 20, 1971 in Conference Room B.

1. Present: Messrs. Cope (Chairman), Baum, Benjenk, Armstrong, Davar, El-Fishawy, Mitchell, Sathar, Vasudevan and Wittusen (Secretary).

2. Issue: The meeting was called to consider what the Bank's attitude should be if the Government were to disqualify any firm which submitted the lowest evaluated bid under the Bank's rules for international competitive bidding, on the grounds that the firm was on the Arab boycott list.

3. Discussion: The meeting noted that:

(i) During loan negotiations the Government agreed to observe the Bank's normal procedures governing procurement. An understanding was reached that there should be no specific clause in bid invitations and documents excluding consideration of any bid, except possibly from Israeli sources. In view of the sensitivity of Bank-Iraqi relations, the Iraqi anxiety that Bank procurement procedures should as far as possible not disturb Iraqi law (which covers the Arab boycott), and the feeling that boycotted firms might reasonably be expected not to bid, the question of what would happen if a boycotted firm submitted the lowest and otherwise satisfactory bid was not specifically raised with the Iraqis.

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Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
Controller

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The Economic Adviser to the President
Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

(ii) The Bank had made loans in the past to Arab nations despite the existence of the boycott. Few, if any, boycotted firms had submitted bids and no occasion had yet arisen calling for such a firm to be disqualified. On the other hand, the issue might be raised in principle by the Executive Directors; or, since boycotted firms were not excluded from bidding, one of them might be successful in submitting the lowest evaluated bid. Thus the Bank should have a policy on dealing with a borrower's decision to disqualify the bid of a boycotted firm.

(iii) The view expressed by the Public Utilities Projects Department was that the Bank should "live with" the boycott. The Bank's policy usually respected import duty arrangements legislated by Bank borrowers, as well as bilateral, regional and international preferential and trade arrangements such as Commonwealth Preference, etc. The Arab boycott could be considered a similar treaty. There was also a possibility that a boycotted firm might submit an unrealistically low bid in order to embarass an Arab borrowing member or to try to break the boycott. A further question that needed to be considered was whether a boycotted firm, if given the award, could carry out the project in an "efficient and economic" manner, since difficult relations with the Borrower could be anticipated.

4. <u>Decision</u>: The meeting concluded that:

(i) The Arab boycott, which was political in nature, should be distinguished from preferential and bilateral trade arrangements which were economic. Further, while it was possible that a boycotted firm might submit an unrealistically low bid, the Bank could effectively guard against it through the bid evaluation process.

(ii) If the lowest evaluated bid under the agreed procurement procedures was found to be that of a boycotted firm and the Borrower decided not to award the contract to that firm, this would preclude the Bank from disbursing against the project item.

(iii) Since understanding on the decision in (ii) above had not been specifically reached during negotiations, it would be desirable to inform the Government as soon as possible. The Area Department undertook to apprise the Iraqi Under-Secretary of Planning presently in Washington, of the Bank's thinking and inform him that the matter would be discussed more fully with the Iraqi delegation at the time of the Annual Meeting.

Dag F. Wittusen
Secretary

Cleared by: Messrs. Cope
Armstrong
Benjenk
El-Fishawy

Cleared in substance by Mr. Baum

cc: Loan Committee
Participants

FORM No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

September 3, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Uganda - Second Beef Ranching Development Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated August 31, 1971 from the Eastern Africa Department, entitled "Uganda - Second Beef Ranching Development Project" (LC/O/71-98).

2. Comments, if any, should be sent to reach Mr. Vita (ext. 4918) by 5:00 p.m. on Wednesday, September 8.

3. It is planned then, if the Committee approves, to inform the Government that the Association is prepared to begin negotiations for the proposed credit on the terms and conditions referred to in the attached memorandum.

Dag F. Wittusen
Secretary
Loan Committee

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Committee:

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Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
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LC/0/71-98

September 3, 1971

LOAN COMMITTEE

Memorandum from the Eastern Africa Department

UGANDA: Second Beef Ranching Development Project

I. INTRODUCTION

1. In furtherance of the agricultural diversification strategy enunciated in the Second Five-Year Development Plan, the Government of Uganda has initiated a long-term livestock development program which emphasizes the introduction of beef ranching on a commercial scale into underutilized and underpopulated areas of the country.

2. The Beef Ranching Project for which the Association extended a Credit (No. 130 UG) of $3 million in October 1968 was the pioneer effort under this program. This first project, while concentrating on the development of six large ranches, five of which were owned and operated by the Uganda Livestock Industries (ULI), a parastatal organization, also provided for the development of about 40 medium-sized ranches. This project, which is ahead of schedule, has been a success, and the performance of the medium-sized ranches (owned by cooperatives, small companies and individuals) in particular has prompted the formulation of the proposed follow-up project which envisages a greater role for the medium-sized rancher in the development of the beef industry.

3. The FY1972-76 Operations Program is attached.

II. THE PROJECT

4. The attached appraisal report (No. PA-98) recommends an IDA Credit of $6.6 million for the financing of the proposed project which is estimated to increase annual beef production by about 12 percent. The project would provide for:

(a) ranch infrastructure development, including construction of perimeter fencing, basic water storage and stock handling facilities and feeder roads;

(b) credit and technical services to:

(i) about 140 medium (500 head) sized breeding/fattening ranches,

(ii) one large (50,000 hectare) steer fattening ranch and

(iii) about 30 small mixed farms;

(c) training in ranch management for ranch managers, technicians and foremen;

(d) consultant services to assist Government in:

(i) reorganizing livestock and meat marketing services and establishing marketing agencies and

(ii) preparation of further livestock development projects.

5. The total cost of the project is estimated at $13.4 million equivalent. Fifty-one percent of the project financing will be provided from sources in Uganda as follows: the ranchers - $1.4 million (10%); participating commercial banks - $4.4 million (33%); and the Government - $1.0 million (8%). The balance, $6.6 million (49%), will be covered by the proposed IDA credit, which would include the entire foreign exchange component of $4.6 million and $2 million for local costs.

6. The project, which will exploit the untapped potential of Uganda's natural grasslands, will involve participation of about 13,000 heads of families. In addition to increasing the supply of beef, the project will serve to train a cadre of skilled people capable of undertaking further rapid expansion of the industry. The economic rate of return is estimated at 12 percent.

III. ISSUES AND HIGHLIGHTS

Ranch Infrastructure Development

7. Basic improvements, such as access roads, fencing, water storage, cattle yards and dips, which are essential for preparing new areas for ranching operations, would be carried out by the Government, but the total cost would be prorated among the individual ranchers served by the improvements who would repay the Government over a period of 20 years at an interest rate of 8 percent per annum.

Since such basic improvements must precede any on-ranch investments under this project, it is necessary to ensure that this work is fully coordinated with the plans for development of individual ranching enterprises. To this end, the Ministry of Animal Industry, Game and Fisheries (Animal Industry) which generally undertakes such work, would establish an adequately staffed and equipped Infrastructure Development Unit headed by a manager with qualifications and experience satisfactory to the Association. This unit would be placed under the control of the Project Director to ensure full coordination. The establishment of such a unit and the appointment of the Unit Manager would be a condition of effectiveness of the credit.

On-Ranch Development

8. The ranchers themselves would contribute in cash and kind (mostly cattle) over 20 percent of the on-ranch investments. The balance would be financed by loans channeled through commercial banks. These loans would be repaid over a period of up to 12 years (including up to 5 years of grace) and would carry interest at 8 percent per annum.

9. The proposed mechanics for the extension of credit to ranchers for on-ranch development and working capital are based on those employed successfully under the first project. The part of the proceeds of the IDA credit to be made available for on-ranch development would be relent by the Government in the first instance to the Uganda Commercial Bank (UCB), a wholly government-owned institution, under a subsidiary loan agreement acceptable to the Association. Under an administration agreement, also to be acceptable to the Association, the UCB would onlend funds to participating commercial banks willing to lend to ranchers. In addition to being a channel for onlending, the UCB would also operate as a participating bank. Individual ranch plans would be appraised by the Project Office which would determine the requirement for long-term credit and working capital. If that appraisal is positive, the Project Office would help the rancher to approach the participating commercial bank of his choice and notify that bank how much of the long-term credit required would be made available from the proceeds of the IDA credit and hence the balance of long-term credit and working capital that would have to be provided out of the bank's own funds. It would then be the responsibility of the commercial bank to appraise the credit risk.

10. Under the first project, the credit risk on IDA funds onlent to ranchers had been borne by the Government, and the participating commercial banks had been allowed a spread of 1.5 percent for their services as "disbursement agents". The credit risk borne by participating banks was limited to their own funds. For the second project, the appraisal report proposes that the commercial banks should also take on the credit risk for onlent IDA funds and that to compensate them for so doing the spread on relending IDA funds be increased to 3 percent. (See paragraph 3.30.)

Accordingly, if the ranchers select a participating bank other than the UCB, UCB would onlend IDA funds to such participating bank at 5 percent per annum for lending, together with the bank's own funds, to the rancher at 8 percent. If, however, UCB is acting as a commercial bank and lending directly to a rancher, UCB would receive the same spread of 3 percent, borrowing the proceeds of the IDA credit from the Government at 5 percent. If UCB is onlending to another commercial bank as agent for the Government, it would receive one half of one percent as a handling fee and thus borrow the proceeds of the IDA credit from the Government at 4½ percent.

11. Of the total loans to ranchers (including working capital) amounting to $8.1 million equivalent, $4.4 million equivalent would be from the commercial banks' own resources. Hence, the credit risk on approximately 54 percent of loans to ranchers will be borne by the commercial banks. I agree that we should try to encourage the commercial banks to increase their involvement in credit for agriculture and livestock. Changes in the existing Chattel Mortgage Law designed to strengthen enforceability, which would be a condition of effectiveness, will increase the value of the security available to commercial banks. But this measure and the offer of a 3 percent spread may not persuade them to increase their exposure, and we cannot force them to do so. As noted in the Appraisal Report, they have already expressed some reluctance. I therefore recommend, and the Agriculture Projects Department concurs, that, if we cannot reach an agreement satisfactory to the Association and the Government under which the commercial banks, which will be represented at the negotiations, would assume the full credit risk on onlent IDA funds, we should be prepared to revert to arrangements similar to those under the first project.

Mixed Farm Development

12. The proposed project includes a pilot venture into mixed-farm development, taking advantage of the management and technical resources mustered for the ranching project for monitoring and evaluating the results of such an experiment. About 30 small crop farms would be provided with funds required for livestock, pasture improvement, irrigation equipment, animal housing and disease control. The total cost of this component is estimated at $155,000 of which IDA would provide $95,000. It is hoped that the experience gained from this pilot project would enable Uganda to plan for a larger scale mixed-farm development project.

Project Management

13. As in the case of the first project, overall management and coordination will rest with the Project Office headed by a Project Director with qualifications and experience acceptable to the Association. A Project Committee, which consists of representatives of the various ministries involved would continue to provide guidance and assistance

to the Project Director. The Project Committee would be enlarged by including representatives of the Ministries of Finance and Planning and the Project Office would be strengthened by the addition of at least seven additional credit officers to process and supervise loans to ranches. In addition, as mentioned in paragraph 7 above, the Ranch Infrastructure Development Unit would be placed under the control of the Project Director, so as to ensure adequate coordination.

Marketing and Pricing Policy

14. The increased production of beef resulting from the proposed project would be fully absorbed by the domestic market. Given the emphasis in this project on increasing the production of beef in hitherto under-populated areas, an effective system to process, store, transport and distribute beef is essential. The Government has decided, in principle, to establish a Meat Commission with regulatory powers in respect of marketing of livestock, meat and dairy products, including pricing and import policy. This policy making body would be provided with technical support by a Livestock Marketing Division to be established within the Ministry of Animal Industry.

15. The proposed credit provides for consultants to survey and formulate recommendations on the reorganization of the marketing services and the operations of the Meat Commission, covering processing, storing, transport, grading and pricing and the policy, investment and control measures required. The members of the Meat Commission and the heads of the Meat Commission and the Livestock Marketing Division must be actively involved in this exercise,and the consultants would not be retained until these two entities had been established and their respective heads appointed.

16. In February 1971 the Government established a maximum retail price ceiling on a number of commodities including meat. If enforced, this regulation, which does not differentiate between grades of meat, could act as a disincentive to beef production; it is, moreover, contrary to understandings given under the first project. As a condition of presentation to the Executive Directors, we would require that the Government either repeal the existing regulation or modify it so as to permit differentiation between grades, pending the consultants' recommendations on the grading and pricing of meat. This may mean a delay of probably several months between negotiations and Board action. Some delay is, however, desirable in any case before making a decision to submit the credit to the Executive Directors (see paragraph 23 below).

Procurement

17. International competitive bidding would be followed for the procurement of fencing materials and heavy construction equipment required for ranch infrastructure development, totaling about US$750,000. Other physical inputs required for ranch infrastructure development, on-ranch

development and supporting services which are not suitable for bulk procurement through international competitive bidding would be obtained from local suppliers, many of whom represent international manufacturers. Competition among local suppliers is sufficiently keen to ensure economic procurement.

18. Procurement of breeding cows, bulls and feeder steers is dictated by the need to obtain improved breeds indigenous to East Africa and adapted to Ugandan conditions. Procurement would therefore be confined to Uganda and to Kenya, which has traditionally been a supplier of livestock to Uganda.

Training Program

19. The proposed credit provides fundsfor expanding the ongoing program for overseas training in ranch management and introducing an on-ranch training scheme in Uganda for foremen and technicians. This program would produce about a 100 trained personnel within four years. The plans and curriculum for the training program would be prepared by the Project Director and submitted to the Association for approval before the program is initiated. The Appraisal Report (paragraph 3.25) recommends that a deadline of nine months after effectiveness be specified for the submission of this program. There is no reason why preparation of the training program should not go ahead as soon as the credit is signed and delays in effectiveness are no reason for permitting delay in preparing the program. I therefore recommend, with the agreement of the Agriculture Projects Department, that the deadline should be one year after credit signature.

IV. COUNTRY SITUATION

20. Volume I of a report entitled "Economic Developments in East Africa" (Report No. AE-16a) was distributed to the Executive Directors on July 16, 1971. Section D of this volume reviews economic developments in Uganda. While, as the report noted, the management of public finances was generally sound during the first four years of the Second Five-Year Plan (1966-1971), a considerable deterioration occurred in 1970/71. Capital expenditure, in part due to large-scale military procurement by the new government, was higher than anticipated. The recurrent budget surplus and medium- or long-term borrowing were inadequate to meet this increased expenditure, and there was a large net deficit which was covered by short-term borrowing mainly from the Bank of Uganda.

21. The 1971/72 budget estimates, if maintained in practice, would certainly help to restore financial stability. However, 28 percent of the reduced capital budget has been allocated for defense, at the expense of funds for projects of a development nature. It is moreover known that,

after the coup, there was a considerable amount of unauthorized spending, mainly by the military. The Finance Minister is trying very hard to keep control overall government spending; his problem is essentially to control spending by President Amin himself, who is reported to have recently made a number of commitments to purchase arms, including jet aircraft.

22. The deterioration in the fiscal situation was accompanied by a worsening of the balance of payments and a decline in foreign exchange reserves from \$82 million in September 1970 to \$53 million in April 1971. In June this year, the Government entered into a \$10 million Standby Agreement with the IMF undertaking to limit borrowing from the banking system, to avoid further commitments of contractor finance or suppliers' credit and to maintain at least an agreed minimum level of external assets, including SDR's. Both the Government's short-term borrowing from the Central Bank and the Bank's external assets are now close to the new limits. We have already, and shall continue, to express our concern to the Ugandan authorities and made clear that their performance and the progress of our lending operations are closely related.

23. The economic situation in Uganda is obviously difficult. The political situation is uneasy and, if incidents such as the reported recent border skirmish between Tanzanian and Ugandan troops continue, the repercussions both within Uganda and within East Africa could have a serious effect on Bank Group operations. We therefore intend to keep in close touch with the situation, in cooperation with the Fund. A mission will go to Uganda before the end of 1971 and in any event prior to a decision to present this project to the Executive Directors.

24. The latest Country Program Paper for Uganda (March 18, 1971) justifies financing for some local expenditures on the grounds that the amount of foreign aid which Uganda can use effectively exceeds the foreign costs of priority projects suitable for external financing.

V. RECOMMENDATION

25. I recommend that the Association invite representatives of the Republic of Uganda to negotiate a credit of \$6.6 million equivalent for a Second Beef Ranching Development Project substantially on terms and conditions set forth in the Appraisal Report, subject to the modifications proposed in paragraphs 11 and 19 of this memorandum.

J. H. Williams
Deputy Director

Attachment: Five-Year Operations Program

Attachment

Population: 8.1 m
Per Cap Inc: $110

UGANDA - FIVE-YEAR OPERATIONS PROGRAM

		($ million) Fiscal Years				
		1972	1973	1974	1975	1976
Agricultural Credit I	IDA			6.0		
Livestock II	IDA	6.6				
Livestock III	IDA					8.0
Cotton	IDA			9.0		
Smallholder Tea	IDA	6.0				
Tobacco II	IDA				7.0	
Smallholder Tea II	IDA					6.0
Horticulture	IDA				4.0	
Agriculture Unidentified	IDA					7.0
Education III	IDA				10.0	
Industry	IBRD				3.0	
Murchison Falls Power	IBRD					40.0
Tourism	IBRD			5.0		
Highways III	IDA		7.0			
Highways IV	IDA					10.0
Urban	IDA				5.0	
Water Supply - Kampala	IBRD		7.0			
Operations Program	IBRD	-	7.0	5.0	3.0	40.0
	IDA	12.6	7.0	15.0	26.0	31.0
	Total	12.6	14.0	20.0	29.0	71.0
	No.	2	2	3	5	5

Eastern Africa Department
August 30, 1971

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LM/M/71-35

September 3, 1971

Minutes of Special Loan Meeting to consider "Morocco - Second Agricultural Credit Project" held on August 25, 1971 in Conference Room B.

1. Present: Messrs. Knapp (Chairman), Cope, Broches, Baum, Benjenk, Evans, Asfour, El-Fishawy, Goffin, T.M. Jones, Stevenson, Wapenhans and Wittusen (Secretary).

2. Issues: The meeting was called to consider two memoranda to Mr. Cope, Mr. Benjenk's dated August 19, 1971 and Mr. Evans' dated August 20, 1971, on the interest rate at which CNCA would relend Bank funds. The Agriculture Projects Department had recommended an 8% relending rate, while the Area Department, maintaining that 8% was unacceptably high to the Government, had recommended a lower rate. The issues for discussion were:

(i) at what relending rate should the Bank's funds be employed, and

(ii) whether to insist that CNCA charge this interest rate on all its lending operations.

3. Level of Relending Rate. The meeting noted that:

(i) To ensure the efficient allocation of resources, the relending rate should bear some relation to the real cost of capital. The cost of capital, rate of return from the project and relative financial strength of the beneficiaries (mainly large farmers) did not justify a less than 8% relending rate. The Area Department, however, stated that the problem was not misallocation

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Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
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of loan capital in agriculture but its low volume. Raising the interest rate was likely to discourage private investment in agriculture.

(ii) The Area Department further maintained that increasing CNCA's lending rate from 6 1/2% to 8% for medium-term agricultural loans, making them more expensive than industrial loans, would be unacceptable to the Government. BNDE presently lends at 9% to industrial borrowers but the Government pays the borrower a refund of 2%, making a net rate of 7%. If the Bank insisted on an 8% relending rate for CNCA the Government was certain to insist on similar rebates for agricultural loans.

(iii) The general structure of interest rates in Morocco had remained unsatisfactory for some time and at some point the Bank should insist that the rate structure reflect more properly the cost of capital.

(iv) Several times in the past the Bank had been deadlocked with the Government on the same issue. It would be unfortunate if the Bank made a strong stand on the issue only to back down again.

4. Uniformity of Interest Rates. The meeting noted that:

(i) If the short-term interest rate remained 6% and the medium-term rate was set at 8%, farmers might borrow short-term and invest long-term. This might upset the financial structure and be cumbersome to administer.

(ii) Uniform interest rates on project and non-project funds would contribute to a more efficient application of project funds. Similar projects in other countries indicated that when a lower rate than that charged for project funds was available, project funds might remain largely unused.

(iii) On the other hand, it might not be possible to get CNCA to adjust its lending rates on non-project funds. CNCA might want to employ a differential rate structure or other means to provide selective incentives for agricultural investments.

5. Decision: The meeting concluded that:

(i) Bank funds should be relent at 8% interest rate without subsidies or rebates.

(ii) The Bank should press CNCA to make corresponding adjustments on its rates for other lending operations. But the Bank should not insist on an across-the-board increase of rates for all lending as long as CNCA advanced proposals which would ensure the prompt utilization and efficient allocation of the loan proceeds.

Dag F. Wittusen
Secretary

Cleared by: Messrs. Knapp
Broches/El-Fishawy
Benjenk/Asfour
Stevenson
Wapenhans

cc: Loan Committee
Participants

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LM/M/71-35

September 3, 1971

Minutes of Special Loan Meeting to consider "Morocco - Second Agricultural Credit Project" held on August 25, 1971 in Conference Room B.

1. Present: Messrs. Knapp (Chairman), Cope, Broches, Baum, Benjenk, Evans, Asfour, El-Fishawy, Goffin, T.M. Jones, Stevenson, Wapenhans and Wittusen (Secretary).

2. Issues: The meeting was called to consider two memoranda to Mr. Cope, Mr. Benjenk's dated August 19, 1971 and Mr. Evans' dated August 20, 1971, on the interest rate at which CNCA would relend Bank funds. The Agriculture Projects Department had recommended an 8% relending rate, while the Area Department, maintaining that 8% was unacceptably high to the Government, had recommended a lower rate. The issues for discussion were:

(i) at what relending rate should the Bank's funds be employed, and

(ii) whether to insist that CNCA charge this interest rate on all its lending operations.

3. Level of Relending Rate. The meeting noted that:

(i) To ensure the efficient allocation of resources, the relending rate should bear some relation to the real cost of capital. The cost of capital, rate of return from the project and relative financial strength of the beneficiaries (mainly large farmers) did not justify a less than 8% relending rate. The Area Department, however, stated that the problem was not misallocation

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Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
Controller

Copies for Information:

President
The Economic Adviser to the President
Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

of loan capital in agriculture but its low volume. Raising the interest rate was likely to discourage private investment in agriculture.

(ii) The Area Department further maintained that increasing CNCA's lending rate from 6 1/2% to 8% for medium-term agricultural loans, making them more expensive than industrial loans, would be unacceptable to the Government. BNDE presently lends at 9% to industrial borrowers but the Government pays the borrower a refund of 2%, making a net rate of 7%. If the Bank insisted on an 8% relending rate for CNCA the Government was certain to insist on similar rebates for agricultural loans.

(iii) The general structure of interest rates in Morocco had remained unsatisfactory for some time and at some point the Bank should insist that the rate structure reflect more properly the cost of capital.

(iv) Several times in the past the Bank had been deadlocked with the Government on the same issue. It would be unfortunate if the Bank made a strong stand on the issue only to back down again.

4. Uniformity of Interest Rates. The meeting noted that:

(i) If the short-term interest rate remained 6% and the medium-term rate was set at 8%, farmers might borrow short-term and invest long-term. This might upset the financial structure and be cumbersome to administer.

(ii) Uniform interest rates on project and non-project funds would contribute to a more efficient application of project funds. Similar projects in other countries indicated that when a lower rate than that charged for project funds was available, project funds might remain largely unused.

(iii) On the other hand, it might not be possible to get CNCA to adjust its lending rates on non-project funds. CNCA might want to employ a differential rate structure or other means to provide selective incentives for agricultural investments.

5. Decision: The meeting concluded that:

(i) Bank funds should be relent at 8% interest rate without subsidies or rebates.

(ii) The Bank should press CNCA to make corresponding adjustments on its rates for other lending operations. But the Bank should not insist on an across-the-board increase of rates for all lending as long as CNCA advanced proposals which would ensure the prompt utilization and efficient allocation of the loan proceeds.

Dag F. Wittusen
Secretary

Cleared by: Messrs. Knapp
Broches/El-Fishawy
Benjenk/Asfour
Stevenson
Wapenhans

cc: Loan Committee
Participants

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

August 30, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Dahomey - Zou-Borgou Cotton Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated August 30, 1971 from the Western Africa Department, entitled "Dahomey - Proposed Credit for a Cotton Project" (LC/O/71-97).

2. Comments, if any, should be sent to reach Mr. Schott (ext. 4758) by 5:00 p.m. on Thursday, September 2.

3. It is planned then, if the Committee approves, to inform the Government that the Association is prepared to begin negotiations for the proposed credit on the terms and conditions referred to in the attached memorandum.

Dag F. Wittusen
Secretary
Loan Committee

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LC/O/71-97

LOAN COMMITTEE

August 30, 1971

Memorandum from the Western Africa Department

DAHOMEY: Proposed Credit for a Cotton Project

Introduction

1. Attached for the consideration of the Committee is Report No. PA-99 entitled "Dahomey—Zou-Borgou Cotton Project." It recommends an IDA credit of US$5.7 million. In 1969 the Government of Dahomey requested IDA financing for an agricultural development project based on cotton in the districts of Zou and Borgou. The project was prepared by PMWA during 1969 and 1970 with the assistance of the Government, CFDT (Compagnie Française pour le Développement des fibres Textiles) and SATEC (Société d'Aide Technique et de Coopération). The project was appraised in January, 1971.

2. The proposed credit would be IDA's third operation in Dahomey. In March, 1969, IDA made a credit of US$4.6 million for the development of oil palm and food crop production (Hinvi Agricultural Project, Credit No. 144-DA), which became effective on August 5, 1969. Several important problems have beset this project and a memorandum proposing corrective measures was submitted to Mr. Knapp on August 13, 1971. In September, 1970, IDA made a second credit of US$3.5 million for a highway maintenance and engineering project which became effective on April 8, 1971. Project execution is satisfactory.

The Economy

3. Dahomey is one of the poorest of our member countries, and it has few natural resources that can be quickly or easily developed. The country's economic growth in the past decade has been very slow. Although progress has been made in solving some of its problems in external trade and public finance, the country's economic situation is still very serious.

4. From partial indicators, it appears that for the last three years there has been a mild acceleration of the very slow rate of growth (4.5 percent a year at current prices during the period 1960-68) mainly as a result of increased exports and unofficial transit trade with Nigeria. Considering the rapid population growth (2.8 percent per annum) and the general increase in prices (about 3 percent per annum), it is most likely that real per capita income has remained stagnant and does not exceed $70. There are, however,

some encouraging signs of progress in agriculture. The oil palm plantation program has developed favorably and cotton production increased more than threefold over the period 1965-66 to 1968-69; exports of these crops increased rapidly during the last three years. On the other hand, little progress was made in the development of food crop production in the same period. Expansion of the oil palm and cotton programs, in which the Bank Group is involved, will continue to be the most important growth factor for Dahomey's economy during the coming five years.

5. Agricultural products represent about 90 percent of Dahomey's exports, with palm products accounting for about 31 percent and cotton for about 14 percent. Cotton production has grown rapidly from 1,400 tons in 1964 to 35,000 in 1970. It is expected to reach 80,000 tons in 1974. The present project will account for about 31,000 tons of this increase. Other agricultural exports include groundnuts and some cocoa smuggled from Nigeria. At present rice imports amount to about 7,000 tons, valued at US$1.0 million. Food crops occupy about 66 percent of the cultivated area, maize being the main crop.

6. At the core of Dahomey's economic difficulties is the Government budget. Since independence, Dahomey has suffered from chronic budget deficits that have been financed through French budget support. The main structural reason for this situation is personnel expenditures which rose to a very high level in the early days of independence and have continued to increase rapidly since then. Moreover, school leavers cannot find employment opportunities in the private sector and thus exert a constant pressure on the Government's recruitment policy. Scaling down current budgetary expenditures to match current receipts will remain the basic issue of the Government's financial policy in the near future.

7. The Bank has been concerned about Dahomey's precarious financial situation for several years. Hence, before negotiating the present project we are seeking agreement with the Government on specific actions to improve its budgetary performance. For this purpose, a two-man mission is presently visiting Dahomey, and our forthcoming economic mission (late 1971 or early 1972) will discuss with the Government a program for further measures to improve the present tax system and expenditure control.

8. However, in the long run, only the broadening of the tax base is likely to bring about a permanent improvement in public finance. In this respect the cotton project, by its important direct and indirect effects on the country's growth prospects, will make a substantial contribution to the improvement of the Government's financial situation.

The Project

9. The project aims at developing cotton production by extending cotton growing areas in two large districts, the Borgou and the Zou, from 29,000 ha. to 59,000 ha. over a four-year period. The number of farmers growing cotton would increase from 29,000 to 41,000. Production of maize and groundnuts, grown in rotation with cotton, is also expected to double. In addition, rice production would be developed on some 3,300 ha. and rice milling facilities provided. This project would be the final phase of a program supported up to now with financial and technical assistance from France and managed by CFDT in the Borgou and by SATEC in the Zou. The present program which started in 1966 represents one of the best means, foreseeable at this time, of substantially improving the standard of living of a large segment of the rural population and improving Dahomey's balance of payments.

10. The project would cover the four-year period 1971-74. Its principal components would be:

a) staffing and equipping the "Société Nationale Agricole pour le Coton" (SONACO), which will administer extension, credit and marketing services;

b) establishment of a revolving fund to provide cotton growers with seasonal and medium-term credit;

c) construction of two additional ginneries in the project area to increase annual ginning capacity from 43,000 tons of seed cotton to 67,000 tons and provision of six small rice mills to process 3,600 tons of paddy;

d) rehabilitation of about 610 km of feeder roads;

e) execution of field trials to adapt research results for practical application;

f) provision of funds for preparation of an agricultural diversification project in the Borgou and Zou districts.

11. The extension methods will aim at inducing Borgou growers successively (i) to use fertilizers in addition to insecticides which are mandatory already; (ii) to grow cotton in blocks and observe crop rotations; and (iii) to use animal drawn farm implements. In the Zou district, most farmers have already mastered stage two above, and due to the lack of draught animals in this area, the farmers will generally not move to stage three. Fertilizers are presently being subsidized by FED, but the subsidy will be phased out gradually. If necessary, the Government will continue the subsidies if FED discontinues its support policy. Gradual elimination of the subsidies is deemed advisable in order to avoid discouraging their use through a sudden price increase.

12. Total project costs (including taxes --$350,000, but not including import duties from which the project will be exempt) are estimated at about US$11.8 million equivalent, of which about US$5.4 million will be for agricultural extension and operating expenses of SONACO, US$1.5 million for processing plants, US$0.6 million for the feeder road improvement program, US$0.6 million for the research program and crop diversification studies, and US$2.7 million for a revolving credit fund to finance seasonal and medium term credits for fertilizers, insecticides and implements. The balance of project costs consists of a reserve for contingencies. The foreign exchange component is estimated at $7.1 million or 60 percent of total project cost. The proposed credit of 5.7 million would finance 48 percent of the project. FAC would contribute $2.9 million, 24.5 percent, and thus finance the balance of the foreign exchange component and part of local cost. The Government would contribute through FAS $3.2 million equivalent or 27.5 percent of total project cost. FAC's contribution would be in the form of a grant and $1.0 million of it will be used to meet the bulk of project costs in calendar 1971.

13. Disbursement of the proposed credit would be made against (i) 100 percent of the cost of goods, c.i.f. Cotonou, imported for the project; (ii) 90 percent of the cost of office equipment and furniture, building and road construction, applied research and study; (iii) 39 percent[1/] of the total costs, c.i.f. Cotonou, of fertilizers, insecticides and agricultural equipment. Procurement would be by international competitive bidding where orders and contracts are of a sufficient value to justify this procedure; goods and services procured in this way are estimated to have a value of US$7.5 million.

14. Organization: Overall responsibility for the project would rest with the Ministry of Rural Development and Cooperation which would delegate operational responsibility to a recently established "Société Nationale Agricole pour le Coton" (SONACO), an autonomous government corporation. The latter's functions will include the preparation and administration of programs for cotton and other annual crops cultivated by the cotton growers, and it will contract with SATEC and CFDT for the necessary management and technical assistance. SONACO's Secretary General will be provided by CFDT and appointments to key posts in SONACO will be made under conditions acceptable to IDA. SATEC and CFDT will each provide a chief of operations and administrative and training officers to assist in managing the project in their respective districts.

1/ 39 percent of total purchases of annual inputs equals 90 percent of total purchases in the first project year and 90 percent of incremental requirements in the following years.

15. Both CFDT and SATEC are French public technical assistance agencies for agricultural development. CFDT was established especially to develop the production and marketing of textile fibers; its achievements in developing cotton production in African countries are well known. Moreover, an important feature of the project is the creation of a joint venture between the Government and CFDT for the purchasing, processing and marketing of cotton. Under their contract, CFDT and the Government would place their industrial and commercial assets at the disposal of the joint venture although they would each keep the ownership of these assets and remain separately responsible for the repayments of any debt incurred to finance them. CFDT would manage the joint venture and be responsible to a committee comprising three members appointed by the Government and three by CFDT. This agreement will replace an existing agreement between CFDT and the Government, signed in 1967 for ten years. CFDT will receive fixed fees for its services and 20 percent of profits. It will participate in losses to the extent of 25 percent of its cumulative share of profits. Certain unresolved legal issues arising out of the above arrangements are being discussed by the mission presently visiting Dahomey.

16. Stabilization Fund: The Government's share of profits from the joint venture with CFDT would be paid into the "Fonds Autonome de Stabilisation et de Soutien des Prix des Produits à l'Exportation" (FAS), a governmental agency which guarantees minimum producer prices for Dahomey's principal export crops. In turn FAS would help finance SONACO's operations as well as accumulating sufficient reserves to stabilize cotton prices as required. Producer prices would be established in consultation with IDA to assure that FAS' accounts are maintained on a sound financial basis.

17. The appraisal report states that submission of a plan by the Government to strengthen the management and accounting procedures of FAS should be a condition of Board presentation. Although the proper functioning of FAS is essential to the operation of the project, the deficiencies in that organization are not such as should in any way delay presentation of the project to the Executive Directors. Therefore, we feel that it would be sufficient to make submission of a plan for corrective action, as well as implementation of it, a condition of effectiveness.

18. Credit: Seasonal and medium term credit would be provided to participating farmers through a revolving fund managed by SONACO. CFDT and SATEC would assure collection of the credits by deducting payments from the proceeds of the farmer's cotton sales. Interest rates on both seasonal and medium term credit would be about 8 percent. It is intended that the revolving credit fund would eventually be transferred to the Banque Dahoméenne de Développement after its forthcoming reorganization.

19. Rate of Return: Assuming a project life of 20 years, the economic rate of return on the project, including the cost of the road improvements and the applied research program and taking only cotton production into consideration, is estimated at 54 percent. If a decrease of 15 percent in revenue from either lower yields or prices were assumed, the rate of return would fall to about 33 percent. The project is expected to yield total net foreign exchange earnings of US$27.0 million over the entire project life at a discount rate of 9 percent. Some 41,000 farmers of whom 12,000 would be new cotton growers, would benefit from the project; and, by the end of the project development period, the increase in the average annual net cash return to new cotton farmers is expected to reach about $100.

Recommendation

20. I recommend that representatives of the Republic of Dahomey be invited to negotiate a credit of US$5.7 million equivalent to assist in the financing of this project, substantially in accordance with the terms and conditions set forth in paragraphs 9.01 through 9.04 of the appraisal report, with the exception that the condition of Board presentation contained in paragraph 9.02 (b) be made a condition of effectiveness as stated in paragraph 17 above.

Roger Chaufournier
Director

Attachment: Five-year Lending Program

D A H O M E Y

POPULATION: 2.5M

GNP PER CAP: $ 80

\- 5 YEAR OPERATIONS AND LENDING PROGRAMS
(BY FISCAL YEAR - AMOUNTS IN $ MILLIONS)

OPERATIONS PROGRAM

			1972	1973	1974	1975	1976
7-DAH-AC-01	AGRIC.CREDIT	IDA				1.0	
7-DAH-AD-02	COTTON DEVELOPMENT	IDA	5.7				
7-DAH-AD-03	COTTON & FOOD CROPS	IDA			2.5		
7-DAH-AX-01	AGRICULTURE UNIDENT I	IDA					2.0
7-DAH-CC-01	TELECOMMUNICATIONS	IDA					2.0
7-DAH-EE-01	EDUCATION REGIONAL	IDA			2.5		
7-DAH-EE-02	EDUCATION VOCATIONAL	IDA					2.0
7-DAH-TH-02	ROAD CONSTRUCTION I	IDA		4.0			
7-DAH-TH-03	ROAD CONSTRUCTION II	IDA				4.0	
7-DAH-TP-01	PORT	IDA				3.0	

	1964-68	1969-73	1972-76
IBRD			
IDA		17.8	28.7
TOTAL		17.8	28.7
NO		4	10

	1972	1973	1974	1975	1976
IBRD					
IDA	5.7	4.0	5.0	8.0	6.0
TOTAL	5.7	4.0	5.0	8.0	6.0
NO	1	1	2	3	3

LENDING PROGRAM (3/25/71)

	1964-68	1969-73	1972-76
IBRD			
IDA		18.1	25.0
TOTAL		18.1	25.0
NO		4	7

	1972	1973	1974	1975	1976
IBRD					
IDA	6.0	4.0	5.0	4.0	6.0
TOTAL	6.0	4.0	5.0	4.0	6.0
NO	1	1	2	1	2

P & B 08/13/71

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LC/A/71-11

August 27, 1971

NOTICE OF MEETING

A meeting of the Loan Committee will be held on Tuesday, August 31, 1971 at 3:30 p.m. in the Board Room.

AGENDA

Ghana - Sugar Rehabiliation Project

The Committee will consider the attached memorandum dated August 27, 1971 from the Western Africa Department, entitled "Ghana - Proposed Sugar Rehabilitation Project" (LC/O/71-96) and the accompanying green cover appraisal report.

Dag F. Wittusen
Secretary
Loan Committee

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Committee:

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Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
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Vice President (IFC)

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LC/O/71-96

LOAN COMMITTE

August 27, 1971

Memorandum from the Western Africa Department

GHANA - Proposed Sugar Rehabilitation Project

1. Attached is an Appraisal Report (No. PA-100) dated August 16, 1971, recommending Bank Group assistance of up to US$16 million to the Government of Ghana to help finance the rehabilitation of the Ghanaian sugar industry. The proposed Bank Group assistance would be the first operation out of an expected three in Ghana in the current fiscal year. An education project was appraised last February and is scheduled to be submitted to the Executive Directors early in 1972. A road rehabilitation project will be appraised in September. Last June, IDA approved a credit of US$7.1 million for the expansion of power distribution facilities; it was the only Bank Group operation in FY 1971.

2. The proposed Bank Group assistance for the sugar rehabilitation project would be the third for agricultural development, following IDA credits of $8.5 million for the rehabilitation and replanting of cocoa and of US$1.3 million for a fisheries project. Attached is a table summarizing a proposed 5-year lending program for the period FY 1972-76. It is intended to submit this program for approval of the President in connection with the next country program review for Ghana in November.

The Economy

3. An economic mission visited Ghana in April 1971 and its report is about to be completed. It is designed primarily as background documentation for the next debt conference between Ghana and her creditors, to be held sometime before mid-1972, possibly before the end of this year. The report focuses on balance of payments prospects, Ghana's debt situation, preparation of a medium-term development plan, sectoral development strategies, as well as on recent developments and performance during the last year. Discussions of the draft report are to be held in Ghana in mid-September.

4. The preliminary conclusions of the mission confirm that Ghana's balance of payments position continues to be a major constraint on development. The recent fall in cocoa prices has exacerbated the situation and debt service payments remain heavy. Moreover, the Government's attempt last year to eliminate cumbersome licensing restrictions on imports led to a substantial increase in imports. At the same time, the Government has made progress towards promoting new exports as well as import substitution. Nevertheless, the short term balance of payments outlook is exceedingly tight. But even in the longer term, Ghana's export growth will be slow and its large external financing requirements will have to be met to a large extent by external loans on concessionary terms. Ghana remains only marginally creditworthy for lending on conventional terms.

5. In announcing the budget for FY 1972, the Government outlined a number of important policy measures designed to promote agricultural production, to diversify exports and control imports, to raise additional revenues and to check the growth of current expenditures. An increase in the discount rate from 5½ to 8 percent plus various other monetary levies supplement the Government's action on the fiscal and balance of payments side. While the impact of these policy decisions has not yet been fully assessed, they are an important step towards accelerating economic growth while attempting to maintain internal and external stability. They conform largely to the measures recommended by the Bank and bilateral donors in connection with the Consultative Group Meeting last December. They are an encouraging sign after a period of some indecision in economic management.

The Project

6. The project is designed to stimulate the production of a commodity which is at present almost entirely imported and for which fairly rapid demand growth is forecast. Ghana's sugar industry was started under the Nkrumah regime with two sugar producing units, one at Asutsuare and one at Komenda, each with plantations and factories and surrounded by outgrowers. It began operations in 1967. Despite relatively good agricultural conditions, the enterprises have failed, mainly through poor planning and execution of the industry, and inadequate management. As a result, factory efficiency has been very low, and production has been only a fraction of capacity. Very heavy financial losses have been carried by the central government since the start of production.

7. Sugar consumption in Ghana has continued to grow despite a rising price trend since 1967 and restrictive import licensing requirements until early 1970. In 1969, total consumption of sugar reached 71,000 tons or over 8 kilograms per capita, compared to 4.5 kilograms in 1963. This level of consumption is about 2 kilograms below the average for Africa but is expected to continue to increase, so that total consumption in 1978 would be around 100,000 tons. In the absence of the rehabilitation and efficient operation of the industry, practically all the sugar would have to be imported at an estimated cost of US$160 per ton, i.e., a total cost of $16 million per annum.

8. The proposed project would provide funds and necessary technical expertise to rehabilitate the existing factories and plantations as well as to improve the outgrowers' schemes. Funds for studies of further expansion are included in the project, which in its present form should be seen only as a first phase. The project aims to expand cane production to meet factory capacities. Specifically, the project would comprise replanting 9,200 acres of estate cane, expansion of estate acreage by 2,800 acres and farmers' acreage by 3,800 acres. Under the project, field and factory machinery and equipment would be rehabilitated, efficient management provided and Ghanaian personnel trained. Credit would be provided to the cane farmers through the Agricultural Development Bank which itself would receive technical assistance to re-organize its credit accounting and control methods.

9. The project will be managed by the to-be-formed Ghana Sugar Company (GSC), an autonomous public corporation which would take over the existing factories and estates from the Sugar Division of the Ghana Industrial Holding Company (GIHOC) in order to improve the present management control of Ghana's sugar industry. A major cost to the project will be the employment of an experienced expatriate management team to train Ghanaians and to run the new company. This is considered essential to the success of the enterprise.

10. The project is justified by the benefits anticipated from the additional sugar to be produced, by its foreign exchange savings, and substantial indirect benefits. Sugar production under the project should increase from about 2,600 tons before implementation to 44,700 tons by 1977/78. The increase is due both to higher cane supplies and an improvement in sugar recovery. The expected growth in consumption of sugar, however, will mean that despite this increase imports will still be on the level of those in 1967, but the share of domestic production in total consumption will rise from 3 percent to 43 percent.

11. The economic rate of return for the project is estimated at 14.5 percent for the two estates and factories jointly. Using a shadow wage of N₵0.50, i.e., two-thirds the official minimum wage, to reflect the low productivity of alternative occupations and the under-employment in Ghana, and a shadow exchange rate of US$1 = N₵1.50, the rate of return is 18 percent. If the estimated benefits were reduced by 10 percent the rate of return would fall to 12 percent. In all these calculations, the assumptions may be considered conservative, especially those for cane yields, and sugar recovery. The project's economic justification has been calculated by considering the investments made in the past at Asutsuare as "sunk costs".

12. The free world market price of raw sugar in the late 1970's is estimated at US¢4.5 per pound f.o.b. Caribbean ports. This corresponds to a c.i.f. Ghana price for refined sugar of US¢7.2 per pound or N₵164.5 per ton. The following decade the price is assumed to rise to the upper limit of the present International Sugar Agreement range, giving a Ghana import price of N₵182.8 per ton. Using these prices and a discount rate of 11 percent, the present worth of the net foreign exchange benefits for the life of the project would amount to US$12.5 million. Comparing this with the local costs of the project, also discounted at 11 percent, the effective rate of exchange for the project equals N₵0.60 per U. S. dollar, which is 70 percent more favorable than the official rate of N₵1.02 per U. S. dollar and 150 percent more favorable at the shadow exchange rate of N₵1.50 to per U. S. dollar.

13. Other significant benefits of the project include: the employment of about 6,700 estate and farm workers of whom about 5,000 would be liable to lose employment if the alternative of closing the industry were taken; the conversion of a cash deficit in the sugar industry to an annual cash income of about N₵3.5 million. (The financial rate of return for GSC is estimated at an acceptable 13 percent.) The net gain to Government revenue, assuming current levels of duties on sugar imports, would be about N₵2.8 million per year. The ADB, whose activities are crucial to the Government's agricultural policies, will be significantly strengthened

by participation in the project (discussed in paragraph 26) and the benefits of the planned improvement in ADB procedures will accrue to the sector as a whole, not merely to the sugar farmers.

14. Finally, the successful rehabilitation of the two estates and factories will, over the medium term, establish experience and expertise needed to expand the industry and reduce its costly dependence on foreign know-how. Such an expansion should result in a lowering of overhead costs and, more importantly, bring production to the point where it can meet the growth of consumption.

15. The proposed credit would be re-lent to GSC at 7½ percent with a 25-year repayment period including 5 years grace, and to ADB at 6½ percent repayable over six years. ADB would on-lend to farmers at 9 percent.

16. Equipment and materials valued at about US$7.6 million will be subject to international competitive bidding. Civil works worth US$4.7 million will also be subject to international tender, but it is expected that local firms will win most of the civil works contracts which include irrigation, factory improvements and housing. The expatriate management contract will be negotiated.

Financing

17. The total cost of the project is estimated at US$22 million. The foreign exchange component amounts to US$16 million or 73 percent of total cost. Almost one-third of the foreign exchange cost represents the capitalized cost of the management team which is crucial for running GSC. The financing plan for the project has not been finalized in the Appraisal Report pending a decision on possible parallel financing by the U. K. or the Netherlands. Recently, the Government has approached a Dutch firm (HVA) for providing the management team. HVA's response appears to be favorable and the company is even considering investing a minor amount of equity in GSC. It is not clear whether the Dutch Government would be prepared to provide long term financing out of its aid program to meet all or part of the management costs in foreign exchange. U. K. financing would only be available on a tied basis for the equipment component of the project.

18. In the light of these considerations and on account of Ghana's extremely difficult balance of payments situation, it is proposed that Bank Group financing be provided in the amount of about US$15 million (i.e. the estimated foreign exchange component shown in the project cost table less about US$1 million which is now considered to be properly allocated to operating costs) to cover the entire foreign exchange cost if bilateral financing would not become available. This would be a relatively high proportion of Bank Group financing but would be fully justified on balance of payments grounds.

For the same reason, it would be preferable to provide all the financing on concessional terms. However, given the limitation on IDA resources and contemplated IDA financing of two other projects in FY 1972, the Chairman of the Loan Committee has proposed joint Bank/IDA financing, on a 50/50 basis. Efforts to secure parallel financing will continue and it is understood that in this event the amount of Bank Group financing would be reduced accordingly. It is proposed that the Bank loan be on extended terms - 35 years including ten years of grace. Even such terms on an individual project basis would be somewhat harder than those compatible with our assessment of Ghana's creditworthiness position and with the posture we propose to take at Ghana's debt rescheduling meeting late this year or early in 1972. However, the blending envisaged in our 5-year lending program would result in average terms which are compatible with Ghana's position.

ISSUES

Financing sugar expansion and the issue of protection

19. The major purpose of the project would be to expand sugar production as a measure of import substitution. All of the sugar produced is intended for domestic consumption.

20. On a worldwide basis, the past sugar surplus is disappearing and consumption continues to rise. Production expanded during the 1960's but not as rapidly as did consumption. Prices have been increasing. At this stage, therefore, there is scope for some additional investment to expand sugar production without undue effects on the world market situation. Some share of such investments are justified in the developing countries where production in the 1960's expanded far less than in the developed countries and where consumption expanded at a greater rate than production.

21. Ghana's growth prospects and balance of payments outlook in the short term rely heavily on substantial reduction in imports because of the limits on possible export growth, as well as the fluctuations in the world cocoa market. Sugar is one of the commodities which can be produced viably with the possibility of substantial economies in foreign exchange.

22. Sugar production costs are difficult to compare between countries because of exchange rate distortions, and partly also for technical reasons. Within the context of these limitations, production costs for the project are comparable to those in Nigeria and Zambia, and below the projected c.i.f. price of imported refined sugar. At the official exchange rate, production costs would amount, at full production, to $150 per ton at Asutsuare and $167 per ton at Komenda, falling by $5 and $6 per ton respectively by 1980 - 1981 due to reduction in management costs. These costs compare with $145 per ton in Zambia and $155 in Nigeria currently.

23. Adding the cost of debt service and a small profit margin raises the ex-factory price for project sugar to around $186 equivalent per ton. This compares with, for example, $176 per ton ex-factory at the IFC

supported Metahara project in Ethiopia. Based on this ex-factory price, which corresponds to N₵190 per ton, project sugar would cost N₵193.5 per ton at Accra warehouse. Taking into consideration a 2.5 percent price advantage over imported sugar on commercial grounds as outlined in the appraisal report, the Accra warehouse price for imported sugar would have to be N₵198 per ton. At the projected price for imported sugar of US₵7.2 per pound, the warehouse price Accra would be N₵170 per ton and therefore require a duty of N₵98 per ton. This corresponds to 17 percent of the c.i.f. price. Present duties amount to N₵44 per ton. This level of duty, although providing a protective margin, is in fact no more than is required to restrain importation of sugar to levels consistent with foreign exchange scarcity and to provide a source of revenue for the Government.

24. Production of sugar in Ghana is thus justifiable in Ghana given current forecasts of import prices. The only cheaper source of sugar is bilateral supplies of Cuban sugar via USSR barter arrangements. These arrangements are not always advantageous to Ghana and in any case are not usually sufficient or dependable methods of importing sugar.

25. For reasons of simplicity the appraisal report recommends a protection system of fixed levies per ton. The Government may prefer to set up a Sugar Board to control importation and prices but it is felt that this arrangement is more costly and administratively problematic than is justified. A Sugar Committee is, however, recommended to advise on producer prices for cane, GSC pricing policy and the fixing of the levy.

Agricultural Development Bank

26. Events during the implementation of the fisheries credit and the appraisal of the cocoa rehabilitation project have revealed that ADB's loan control and accounting procedures are exceedingly weak. This issue was sidestepped in the cocoa project by insulating the credit distribution from the main body of ADB. However, since ADB is Ghana's major institution for channeling agricultural credit and since it has over the years gained useful experience and the confidence of farmers, its procedural problems deserve to be remedied so that it can fulfill its functions without running into the serious difficulties with debt recovery into which it is now heading. The appraisal report recommends linking this project with the provision of technical assistance to the ADB as a condition of the project and of on-lending the proceeds of the credit through ADB. Strengthening of ADB is also essential for expanded Bank Group lending to the agricultural sector.

27. The appraisal report stipulates two conditions to be met before invitation to negotiate: the formation of GSC with regulations satisfactory to IDA; and the appointment of a management firm for GSC. A mission is going to Ghana in early September 1971 to discuss the appraisal report and all relevant issues with the Government. Subject to reaching agreement on these issues, it is expected that negotiations could start in November.

Recommendation

28. I recommend that the Bank and the Association invite representatives of the Republic of Ghana to negotiate a maximum loan of US$7 million and a credit of US$8 million on the terms and conditions set forth in paragraphs 9.02 and 9.03 of the appraisal report, after the two conditions in paragraph 9.01 (and outlined above in paragraph 27) have been met by the Government. Should bilateral financing become available, the loan and credit would be reduced accordingly.

Roger Chaufournier
Director

Western Africa Department

GHANA - 5-YEAR OPERATIONS AND LENDING PROGRAM

(By Fiscal Year, in $ Millions)

OPERATIONS PROGRAM		1972	1973	1974	1975	1976
Livestock Development	IDA		2.0			
Cocoa II Ashanti Region	IDA			8.0		
Agriculture - Oil Palm	IDA		5.0			
Sugar Development	) IDA	8.0				
	) IBRD	8.0				
Annual Crops	IDA		6.0			
Annual Crops II	IDA			5.0		
Agriculture - Unidentified I	IDA				10.0	
Agriculture - Unidentified II	IDA					10.0
Agricultural Credit	IDA					5.0
Fisheries II	IDA				2.0	
Telecommunications I	IBRD		4.0			
Telecommunications II	IBRD					8.0
Power Distribution ECG III	IDA		8.0			
Power Generation	IBRD			10.0		
Industry (NIB)	IDA			4.0		
Industry Unidentified	IDA				5.0	
Education	IDA	7.0				
Education II	IDA			8.0		
Road Rehabilitation I	IDA	10.0				
Road Rehabilitation II	) IDA				8.0	
	) IBRD				8.0	
Road Construction	IDA					10.0
Port Improvement	IDA			4.0		
Sewerage	IDA				5.0	
Water Supply II	IDA		8.0			
Water Supply III	IDA					6.0
OPERATIONS PROGRAM	IBRD	8.0	4.0	10.0	8.0	8.0
	IDA	25.0	29.0	29.0	30.0	31.0
	TOTAL	33.0	33.0	39.0	38.0	39.0
	NO.	3	6	6	5	5
LENDING PROGRAM	IBRD	8.0				
	IDA	25.0	25.0	30.0	30.0	30.0
	TOTAL	33.0	25.0	30.0	30.0	30.0
	NO.	3	5	5	4	4

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

August 26, 1971

MEMORANDUM TO THE LOAN COMMITTEE

People's Republic of the Congo - Highway Maintenance Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated August 26, 1971 from the Western Africa Department, entitled "People's Republic of the Congo - Proposed Credit for a Highway Maintenance Project" (LC/O/71-95).

2. Comments, if any, should be sent to reach Mr. Storch (ext. 4743) by 5:00 p.m. on Tuesday, August 31.

3. It is planned then, if the Committee approves, to inform the Government that the Association is prepared to begin negotiations for the proposed credit on the terms and conditions referred to in the attached memorandum.

Dag F. Wittusen
Secretary
Loan Committee

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Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
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Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

CONFIDENTIAL

LC/O/71-95

August 26, 1971

LOAN COMMITTEE

Memorandum from the Western Africa Department

PEOPLE'S REPUBLIC OF THE CONGO -
Proposed Credit for a Highway Maintenance Project

Introduction

1. Attached is an appraisal report on a highway maintenance project in Congo (B). The total project cost is equivalent to about US$4.0 million, and the foreign exchange component of approximately $3.1 million would be financed by IDA. The proposed IDA credit would actually amount to $3.7 million, since it is to include $600,000 for refunding the outstanding balance of Credit S6-COB. This project would be the third Bank Group lending operation for highways in Congo (B). It is based on studies financed under the IDA highway engineering Credit (S6-COB) of FY 1969 which also provided detailed engineering for an IDA highway improvement Credit (189 COB) of FY 1970. There will be another project in the transport sector later this year, for engineering and improvement of the railway.

2. The dominant feature of the Congolese economy is its position as an inter-regional transport center. Bank strategy is focusing on transport because it constitutes the major bottleneck to economic development in general, and to the development of forestry and market agriculture in particular.

The Economy

3. Economic growth in recent years is estimated at about 4.5% per annum in real terms. In 1970 the gross domestic product (GDP) per capita was about US$255 equivalent. Timber extraction is the major industry accounting for almost 60% of total export earnings. Except in the region of the Niari Valley, along the CFCO railway, the development of agriculture has been limited, especially in the vast northern region which presents difficult problems in transport and communications. The service sector, particularly transport, has grown rapidly and accounts for about 30% of GDP. The manufacturing and mining sectors have grown in importance in recent years, and their share of GDP is estimated at about 15%. In terms of investment, the main industrial venture is the potash mine and refinery of the CPC (Compagnie des Potasses du Congo) near Pointe Noire. The CPC, which received a Bank loan (480 COB) of US$30 million in 1967, started production in mid-1969. Output has been less than expected and, in 1970, was still limited to about 25% of planned capacity as a consequence of major

mining difficulties; the possibility of developing a viable operation is now discarded and prospects of continued exploitation, even at the present reduced rate, are uncertain.

4. Congo's budgetary performance has traditionally been very good; but there have been signs of deterioration in recent years, essentially because of steady increases in current expenditures and losses of inefficient state enterprises. Public savings decreased from CFAF 1.5 billion in 1968 to CFAF 0.7 and 0.8 billion in 1969 and 1970, notwithstanding the Government's deliberate intention to increase them and despite successful efforts in raising revenues. This is cause for concern since the declining current surplus is accompanied by a considerable increase in unpaid bills, and by the use of all available Treasury resources including maximum drawings on the resources of the Central Bank. We have discussed these matters with the Government, which is now considering specific measures to reverse the present trend. Whatever success the Government has, external assistance should be essentially on concessional terms until the expansion of oil production, which gives good promise, can have a significant impact on the country's financial and balance of payments position.

The Project

5. The backbone of Congo's transportation network is its railway and waterway ststem, which not only carries the bulk of the freight and passenger traffic of Congo (B), but also serves large volumes of transit traffic for neighboring countries. The highway network constitutes a feeder to this system and plays a vital role in ensuring communication with sparsely populated regions of the interior. Although the highway network is rather extensive, most of the roads have low design standards and are in very poor condition. Traffic volumes are light and major upgrading cannot be justified at present. Improved maintenance is clearly the first measure to be taken to satisfy the urgent needs of road transport.

6. The project consists of a four year highway maintenance program (1972-1975) to be implemented with the assistance of consultants, providing for:

(1) reorganization and strengthening of the road maintenance organization;

(2) comprehensive training of personnel;

(3) overhaul of the existing equipment fleet and procurement of supplemental equipment;

(4) extension and renovation of workshops for the maintenance of equipment.

The main objective of the program is to improve the condition of the roads through more efficient use of resources devoted to maintenance.

7. The project's internal economic rate of return is estimated to be about 22%, assuming an annual traffic growth of 6%. The rate of return remains acceptable when tested with low estimates of future traffic growth and road user savings. The project's return remains satisfactory if the cost of supplemental technical assistance, which might be required after the four-year period of the project, is added to the project cost.

8. Total cost of the project is estimated at $3.95 million. The foreign exchange component, to be financed entirely by IDA, is $3.1 million representing 78% of project costs. The Government would cover the local expenditures estimated at $0.85 million, which includes $0.4 million for taxes. We propose that this credit also be used as the occasion for refunding the outstanding balance of $0.6 million under the Highway Engineering Credit (S6-COB) made in FY 1969. Studies financed under that earlier credit have been completed and served as a basis to prepare this project. The total amount of this credit would thus be $3.7 million.

9. Additional recurrent expenditures called for under the project, which are to be borne by the Government, will total about US$1.1 million over a five-year period (1972-1976). We will require the Government to confirm that the annual budgetary allocation for highway maintenance will be adequate.

10. Procurement will be in accordance with Bank/IDA guidelines. Proceeds of the IDA Credit should be completely disbursed by June 30, 1976.

11. The Government entity executing the project will be the Régie Nationale des Transports et des Travaux Publics (RNTP). The Ministry of Transport and Public Works has final authority over the RNTP which is entrusted with responsibility for administration, maintenance, and improvements of the classified highway network. We have asked FAC to confirm its intention to maintain its assistance to RNTP at present levels throughout the four-year period of the project and to coordinate its activities with the technical assistance to be provided under the project.

Issues for the attention of the Loan Committee

12. In 1969 the Government withdrew from the convention establishing the Agence Transéquatoriale des Communications (ATEC) a multi-national transport agency jointly established with the C. A. R., Gabon, and Chad. The Government took over ATEC's transport facilities located on its territory and set up a national agency, the Agence Transcongolaise des Communications (ATC), to run them. ATC is continuing transport services to the former ATEC partners under a series of bilateral agreements which have led to satisfactory cooperation.

13. In addition to the issue of ATEC-ATC, the Congolese Government has undertaken a number of nationalizations on which the status of settlement is as follows:

(a) Société Equatoriale d'Energie Electrique (SEEE) -- Agreement has been reached.

(b) Union Electrique d'Outre-Mer (UNELCO) -- The Government has recognized the principle of compensation, but settlement has not been reached on the evaluation of assets; the last time we received information on this issue was in April 1970.

(c) Compagnie Générale de Transports en Afrique Equatoriale (CGTAE) -- The Governments of Congo (B) and C. A. R., who both nationalized CGTAE, have reached a common position. The outstanding issue concerns the valuation of the assets of the Company. Discussions between Congo, C. A. R., and the Company were resumed in February 1971 and then broken off. In March 1971 the Company made a compromise proposal and in May informed us about the lack of response from the Congo Government.. We have received no subsequent information.

(d) Société Industrielle et Agricole du Niari - Société Sucrière du Niari (SIAN - SOSUNIARI) - The Government has endorsed the outstanding debts and has recognized the shareholders' right to compensation. Before the start of negotiations, the Government must receive from the Company the financial data and balance sheets up to September 25, 1970, the date of nationalization. Agreement has been reached with CCCE on the payment of all obligations and with COFACE on its short term debts.

14. From the above it is evident that there has been some progress in the settlement of nationalization disputes. However, we do not have any recent information on UNELCO, CGTAE, and SIAN-SOSUNIARI. When negotiations are authorized, we will write immediatly to the Government requesting the latest information on the nationalization issues outstanding and indicating that this subject will be discussed during negotiations.

Recommendations

15. I recommend that the Congolese Government be invited to send representatives to Washington to negotiate a credit of \$3.1 million for this project on the terms and conditions set forth in the attached Appraisal Report. I also recommend that the total amount of the proposed IDA credit be \$3.7 million in order to refund the outstanding balance of \$600,000 under the Highway Engineering Credit (S6-COB).

Roger Chaufournier
Director

POPULATION: .9M

GNP PER CAP: $ 230

IVA CONGO B - 5 YEAR OPERATIONS AND LENDING PROGRAMS
(BY FISCAL YEAR - AMOUNTS IN $ MILLIONS)

OPERATIONS PROGRAM			1972	1973	1974	1975	1976
7-COB-AL-01	LIVESTOCK	IDA		2.0			
7-COB-TH-03	ROADS-SIBITI-ZANAGA	IDA	3.1				
7-COB-TH-04	ROADS II	IDA				4.0	
7-COB-TR-01	RAILROAD ENGINEERING	IDA	5.6				
7-COB-TR-02	RAILROAD CONSTRUCTION	IDA			5.0		

	1964-68	1969-73	1972-76
IBRD	30.0		
IDA		16.3	19.7
TOTAL	30.0	16.3	19.7
NO	1	6	5

	1972	1973	1974	1975	1976
IBRD					
IDA	8.7	2.0	5.0	4.0	
TOTAL	8.7	2.0	5.0	4.0	
NO	2	1	1	1	

LENDING PROGRAM (3/ 9/71)

	1964-68	1969-73	1972-76
IBRD	30.0		
IDA		14.6	18.0
TOTAL	30.0	14.6	18.0
NO	1	6	5

	1972	1973	1974	1975	1976
IBRD					
IDA	7.0	2.0	5.0	4.0	
TOTAL	7.0	2.0	5.0	4.0	
NO	2	1	1	1	

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

B/106

LC/M/71-10

August 24, 1971

OK/DRS/8/25/71

Minutes of Loan Committee Meeting held on Friday, August 13, 1971 at 4:00 p.m. in the Board Room.

A. Present:

J. Burke Knapp (Chairman)	E. Gutierrez
S.R. Cope	J.P. Hayes
A. Broches	C.G. Melmoth
W.C. Baum	D. Richardson
I.P.M. Cargill	P. Sella
V.C. Chang	G.K. Wiese
R. Chaufournier	J.H. Williams
R.J. Goodman	J. Chaffey (Acting Secretary)

In Attendance:

D. Bahl	S.S. Kirmani
R.H. Cassen	A.D. Knox
G.F. Darnell	L.J. Lind
W. Diamond	J.C. Lithgow
L.J.C. Evans	S.N. McIvor
S.C. Hardy	W.P. Thalwitz
M.L. Hoffman	D.F. Wittusen
B.B. King	

B. International Competitive Bidding for Civil Works

1. The Committee considered a memorandum from Mr. Baum and Mr. Cope on International Competitive Bidding for Civil Works (LC/A/71-10 dated August 12, 1971). The Chairman reminded the Committee that the issue had originally been raised in relation to India, but in this paper was being considered as a matter of general policy. While it was ultimately intended

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Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
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Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

to submit a paper to the Executive Directors, the next step would be to send a fact-finding mission to India to review legal, administrative and other requirements relating to bidding for civil works and see to what extent they are consistent with the policies set out in the paper.

2. The Chairman identified for discussion three main issues arising from the paper:

(i) the proposal that due consideration should be given to the use of labor-intensive methods in project design, using shadow pricing for labor whenever desirable, and that in the award of contracts for civil works borrowers should be permitted to provide bonuses or subsidies for the use of labor in appropriate cases;

(ii) the conclusion that it would be impracticable to give preference to local contractors, although other measures should be employed to foster the local contracting industry; and

(iii) the criteria that should be used to determine the suitability of civil works contracts for international competitive bidding.

C. Labor-Intensive Methods

3. There was general agreement with the proposals in the paper on this subject. One speaker asked how the shadow rate for labor should be determined in specific instances. In reply it was suggested that many variables entered into the calculation, and while precise measurement was impossible it should be possible to make some rough judgments at the design stage, based on the relative resource availability, which should result in a better use of labor vis-a-vis capital. The Chairman pointed out that the responsibility for determining the level of labor bonuses or subsidies would rest largely with the Government; the Bank would only pass judgment on the reasonableness of a proposal. One alternative open to the Government which would have the same effect as wage subsidies was to tax capital inputs.

4. The Chairman said that it was assumed that the Bank would be prepared to assist in financing the additional financial cost of a project arising from the choice of labor-intensive design or the payment of wage subsidies. This would often mean an increase in the local expenditure financing element, which would have to be examined on its merits.

D. Encouraging Local Contracting Industry

5. There was general agreement with the steps outlined in paragraph 31 of the paper for encouraging a local contracting industry. It was noted that the Bank's procedures enabled it to disburse the same amount for the civil works on a project irrespective of whether the balance of foreign and local costs differed from that estimated at the time of appraisal.

6. It was also generally felt that there was not much need for a margin of preference for local contractors and that it would not be worth the difficulties involved. Some speakers commented in particular on the difficulties in distinguishing between locally-owned companies and domestic offices set up by foreign contractors.

7. With reference to procurement (paragraph 4 of the paper), attention was drawn to the additional words, "and competitive international trade" in Article V Section 1 (g) of IDA's Articles of Agreement which were not in the Bank's Articles. It was agreed that this lent more weight to IDA support for international competitive bidding and that paragraph 4 should be amended to reflect this.

E. Suitability for International Competitive Bidding

8. In response to the Chairman, it was stated that while in some cases international competitive bidding was judged to be unsuitable because of the technical nature of the works (e.g. small scattered works best done by the borrower with its own forces) in more instances the judgment was not as to suitability but as to whether or not foreign firms would be interested in bidding. In the latter cases, the Bank tended to give international bidding the benefit of the doubt: unless it was very evident that foreign firms would not be interested in tendering, the Bank insisted that they be given the opportunity to do so. The Bank's approach in this regard had not changed over time. There was no rule of thumb about the minimum size of contract likely to interest foreign firms because of the many factors that would affect a decision in a particular case (for example, a contractor having existing capacity in the region under another contract). It was pointed out that the adoption of labor-intensive design and construction methods would have the effect of favoring domestic over foreign contractors and consequently diminished the need for protection for local contractors.

F. Adjournment

9. The meeting adjourned at 5:30 p.m.

Secretary's Department
August 24, 1971

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LM/M/71-34/1

August 20, 1971

MEMORANDUM TO THE LOAN COMMITTEE

The attached revised minutes of a Special Loan Meeting to discuss "Iran - Pipeline Project" held on Wednesday, August 11 (LM/M/71-34/1) incorporate an amendment to paragraph 3(vii) of the original minutes dated and distributed to the Committee on August 19 (LM/M/71-34) and should be substituted for the latter.

J. Chaffey
Acting Secretary
Loan Committee

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Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
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Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

LM/M/71-34/1

August 20, 1971

Minutes of Special Loan Meeting to consider "Iran - Pipeline Project" held on August 11, 1971 in Conference Room B.

1. Present: Messrs. Knapp (Chairman), Cope, Broches, Baum, Cargill, Elliott, Eschenberg, Geolot, Lecuona, Loos, Melmoth, van der Meer and Chaffey (Acting Secretary).

2. Issues: The meeting considered:

(i) whether there could be effective international competitive bidding for the Rey-Tabriz pipeline if Ahwaz Pipe Mill Company, a wholly-owned subsidiary of the beneficiary of the loan, were permitted to participate in the bidding and, if so

(ii) whether a margin of preference should be extended to Ahwaz as a local supplier, and

(iii) whether it would be feasible to make the loan directly to the National Iranian Oil Company.

3. Discussion: The meeting noted that:

(i) One of the objectives of the project was to help steer NIOC towards better forward planning and management control.

(ii) Ahwaz had made unsuccessful bids in competition with other suppliers for previous NIOC pipeline contracts. There appeared to be no special advantage that Ahwaz could gain through its association with NIOC at the tendering stage; the adjudication was strictly neutral under the supervision of consultants; at the execution stage, if Ahwaz were awarded the contract, although a situation might conceivably occur in which there could be a conflict of interest with NIOC, this was thought to be unlikely and could be handled by proper project supervision.

(iii) Whether other companies would bid if they knew that Ahwaz was tendering was not known but was probable. However, they should be advised in the tender documents that Ahwaz was eligible to participate.

(iv) With regard to preference for domestic suppliers, the special circumstances of this project were first that the cost of the pipe for the proposed Rey-Tabriz line amounted to about 30 percent of the total foreign exchange costs of the project; secondly that there was normally low value added in the domestic production of pipe - about 27 percent in this case depending on the capital depreciation schedule employed.

(v) While it was recognized that 15 percent preference for domestic suppliers sometimes had an inequitable effect, the Bank had no policy guidelines on the use of a sliding scale of preferences.

(vi) NIOC and Ahwaz normally procured from abroad duty-free which suggested that there was no basis for the Bank to give protection to Ahwaz. NIOC had not requested the 15 percent preference, but the Government had done so.

(vii) On the question of who should be the recipient of the proposed loan, the Bank would strongly prefer to lend directly to NIOC in order to establish a closer relationship with them. Legislation will be required to enable the Government to guarantee NIOC's borrowing abroad.

4. Decision: The meeting concluded that:

(i) International competitive bidding procedures would not be prejudiced by the participation of Ahwaz provided that there was full disclosure of the situation to all interested parties.

(ii) Bearing in mind the decision in (i) above, if NIOC customarily purchased abroad without paying import duties there would be no case for granting a 15% preference to Ahwaz.

(iii) The Bank should make clear to the Iranian Government its preference for lending directly to NIOC.

J. Chaffey
Acting Secretary

Cleared by: Messrs. Cope
Broches
Baum
Eschenberg
van der Meer

cc: Loan Committee
Participants

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LM/M/71-34

August 19, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Attached for information are the Minutes of a Special Loan Meeting to consider "Iran - Pipeline Project" held on August 11, 1971 in Conference Room B.

J. Chaffey
Acting Secretary
Loan Committee

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Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
Controller

Copies for Information:

President
The Economic Adviser to the President
Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

LM/M/71-34

August 19, 1971

Minutes of Special Loan Meeting to consider "Iran - Pipeline Project" held on August 11, 1971 in Conference Room B.

1. Present: Messrs. Knapp (Chairman), Cope, Broches, Baum, Cargill, Elliott, Eschenberg, Geolot, Lecuona, Loos, Melmoth, van der Meer and Chaffey (Acting Secretary).

2. Issues: The meeting considered:

(i) whether there could be effective international competitive bidding for the Rey-Tabriz pipeline if Ahwaz Pipe Mill Company, a wholly-owned subsidiary of the beneficiary of the loan, were permitted to participate in the bidding and, if so

(ii) whether a margin of preference should be extended to Ahwaz as a local supplier, and

(iii) whether it would be feasible to make the loan directly to the National Iranian Oil Company.

3. Discussion: The meeting noted that:

(i) One of the objectives of the project was to help steer NIOC towards better forward planning and management control.

(ii) Ahwaz had made unsuccessful bids in competition with other suppliers for previous NIOC pipeline contracts. There appeared to be no special advantage that Ahwaz could gain through its association with NIOC at the tendering stage; the adjudication was strictly neutral under the supervision of consultants; at the execution stage, if Ahwaz were awarded the contract, although a situation might conceivably occur in which there could be a conflict of interest with NIOC, this was thought to be unlikely and could be handled by proper project supervision.

(iii) Whether other companies would bid if they knew that Ahwaz was tendering was not known but was probable. However, they should be advised in the tender documents that Ahwaz was eligible to participate.

(iv) With regard to preference for domestic suppliers, the special circumstances of this project were first that the cost of the pipe for the proposed Rey-Tabriz line amounted to about 30 percent of the total foreign exchange costs of the project; secondly that there was normally low value added in the domestic production of pipe - about 27 percent in this case depending on the capital depreciation schedule employed.

(v) While it was recognized that 15 percent preference for domestic suppliers sometimes had an inequitable effect, the Bank had no policy guidelines on the use of a sliding scale of preferences.

(vi) NIOC and Ahwaz normally procured from abroad duty-free which suggested that there was no basis for the Bank to give protection to Ahwaz. NIOC had not requested the 15 percent preference, but the Government had done so.

(vii) On the question of who should be the recipient of the proposed loan, the Bank would strongly prefer to lend directly to NIOC in order to establish a closer relationship with them. Legislation would be required to enable NIOC to borrow directly from abroad and to authorize the Planning Organization, in that circumstance, to provide the guarantee.

4. Decision: The meeting concluded that:

(i) International competitive bidding procedures would not be prejudiced by the participation of Ahwaz provided that there was full disclosure of the situation to all interested parties.

(ii) Bearing in mind the decision in (i) above, if NIOC customarily purchased abroad without paying import duties there would be no case for granting a 15% preference to Ahwaz.

(iii) The Bank should make clear to the Iranian Government its preference for lending directly to NIOC.

J. Chaffey
Acting Secretary

Cleared by: Messrs. Cope
Broches
Baum
Eschenberg
van der Meer

cc: Loan Committee
Participants

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LC/A/71-10

August 12, 1971

NOTICE OF MEETING

A meeting of the Loan Committee will be held on Friday, August 13, 1971 at 4:00 p.m. in the Board Room.

AGENDA

International Competitive Bidding for Civil Works

The Committee will consider the attached memorandum dated August 12, 1971 from Mr. Baum on International Competitive Bidding for Civil Works. The Committee met in March and June this year to discuss bidding procedures for Indian civil works and this meeting will be a continuation of the earlier discussions.

The Chairman has asked me to apologize on his behalf for the unavoidable short notice of this meeting.

J. Chaffey
Acting Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
Controller

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Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

INTERNATIONAL COMPETITIVE BIDDING FOR CIVIL WORKS

Introduction

1. During a recent discussion by the Executive Directors of an Indian irrigation project (Pochampad), I indicated that I would review the Bank's[1/] policies with respect to international competitive bidding for civil works and advise the Directors of any changes in this policy which I considered desirable. This paper presents the results of the review, and discusses various possible modifications of our policy.

2. The criteria which I believe should guide our policy in this field, and which have been used in this paper to analyze various alternatives, were set forth by several of the Directors during the Pochampad discussion. In brief, they are:

a) to help ensure the economical and efficient execution of Bank projects;

b) to provide equitable treatment of all the Bank member countries;

c) to provide the optimum use of the local resources of the borrowing country; and

d) to promote the sound development of a local contracting industry.

3. This paper first describes the Bank's present policy with respect to international competitive bidding, including the circumstances under which exceptions to international bidding are accepted. It then considers a number of possible modifications to the policy, designed to improve the use of local resources and to help develop the local contracting industry, and presents some conclusions.

Part I: Bank Policy on International Competitive Bidding[2/]

4. It is the general policy of the Bank to require that procurement financed by Bank loans and IDA credits be effected on the basis of international competitive bidding. This policy, which applies equally to equipment and to civil works, has been endorsed by the Executive Directors on various occasions. The Articles of Agreement of the Bank or IDA do not refer specifically to international competitive bidding.

1/ All references to the Bank apply equally to IDA.

2/ This section draws heavily on a paper "International Competitive Bidding and Preference for Domestic Suppliers" (SecM 71-111 circulated to the Executive Directors for information on March 1, 1971).

With respect to procurement, the Bank's Articles provide (Article III, Section 5):

"a) the Bank shall impose no conditions that the proceeds of a loan shall be spent in the territories of any particular member or members."

"b) the Bank shall make arrangements to ensure that the proceeds of a loan are used only for the purposes for which the loan was granted, with due attention to considerations of economy and efficiency and without regard to political or other non-economic influence or considerations." (Underlining added)

Article V, Section 1 of the IDA Articles virtually duplicates this language. The report of the Executive Directors on the Articles of Agreement of IDA is more explicit, however, and states in paragraph 18 that:

"Section 1(g) of Article V provides that the Association, in making arrangements with respect to the use of the proceeds of any financing, including currencies accepted as supplementary resources, shall give due regard to considerations of competitive international trade. It is expected that the Association, like the Bank, will require that the choice of equipment and services to be purchased with funds supplied by the Association shall normally be determined on the basis of international competition." (Underlining added)

5. The subject of international competitive bidding was last reviewed by the Executive Directors in a full discussion in 1965, in conjunction with a memorandum of the President on preference for domestic suppliers. The text of the decision approved by the Executive Directors (paragraph 9 of Minutes of Meeting of December 14, 1965) states *inter alia*:

"a) the principle of international competition reflects the interests of all members in that it encourages borrowers to carry out their projects economically while providing an opportunity for members generally to supply goods and transportation and other services for projects financed out of loans and credits..."

"c) the Bank and IDA would ordinarily require that borrowers make their purchases on a competitive basis, including broad international bidding, in all cases in which it was appropriate and take due account, in addition to price, of such considerations as delivery dates, quality and performance."

6. Pursuant to this general policy, the Bank's "Guidelines for Procurement under World Bank Loans and IDA Credits" of August 1969 (circulated to the Executive Directors with document SecM 70-340, dated July 24, 1970) provide:

> "The International Bank for Reconstruction and Development (the Bank) and the International Development Association (IDA) are required by their Articles of Agreement to ensure that the proceeds of their loans and credits are used with due attention to considerations of economy and efficiency. For this reason, and as cooperative international institutions, the Bank and IDA require their borrowers to obtain goods and services (other than consultants' services) through international competition open to all member countries of the Bank and to Switzerland unless another procedure, more appropriate to the circumstances, has been agreed between the Bank or IDA and the borrower..."

7. In practice the large majority of the procurement financed by Bank loans and IDA credits has been carried out through international competitive bidding. When such bidding has not been followed with respect to the whole or a part of the goods and services financed by a loan or credit, it has been because special considerations such as one or more of the following obtained:

a) the nature of the civil works was such, due to considerations such as seasonal weather, the dispersion of work sites, or the need to coordinate closely with on-going operations, that local contracting or the use of the borrower's own labor force was more appropriate and economical;

b) the size of the contracts for individual civil works was too small for international tenders. Whenever possible, however, individual civil works contracts are grouped into packages of sufficient size to interest foreign firms, and bidders are given the option of bidding for individual contracts or for the package as a whole;

c) procurement of equipment was done by individual subborrowers (e.g. farmers) in amounts too small to be appropriate for international tendering. Loans for agricultural and livestock credit are often in this category. Bulking of purchases to permit international tendering is done where practicable; in all other cases, local procurement by the farmers through normal commercial channels is followed, provided:

   i) an adequate choice among several makes of equipment, including foreign, is available to the farmer;

   ii) the individual farmer can exercise a free choice; and

   iii) maintenance and service arrangements are adequate.

d) standardization of equipment from a single source of supply, particularly of licensed, patented or proprietary items, was an overriding consideration in the interest of economizing on costs of inventory, maintenance, and staff training;

e) in rare cases, the emergency nature of the works precluded recourse to international tendering; or

f) professional services (e.g. consultants) were being provided. Consultants are usually selected according to the process outlined in the Bank's Guidelines on "Uses of Consultants by the World Bank and its Borrowers"1/, which does not entail competitive pricing.

8. In the case of loans to development finance companies, the Bank does not insist on formal bidding arrangements. First, private entrepreneurs are the principal beneficiaries of loans to DFCs. They may be relied on, in their own interest, to exercise economy and efficiency in the choice of equipment; and, in making their choice, they are generally guided by experience in the business and by competitive shopping. Second, most contracts involved in DFCs' operations are relatively small, and arrangements for bulk procurement are not practicable. Third, most DFC sub-loans are to finance the expansion of existing capacity in plants already committed to a particular type or brand of equipment; in the case of larger projects, special procurement arrangements often exist. For these reasons, the general application of formal competitive bidding procedures is not appropriate. On the other hand, care is taken to achieve the objectives of the Bank's policies in this regard. The Bank expects DFCs to follow appraisal procedures which include critical assessment of the quality and price of the goods they finance, to require evidence that their clients have shopped, and to evaluate the results of that shopping. The Bank's administration of loans to DFCs includes efforts to insure that DFCs are performing these tasks adequately.

9. The Bank's policy, by making possible widespread competition among foreign and domestic firms, has encouraged the economical and efficient execution of Bank-financed projects. It has been applied flexibly to make possible alternative procedures where international procurement was not suitable. International competitive bidding has provided an equal opportunity for all Bank member countries to participate in the business arising from Bank projects, and has been a significant factor in the ability of the Bank to obtain funds for its operations.

10. Most countries impose duties on imported manufactures with a view to encouraging local industry. The Bank, in deciding the basis on which bids for goods of local and foreign manufacturers are adjudicated, normally limits the protection given to local manufacturers to 15% or the actual rate of customs duty, whichever is lower. The Bank has hitherto not agreed to any preference being given either to local contractors engaged in civil works or to the use of local labor by contractors,

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1/ Copies of this document are available from the Information and Public Affairs Department.

whether local or foreign, nor, save in exceptional circumstances, has the Bank agreed to the exclusion of foreign firms from bidding for civil works of a kind likely to attract foreign competition. I do not believe that it is in the long term interest of members of the Bank, whether developed or developing, to abandon the principle of international competitive bidding. It would be possible, however, while maintaining the principle to modify its application, as has been done in bidding for equipment. The purpose of this memorandum is to consider whether any such modifications should be made, and, if so, what form they should take. Part II of this memorandum considers the case for introducing arrangements to favor the use of local labor. Part III considers the case for arrangements for encouraging the local civil works contracting industry.

Part II: Preference for Use of Labor On Civil Works

Choice of Technology

11. In most developing countries, there is a shortage of capital and, in many localities, there is a surplus of unskilled labor. There is, therefore, a case for taking this factor into account, particularly where unemployment is a serious economic and social problem, in the design, tendering and execution of projects.

12. The optimum choice of technology, as between the use of capital and labor, is a complex subject. At the risk of great oversimplification, civil works can be divided into machine-intensive or labor-intensive works as follows:

a) Machine-intensive works include a number of key operations which cannot be properly done by labor, e.g. compaction of highway pavement and of earthen dam embankments and canal banks. Land-leveling to the small tolerances needed for the irrigation of the more sensitive crop varieties, and silo construction by the most modern construction technique (slip-forming) require not only specialized machines but special skills as well. More generally, this category includes a range of operations where labor or machines can be used, but where (i) the financial advantage (at current prices) lies heavily with machines, or (ii) the much faster rate of machine work brings important benefits through the earlier completion of the project. When earth has to be moved over fairly long distances, or raised vertically over certain heights, as often in highway construction in rolling and mountainous terrain, machine-intensive methods may be the only ones possible. Aqueducts, bridges and similar canal and highway structures usually require machine-intensive methods, but ditches, culverts, regulators and turnouts can just as well be built in labor-intensive masonry. The technical selection of machine-intensive or labor-intensive methods for canal linings often depends on local availability of materials (brick-clay versus concrete aggregates or asphalt).

b) Labor-intensive works include earthworks (clearing, leveling, excavating) of small size or with short hauls and any type of work in which individual jobs are small and the sites so scattered that it is uneconomic to deploy machinery. Typical examples are field drains and distributory canals with their structures, feeder or secondary roads, field or bush clearing, and small storage buildings and markets. A careful analysis must be made in each project, however, to ascertain that labor will in fact be available in the numbers and skills desired and at the right time of the year.

13. Labor-intensive methods can rarely substitute for works requiring specialized machinery and skilled operators without serious loss of benefits. For example, land can be leveled by hand, but the process is too slow in a modern irrigation scheme with heavy investments in dams and canals. For some machine-intensive works, such as hauling earth over longer distances, labor is unlikely to prove a substitute over any realistic range of prices. For some work, such as earth compacting, there are purely technical reasons why hand labor cannot be used. On the other hand, for a considerable range of operations there is the possibility of technical substitution between labor and machines, or between machines of different types, with their associated labor requirements. Excavation of minor canals and drains and some other types of earthworks are cases in point. In these operations, the choice is likely to turn on relative prices.

14. More needs to be known about the substitutability of factor inputs. For this reason, two major studies are under way jointly in the Transportation Projects Department and Economics Department concerned with: (a) the optimum design of highways; and (b) the substitutability of labor for capital in highway construction.[1]

15. As noted above, most developing countries are characterized by a shortage of capital and, in many regions, a surplus of unskilled labor. When, as is also often the case, market prices for capital and labor do not reflect their economic costs, a further issue arises whether "shadow" pricing of factor inputs should be used in the design, tendering and execution of civil works. For example, foreign goods and services may be underpriced because a country's exchange rate is overvalued; domestic capital may be underpriced as a result of the government's interest rate policy, while domestic labor is overpriced where wages (sometimes because of a fixed minimum wage) are higher than labor's marginal productivity. "Shadow" prices are notional prices designed to reflect economic values, defined as what the resources in question could earn in alternative uses. The question is whether such shadow pricing could practically be applied to the design, tendering and execution of the projects. Such pricing need not inhibit the process of international competitive bidding, but could affect the choice of technology within it and the nationality of the firms which win the bids.

16. It is necessary to distinguish between shadow pricing in project design and shadow pricing in tendering for project execution.

1/ A staff paper done in 1965 on the "Substitution of Labor for Equipment in Road Construction" (SecM 65-118) concluded that the range of possible substitution of labor for equipment averages about 15% of the total costs of road construction. The study now under way would examine this question in a much more comprehensive fashion, including extensive field investigations. The range of substitution is likely to be considerably greater in irrigation projects in view of differences in terrain and the nature of works.

17. Where prices do not reflect real costs, shadow pricing could be a significant aid in the determination of the most appropriate project design. The shadow prices which would be relevant are those for foreign exchange, domestic capital and domestic labor. Determination of shadow prices is extremely difficult, and the results can at best be regarded as only rough appro. imations. Where, however, there is ground for believing that there is a substantial disparity between market prices and economic costs, an attempt could properly be made to allow for these disparities in selecting the optimum project design.

18. The use of shadow prices in bidding, however, is in a different category. While the general design can be established so as to reflect shadow prices, there are serious practical difficulties in attempting to ensure that in the execution of the design, labor and capital are used in particular proportions. The contractor pays market prices for labor materials and equipment, not shadow prices, and, once the contract price has been fixed, cannot be expected to execute the work in other than the most economical way in terms of money. The contract could indeed specify in general terms the way the construction work is to be carried out,.but it is impracticable to police it effectively in detail and the contractor must be given sufficient flexibility to adapt his work program, including the proportions of equipment and labor, as the work progresses.

19. These difficulties would largely disappear if, instead of being told how he should carry out the work, the contractor would be given a financial incentive to do it in a way which reflected shadow prices rather than market prices. For example, in a situation in which there was surplus labor, the government could provide, or require agencies executing projects to provide, a subsidy or bonus to contractors for the use of labor on the basis of a formula which could be policed through the certification of payrolls. If such a system were considered worthwhile, and it has been done to a limited extent in some countries in the past, governments could apply it generally to all civil works, at least in areas of labor surplus, and not solely to Bank projects. Responsibility for fixing the appropriate size of the subsidy or bonus would rest with the government, but provided the amount were judged reasonable, the Bank should be prepared to accept it.

20. Two conclusions emerge. First, it is important that projects in developing countries are not carried out to capital-intensive designs and construction techniques if these are not appropriate to the country's needs and resources. Care should therefore be taken during the preparation and appraisal of projects to ensure that the choice of technology gives full consideration to local resources and to the possibility of substituting labor for capital. This can best be accomplished by making certain that the staff of the Bank, consultants, and borrowers are thoroughly aware of the importance of this objective, and by collecting and disseminating the findings of relevant studies as they become available.

21. Secondly, the possibility should be explored of providing a financial incentive to contractors, foreign and local alike, to use

labor more intensively where it is overpriced. This is primarily a matter for governments of developing countries to establish the necessary financial and administrative system, but the Bank should be prepared to give its help in formulating practical arrangements and to accept such arrangements in the projects it finances.

22. It should be noted that a subsidy for labor is not incompatible with international competitive bidding. Firms of all nationalities could be given equal opportunity to bid on the basis of whatever prices are specified in the contract.

Part III: Encouraging a Domestic Civil Works Industry

23. The Bank accepts a preference for domestic manufacturers in bid comparisons under international tenders, defined as the existing level of duty or 15%, whichever is lower. Should it not agree to an equivalent preference for services rendered by domestic contractors? This question has been raised on various occasions and answered in the negative, for reasons which I believe are still valid. On the other hand, there are other ways in which the Bank can assist member governments towards the important objective of developing a local civil works contracting industry.

24. With respect to the need for a preferential margin, the "infant industry" argument in favor of protection applies much more strongly in the case of manufacturing than it does civil works. A local contracting firm already enjoys a considerable natural advantage over foreign competitors, by virtue of its familiarity with government regulations and procedures, customs duties and formalities, wage scales, trade union practices, language, etc., all of which are crucial to timely execution and effective cost control of a project. Mobilization time is shorter and overheads are lower. The difference between the local manufacturing and contracting industries can be illustrated by the fact that in borrowing countries with both types of industries, local civil works contractors win a higher proportion of orders under Bank projects without a margin of preference than do local equipment suppliers with the 15% margin.

25. A second point relates to the appropriate level of any preference. In the case of equipment there is likely to be a substantial difference between local and foreign firms in the amount of value added locally. Foreign-supplied equipment is likely to have practically no value added locally; the local value added to domestically manufactured equipment may be anywhere from very little to close to 100 per cent. On the other hand, on civil works both local and foreign contractors have equal access to local labor and materials and in most instances they also have equal access to foreign or local construction equipment. The difference in value added locally between local and foreign firms is attributable primarily to expatriate salaries, profits and managerial overhead; the difference is therefore small, generally in the neighborhood of 10 to 15 per cent. Even if it were considered desirable to give domestic contractors an effective preference of as much as 25 to 30 per cent on the services provided by them, this would mean giving a margin of preference of only 3 to 4 per cent on the total value of the construction contract.

26. Lastly, there is the problem of the definition of a "local contractor" and a "foreign contractor". In many countries local affiliates of foreign contractors have been established, if for no other reason than the legal requirement that contractors be registered before they are eligible for work in the country. For manufactured goods the

physical location of a plant, and its ownership can readily be established. Contrary to this, a "local" civil works contractor may consist of a one-room office. The domestic physical assets may be small, since equipment is frequently purchased and a labor force recruited only after a contract has been won. Determining whether or not a civil works contractor is really local (and entitled to a preference) may therefore be difficult, and could easily lead to abuse.

27. Aside from possible preferences a much more basic question is what can be done to help develop a competitive, efficient local industry where it does not now exist.

28. Two factors appear to be of particular importance. One is the size and continuity of the civil works program (highways, irrigation, housing, schools, etc.) of the country. A local contracting industry is much more likely to grow in countries which have a fairly large and sustained program of civil works, a condition which is, of course, more likely to be filled in large than in small countries and one which depends also on the stage of development and rate of growth of the economy. Local civil works contracting tends to start with simple works, such as houses and schools, and to develop progressively to the point where it can handle large ones, such as roads and irrigation canals.

29. A second factor is the government's attitude towards the local contracting industry. In some countries, for historical reasons, civil works are executed by governmental departments on force account. Local firms, to the extent they are used at all, carry out small operations essentially as suppliers of labor under the direction of governmental engineers. As a corollary, local firms are not granted the tax status, credit, or access to foreign exchange which are available to the other industries considered of national priority; in some cases the status of local contractors is even less favorable than that of foreign firms doing business in the country. This traditional approach, which has been gradually changing has been a serious impediment in some countries to the growth of an independent and efficient contracting industry.

30. These considerations suggest that, without sacrificing the advantages of international competitive bidding, the Bank can perform a useful role in helping govenments to develop a local contracting industry. Specific measures to this end, some of which are already being followed, are discussed below.

31. The Bank should work with its borrowers to create an administrative and financial environment conducive to the growth of the local contracting industry. Some of the elements of such a climate are:

a) public statements of government intent to develop the local industry by putting large civil works to tender on contracts of substantial size and for a period of years;

b) improvements in the tax status of the contracting industry and its access to public credit;

c) improvements in contract provisions and procedures to cover, inter alia, arrangements for arbitration, delineation of contractor's responsibilities vis-a-vis the government, bonus and penalty provisions, access of contractors to locally made or foreign equipment of their choice and provision of reasonable advances for purchase of equipment and other mobilization costs;

d) encouragement of joint ventures between foreign and local firms. Such joint ventures could be invited in the bid documents and many foreign firms might respond favorably. Joint ventures should not be made compulsory, however; this would reduce the contractor's freedom to carry out the project in what he considers the most expeditious manner and would limit competition to those foreign firms able to find qualified domestic partners;

e) breaking down contracts into individual units within the capability of small firms while larger firms bid for packages of such units, the award being made to the lowest bid or combination of bids.

32. Shortage of equipment has been an impediment to the development of local contracting industries in a number of countries. In a few projects the Bank has provided equipment to the government, which was rented to local contractors. The Bank should be prepared to finance the procurement of equipment for the local contracting industry on a regular basis, just as it finances equipment for the government's highway maintenance services or for other local industries. The equipment could be provided to a governmental department and made available to local firms on a hire-purchase basis; alternatively, a local development bank could be the intermediary through which the finance was provided. In time, equipment rental firms might be established, thereby reducing the risk of excessive investment in equipment.

33. It is expected that other measures will be formulated as a result of the research which the Bank has initiated on how to promote the road construction industry in developing countries.

34. The discussion above leads to two conclusions. The first is that a preference for local contractors bidding under Bank loans is not practicable. The second is that governments can well take measures

to foster an indigenous contracting industry by improving the tax status of the industry, its access to public credit and foreign exchange, and contracting terms and procedures. The Bank can assist in this process; furthermore, the Bank should be prepared to finance the equipment needs of the contracting industry and to provide technical assistance as needed for its development.

WCBaum/SRCope:pen

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LM/M/71 - 33

August 10, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Attached for information are the Minutes of a Special Loan Meeting to consider "Uruguay - Loan to UTE for a Fourth Power Project" held at 3:30 p.m. on Wednesday, July 28, 1971 in Conference Room B.

J. Chaffey
Acting Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
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Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

LM/M/71 - 33

August 10, 1971

Minutes of Special Loan Meeting to consider "Uruguay - Loan to UTE for a Fourth Power Project" (Loan 712-UR) held on Wednesday, July 28, 1971 in Conference Room B.

1. Present: Messrs. Cope (Chairman), Alter, Baum, Wiese, Howell, Kanchuger, Lithgow, Ribi, Sheehan, Wessels and Chaffey (Acting Secretary).

2. Issue: The meeting was called to consider:

(a) whether approval should be given for the purchase of a 125 MW steam generating unit at the Batlle plant in Montevideo, rather than the 100 MW unit authorized in the loan agreement and, if so

(b) on what basis procurement should be made.

3. Discussion: The meeting noted that:

(a) There had been a delay of about 12 months in the procurement of the 100 MW generating unit approved in the loan agreement. The company now took the view that, as demand was growing faster than was originally projected, they would prefer to install a 125 MW unit and get extra capacity at a low incremental cost, rather than run the risk of being unable to meet the system requirements if bad hydrologic conditions prevailed in 1974-75.

(b) On the other hand, the power demand estimates were acknowledged to be sketchy, and the hydrologic data questionable. A 125 MW unit would be no more reliable than the 100 MW, and it was generally considered too large for the system requirements.

(c) Bids for the 100 MW unit had been submitted in accordance with the guidelines on procurement laid down by the Bank and bidders had been given the option of tendering on a component or turnkey basis. However, tucked away in a small paragraph at the end of volume 10 of the tender documents had been a call for bids for a 125 MW unit on a turnkey basis only, which Bank staff had not noticed when the issue of the tender documents was approved.

(d) It was contended by the Projects Department that the call for bids for a 125 MW unit was contrary to the loan agreement and to the guidelines for procurement inasmuch as bidders were not given the option to submit tenders either on a component or turnkey basis. Thus, although the Bank had formally approved the issue of the tender documents, it could not reasonably be held accountable for every condition contained in them, particularly any which were contrary to the loan agreement.

(e) In a letter dated May 20, 1971 from the Public Utilities Department to UTE in which the Bank indicated its awareness that UTE "was ready to propose awarding a contract for the sixth unit at (your) BATLLE plant of 125 MW," no concern was expressed that the bids had not been solicited in accordance with the loan agreement or the guidelines on procurement.

4. Decision: The meeting concluded that, although UTE might not have provided adequate justification for increasing the capacity, it made little practical difference whether a 100 MW and a 125 MW unit was installed. The results of the bidding for the 100 MW unit indicated that the turnkey alternative was cheaper than the components. The turnkey price for the 125 MW was lower per unit of installed capacity. A further delay to permit retendering would be unfortunate and was unlikely to produce a lower bid. However, the decision was left in abeyance, pending further discussion with the Legal Department.

5. Postscript: After consultation with Mr. Aldewereld and the Legal Department, it was agreed that there was no legal issue at stake and a decision could be reasonably taken either way. It was therefore decided that, under the particular circumstances of this case, the Bank should be prepared to finance the 125 MW unit on the basis of the turnkey bids.

J. Chaffey
Acting Secretary

Cleared by: Messrs. Cope
Baum
Howell
Wiese

cc: Loan Committee
Participants

FORM No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

August 5, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Iran - Pipeline Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated August 5, 1971 from the South Asia Department, entitled "Iran - Proposed Loan for a Pipeline Project" (LC/O/71-94).

2. Comments, if any, should be sent to reach Mr. Loos (ext. 4127) by 1:00 p.m. on Wednesday, August 11.

3. It is planned then, if the Committee approves, to inform the Government and representatives of NIOC that the Bank is prepared to begin negotiations for the proposed loan on the terms and conditions referred to in the attached memorandum.

J. Chaffey
Acting Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
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The Economic Adviser to the President
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Mr. M. Shoaib, Vice President
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Executive Vice President (IFC)
Vice President (IFC)

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LC/O/71-94

August 5, 1971

LOAN COMMITTEE

Memorandum from South Asia Department

IRAN - Proposed Loan for a Pipelines Project

1. Attached for consideration by the Loan Committee is an appraisal report (PTR-91) entitled "Appraisal of the National Iranian Oil Company Pipeline Project, Iran", dated July 15, 1971. It recommends a loan of $34.6 million repayable over 20 years (including a grace period of 3 years). The proposed loan will be used mainly to finance the foreign exchange cost of a project for increasing the capacity of two existing pipelines and the construction of a new one. The loan will be made to the Government of Iran and be passed on to the National Iranian Oil Company (NIOC) on substantially the same terms.

2. The Country Program Paper on Iran dated February 18, 1971, provided for three pipeline projects for which $145 million has been included in the lending program for the period 1971-76. The project under consideration, which was identified in part by the Transport Sector Survey mission last year, is the first of these. We understand that NIOC intends proceeding with the second project using medium-term credit. Further Bank financing, including a loan for the third project in the lending program, will have to be considered in the light of the experience gained from this first project.

Background

3. Since 1957 when the first loan was made to Iran, the Bank has made nineteen loans aggregating $612 million (net of cancellations). By the end of FY71, $328 million had been disbursed and $146 million repaid. The lending program for the next five years calls for loans of about $125-150 million annually. Specific proposals are summarized in Annex I.

4. The last economic report "Current Economic Position and Prospects of Iran" (SA-23a) dated May 18, 1971, deals with recent developments in the Iranian economy.

5. There has been an acceleration of economic growth in Iran in recent years, caused primarily by substantial increases in investment in both the public and the private sectors and the rapid rise of oil revenues. Although there was some slackening in the rate of growth of industry and agriculture last year (1970/71), it is estimated that the overall rate of growth has been maintained at the previous years' high level.

6. In the last three years, however, there has been increasing evidence of major strains on the economy. The relative stagnation of domestic savings in a context of high and rising levels of public sector expenditures led to a growing dependence on resource inflows. While receipts from oil increased rapidly, they had to be supplemented to a sharply increasing extent by foreign borrowing, much of it on short-term. The results were reflected in a steadily rising balance of payments deficit and a mounting debt service burden. The recent agreements with the oil companies will have improved Iran's resource position and at the present time, we consider Iran creditworthy for Bank lending in the amounts agreed in the Country Program Paper. Nevertheless, the mobilization of greater resources for investment and an improvement in the average terms of foreign borrowing will continue to be necessary if the growth levels of recent years are to be sustained, let alone enhanced.

7. The oil industry in Iran consists of a foreign operated export-oriented sector and the Government-owned NIOC. Two groups constitute the former: the "Consortium" composed of a number of major international oil companies and the relatively smaller "independents" who are other foreign oil companies operating in joint ventures with NIOC. Although it has only a small share of the total production of the oil industry in Iran, NIOC plays a most important role, because it is responsible for the distribution and sale of petroleum products throughout Iran and is also responsible for the development of oil resources in all parts of the country outside the limited area in which the Consortium operates. It has a number of subsidiary companies engaged in related activities, including the National Iranian Gas Company, the National Iranian Petroleum Company and the Ahwaz Pipe Mill Company.

8. The upsurge of economic activity in Iran in recent years has been reflected in the substantial increase in the demand for energy, which grew at an average rate of almost 11 percent since the middle of the last decade. Oil products form an important part of the total energy supply. The volume of crude oil refined for Iran's domestic market increased from 3.5 million tons in 1964 to almost 8.5 million tons in 1969, representing an annual increase of over 19 percent.

9. This substantial increase in domestic consumption of petroleum products in Iran has cast a heavy burden on the country's transportation and distribution facilities. The oil fields are located at the head of the Persian Gulf in the south, while the main consumption centers are in the populated northern regions. The transportation of oil and oil products, therefore, absorbs considerable resources in Iran, accounting for some 30 percent of the internal traffic ton-km. Several modes of transport are used, but pipelines have become the predominant means. The recent Government decision to waive the requirement whereby NIOC had to deliver a minimum quantity of oil daily for transport by rail will further increase the volume transported by pipeline. This makes good economic sense, since over long hauls and in large volumes transport of oil and oil products by pipeline is considerably cheaper than road or rail transport.

The Project

10. The proposed Bank loan will be used to finance a project which will increase the pipeline capacity in Iran. It includes three elements:

(i) increasing the capacity of the crude oil pipeline from Ahwaz to Tehran (Rey) by replacing diesel stations with electric pumping stations and installing a gas turbine pumping station;

(ii) increasing the capacity of the products line from Tehran to Mashad by installing additional pumping horsepower of approximately 8,400;

(iii) constructing a products trunkline from Tehran to Tabriz with the necessary ancillary equipment.

In addition, it provides for the employment of management consultants to introduce a system of forward planning and for the training of key NIOC personnel.

11. The project is the least cost solution to the problem of transporting oil and oil products from the supply points to the consumption centers. Compared with the next best alternatives the rate of return is expected to be in excess of 35 percent.

12. The total project cost is estimated to be $46.6 million including $33.3 million foreign exchange on the assumption that pipe orders go to foreign suppliers. The project includes the cost of pipe required for the new products trunkline from Tehran to Tabriz which would go to international tender. The appraisal report recommends that 15 percent preference

for the local supplier, the Ahwaz pipe mill, be extended. It is estimated that the value added of the pipe mill amounts to 27 percent. However, in the course of the discussions with the Projects Departments uncertainty developed regarding the eligibility of some of the items included in the estimate of value added. Additional information is required to refine the estimate of local value added. It was agreed that the decision on whether or not the Ahwaz pipe mill should be granted a 15 percent preference should be reviewed after additional information is provided by the Borrower during negotiations. All other procurement would also be by international competitive bidding except for minor contracts which are unlikely to attract international tenders.

13. The project tested against all the usual criteria applied in the Bank, and especially in terms of financial and economic returns, is one of the best in our lending program. It is a project to which the Government attaches considerable importance and one which would be a further step in the development of our relationship with the Government of Iran. In accordance with the recommendations of the Country Program Paper, our efforts are aimed at assisting the authorities in increasing the efficiency of the investment program in terms of cost, efficiency, project preparation and implementation. They are also directed at helping Iran to improve the terms on which it borrows.

14. The proposed loan is in conformity with these aims. NIOC is the most important institution in the crucial oil sector. Its investment program is sizeable, amounting to some $740 million for the period 1971 to 1974. Very nearly half of this will be financed out of NIOC's internal cash generation, the balance being financed by the proposed Bank loan and other borrowings. The Government feels that NIOC's present procedures are inefficient, lead to cost overruns and do not result in effective competition among bidders. Examples of poor project performance abound, and the magnitude of NIOC's investment program greatly increases any adverse effects of poor project handling. One of the outstanding examples of this is the gas trunkline (for which a subsidiary of NIOC is responsible), the cost of which has gone up from $400 million to $700 million. It is clear that the original technical evaluation was inadequate and that project supervision has also been unsatisfactory. The latest example of the cost consequences of NIOC's procedure is in the awarding of contracts for the Ahwaz-Tehran crude oil line. The project was expected to cost about $85 million; but NIOC now proposes to enter into a turn-key contract for a much higher amount. There is also need for institution building, not in terms of engineering but clearly in terms of project planning and financial control. Our emphasis will be on the creation of a Planning Section to deal with forward planning of NIOC's investments in oil, gas and petro-chemicals. Although the proposed loan will constitute

only a small part of NIOC's total investment, it is felt that it would demonstrate the beneficial effects of proper planning and project preparation, of efficient project implementation and of the Bank's procurement procedures.

15. Furthermore, although alternative sources of financing might be available, it is important to note that these would be in the form of medium-term supplier credits, and that project cost could be increased thereby quite considerably. Both the Country Program Paper and the last Economic Report strongly recommend that the Government take steps to improve the average term of borrowing. The provision of Bank financing for this project is consistent with this recommendation.

Recommendation

16. I recommend that the Bank should make a loan of $33.3 million for the pipeline project and that appropriate representatives of the Borrower and NIOC be invited to Washington for negotiations. Referring to paragraph 12 above, if it is decided to extend the 15 percent preference to the Ahwaz pipe mill, I would concur with the recommendation of the appraisal report to include a provision in the loan for meeting the additional cost which could be as high as $1.3 million. In these circumstances, a loan of $34.6 million should be made.

Attachment

Gregory B. Votaw
Deputy Director

Annex I: "Iran - 5 Year Operations and Lending Programs"

POPULATION: 26.3M

GNP PER CAP: $ 280

IVA IRAN - 5 YEAR OPERATIONS AND LENDING PROGRAMS
(BY FISCAL YEAR - AMOUNTS IN $ MILLIONS)

OPERATIONS PROGRAM			1972	1973	1974	1975	1976
5-IRN-AC-02	AGRIC. CREDIT-ADFI II	IBRD	15.0				
5-IRN-AC-03	AGRIC.DEV.FUND III	IBRD			25.0		
5-IRN-AC-04	AGRIC.DEV.FUND IV	IBRD					30.0
5-IRN-AF-01	AGRICULTURE-FISHIRIES	IBRD		30.0			
5-IRN-AI-03	IRRIG.PACKAGE SCKEME I	IBRD		20.0			
5-IRN-AI-04	IRRIGATION DEZ	IBRD	20.0				
5-IRN-AI-05	IRRIG.PACKAGE SCKEME II	IBRD				30.0	
5-IRN-AL-01	LIVESTOCK DEVT.1	IBRD			10.0		
5-IRN-AL-02	LIVESTOCK DEVT.II	IBRD					10.0
5-IRN-CC-02	TELECOMMUNICATION II	IBRD		25.0			
5-IRN-CC-03	TELECOMMUNICATION 111	IBRD					35.0
5-IRN-DD-07	IMDBI VII (DFC)	IBRD	50.0				
5-IRN-DD-08	IMDBI VIII	IBRD			50.0		
5-IRN-DD-09	IMDBI IX	IBRD					50.0
5-IRN-EE-02	ARYA-MEHR UNIVERSITY	IBRD		20.0			
5-IRN-EE-03	EDUCATION III	IBRD			20.0		
5-IRN-EE-04	EDUCATION IV	IBRD					20.0
5-IRN-PP-01	POWER	IBRD	30.0				
5-IRN-PP-03	POWER	IBRD			50.0		
5-IRN-PP-05	POWER IV	IBRD					50.0
5-IRN-TA-01	AIRPORT	IBRD		35.0			
5-IRN-TA-02	AIRPORT	IBRD				30.0	
5-IRN-TH-06	HIGHWAYS VI	IBRD		40.0			
5-IRN-TH-07	HIGHWAYS	IBRD				40.0	
5-IRN-TL-01	PIPELINES	IBRD	33.4				
5-IRN-TL-02	PIPELINE	IBRD		60.0			
5-IRN-TL-03	PIPELINE	IBRD				50.0	
5-IRN-TP-02	PORT	IBRD					10.0

POPULATION: 26.3M

GNP PER CAP: $ 280

IVA IRAN - 5 YEAR OPERATIONS AND LENDING PROGRAMS
(BY FISCAL YEAR - AMOUNTS IN $ MILLIONS)

OPERATIONS PROGRAM

	1964/68	1969/73	1972/76		1972	1973	1974	1975	1976
IBRD	141.0	661.9	888.4	IBRD	148.4	230.0	155.0	150.0	205.0
IDA				IDA					
TOTAL	141.0	661.9	888.4	TOTAL	148.4	230.0	155.0	150.0	205.0
NO	7	20	28	NO	5	7	5	4	7

LENDING PROGRAM (2/10/71)

IBRD	141.0	603.5	745.0	IBRD	145.0	175.0	140.0	140.0	145.0
IDA				IDA					
TOTAL	141.0	603.5	745.0	TOTAL	145.0	175.0	140.0	140.0	145.0
NO	7	17	22	NO	4	5	4	4	5

P & B 07/13/71

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

August 3, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Tanzania - Smallholder Tea Development Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated August 3, 1971 from the Eastern Africa Department, entitled "Tanzania - Proposed Smallholder Tea Development Project" (LC/O/71-93).

2. Comments, if any, should be sent to reach Mr. Clements (ext. 4914) by 5:00 p.m. on Friday, August 6.

3. It is planned then, if the Committee approves, to inform the Government that the Association is prepared to begin negotiations for the proposed credit on the terms and conditions referred to in the attached memorandum.

J. Chaffey
Acting Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
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Executive Vice President (IFC)
Vice President (IFC)

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LC/O/71-93

August 3, 1971

LOAN COMMITTEE

Memorandum from the Eastern Africa Department

TANZANIA: Proposed Smallholder Tea Development Project

I. INTRODUCTION

1. The Association has already provided about $1.6 million for tea development in Tanzania under the $5.0 million Agricultural Credit Project (Credit No. 80 TA) of January 1966. The Government has now requested IDA to help finance a major extension of the smallholder tea development program initiated during the Second Development Plan period (1969-74).

2. Tea output in Tanzania rose from 3.7 million to 8.5 million kilograms between 1960 and 1970, mainly due to large-scale plantings by private estates during the 1950's and the introduction of the use of fertilizer and better planting materials. The industry now accounts for about 2½ percent of Tanzania's total export earnings.

3. Large estates, which presently produce over 90 percent of all tea grown in Tanzania, are not expected to expand much further. Under the Second Development Plan, however, the Government has embarked on a major program to encourage tea-growing by smallholders which has already met with striking success. At the end of FY69 about 4,600 smallholders were growing tea in Tanzania. Their numbers have since doubled and the rate of recruitment of new growers continues to be high.

II. THE PROJECT

4. The proposed project, which would have significant employment benefits as well as substantially increase Tanzania's tea output and exports, would comprise:

(a) the planting by 14,000 smallholders of about 8,300 hectares of tea in the four areas of Bukoba (about 1,600 ha), Rungwe (about 3,700 ha), Lupembe (about 2,300 ha) and West Usambara (about 700 ha);

(b) the construction of tea roads in these four areas and provision for their maintenance;

(c) the construction and equipping of factories for processing leaf produced by smallholders;

(d) the provision of transportation for extension services and green leaf collection;

(e) the establishment of nurseries to provide planting material; and

(f) the strengthening of the Tanzania Tea Authority (TTA) by the provision of additional staff and accommodation.

III. HIGHLIGHTS AND ISSUES

The Financing Plan

5. The total cost of the project is estimated at $16.1 million, of which the foreign exchange component is $6.0 million. The high proportion of local currency expenditure, which is normal for tea projects in East Africa, is chiefly accounted for by the large provision for necessary extension staff and locally-procured planting materials.

6. The Appraisal Report proposes that IDA provide $10.7 million or about two-thirds of the total project cost; this proposal is discussed in paragraphs 7-10 below. About $1.9 million or 12 percent is expected to be provided by Norway, which has been requested by the Tanzanian Government to help finance the construction of tea roads in the Rungwe and West Usambara districts as part of a broader feeder road program in these two areas; finance for this feeder road program was approved by the Board of the Norwegian Agency for International Development (NORAD) in June and the proposal is now to be submitted to the Norwegian Cabinet and Parliament for confirmation. On this basis, external sources would contribute some 78 percent of total project costs and the Tanzanian Government the remaining 22 percent ($3.5 million). Some $6.2 million of the IDA credit would be used to finance local expenditures.

7. In formulating the financing plan outlined in the Appraisal Report, account was taken of the guidelines for loans and credits to Tanzania in the Country Program Paper. The CPP states (in paragraph 61) that because of Tanzania's poverty it is desirable that in our loans and credits for Tanzanian projects we should aim at providing not less than 65 percent of the cost of the projects concerned; where the foreign exchange cost of the project is less than this proportion, we would plan to cover part of the local costs. The amount of the proposed credit accords with this policy; it also falls within the $12.0 million allocated for the project in the Lending Program for FY72.

8. However, the position is complicated in this particular instance by Norway's proposed participation. The NORAD-assisted roads, though an integral part of the project, would be treated for financing purposes as a separate component which would be financed by Norway and the Tanzania Government. If the IDA financing is related to the portion of the project which the Association would be helping to finance, the proposed credit of $10.7 million represents about 77 percent of the $13.9 million expenditure involved.

9. In reviewing the amount of the proposed IDA credit, I have borne in mind that, of the four projects in Tanzania approved during the past year, the Bank/IDA finance has averaged only 55 percent of total project costs and our contribution to local currency expenditure only 8 percent. I have also taken into account the fact that total external assistance from all sources to Tanzania during the past year has been considerably less than assumed when the CPP was prepared, covering only 30 percent of Tanzania's total development expenditure compared with the 45 percent expected. These factors justify a high proportion of external finance for the proposed project.

10. Nonetheless, even allowing for these considerations, I believe that the proposed IDA credit is somewhat on the high side in view of the fact that Norway is expected to finance part of the project. I therefore recommend, and the Agricultural Projects Department concurs, that the IDA credit should be $10.5 million. This would represent 65 percent of the total cost of the project and 75 percent of the IDA portion, with $6.0 million of the credit covering local expenditure. The Government's contribution to the project would then be $3.7 million or 23 percent of total cost.

11. It is proposed that funds provided under the IDA credit for loans to growers through their cooperatives for on-farm development and to TTA for necessary equipment and facilities would be channeled through the Tanzania Rural Development Bank (TRDB). The proceeds of the IDA credit to be administered by TRDB would be passed on to TRDB by the Government under a Subsidiary Loan Agreement satisfactory to IDA, the execution of which would be a condition of effectiveness of the credit. The rest of the credit would be used directly by the Ministry of Agriculture and Cooperatives for the salaries of required extension staff and by the Ministry of Communications, Transport and Labour (COMWORKS) for the construction of tea roads in the Bukoba and Lupembe areas.

12. As already indicated, the project is a continuation of an ongoing program. For purposes of cost calculations, expenditures incurred since July 1, 1971 have been included in the project estimates; this is the beginning of the fiscal year for both TTA and the Government. Retroactive financing is proposed of expenditures since July 1 on extension services to growers and urgently-required tea road construction. The amount involved is not expected to exceed $85,000.

Project Implementation

13. TTA would have the main responsibility for carrying out the proposed project. Its principal functions would be to purchase, own and operate the facilities required for leaf collection, processing and marketing; provide the necessary extension services, with staff seconded from the Ministry of Agriculture and Cooperatives, to recruit and instruct smallholder growers in modern tea production techniques; and develop its nurseries so as to ensure that growers will be able to obtain adequate good-quality planting material.

14. Although TTA has been well managed since it was established in 1969, its headquarters staff requires early strengthening to enable it to perform its substantially expanded functions under the project. Experienced managers are also urgently needed for TTA's factories. It is therefore proposed that, before presentation of the project to the Executive Directors, persons with qualifications and experience satisfactory to IDA should be appointed by TTA to the posts of Chief Marketing Officer, Financial Controller, Cost Accountant and Planning Economist. (We understand that a Financial Controller has in fact already been recruited). In addition, also as a condition of Board presentation, TTA would be required to make arrangements satisfactory to the Association with an experienced tea processing group or groups for the provision of experienced management and management training for TTA's existing factories at Lupembe, Mponde and Katumba.

15. The rate of new plantings proposed for the project is very rapid and requires the recruitment of almost 9,000 new growers in 1972. As already indicated, however, recruitment of farmers for the smallholder tea development program has so far been highly successful and TTA already has lists of potential recruits to the program well in excess of the numbers needed. It is proposed that, if delays in the planting schedule should occur, expenditure on new processing facilities would be postponed.

16. It is proposed that the tea roads in Bukoba and Lupembe would be constructed by COMWORKS using departmental forces and with equipment and materials purchased with IDA funds. Qualified personnel would be obtained from consultants for a period of at least two years to supervise and coordinate the construction and subsequent maintenance of the tea roads in the two areas and to train local staff. The units so established would also subsequently be available to construct and maintain other feeder roads in these areas. These arrangements are similar to those incorporated in the recently-approved Third Highway Project for the betterment of feeder roads in the Mara and Geita agricultural districts in Northern Tanzania. The same approach may also be adopted for the NORAD-assisted tea roads in Rungwe and Usambara. In view of the heavy burden which these various works would place on COMWORKS, even with the support of consultants, we are concerned to ensure that its capability would not be overtaxed. This matter would be thoroughly explored during negotiations with a view to satisfying ourselves on this point and to obtaining necessary assurances from the Government.

On-lending Arrangements

17. As already indicated, it is proposed that loans required under the project by farmers for the purchase of fertilizer and planting materials and by TTA for the purchase of vehicles and processing and marketing facilities would be provided by TRDB. This new institution is also the channel for finance under the Agricultural Credit Project and Flue-Cured Tobacco Project (Credit No. 217 TA), a function which it took over with the agreement of the Association from the now defunct National Development Credit Agency (NDCA) with effect from May 1, 1971. TRDB has the capability to assume these additional responsibilities.

18. A mission which visited Tanzania recently to supervise the Agricultural Credit Project has reported that TRDB had in some instances extended loans without sufficient regard to the borrowers' creditworthiness. The Principal Secretary of the Treasury gave the mission a firm undertaking that TRDB would be required to conduct its operations in accordance with sound practices as required by TRDB's statute. We propose to obtain further assurances from the Government and TRDB to that effect during negotiations.

Procurement

19. Contracts for the procurement of tea factories, vehicles, and of equipment and materials required for the tea roads in Bukoba and Lupembe would be let after international competitive bidding. It is proposed that procurement of fertilizer would also be by international competitive bidding but with a 15 percent preference or the appropriate import duty, whichever is the lower, for local manufacturers. A local fertilizer plant is due to come into production in the near future which, according to our information, is high cost; even with a 15 percent preference, its prices may not be competitive. However, we understand that the factory may not in any case produce the type of fertilizer required for the project. This matter will be further explored during negotiations. Contracts for construction of houses would be put out to tender for local competitive bidding, since their number and scattered distribution would not attract overseas firms. Office equipment would also be purchased locally because of the small quantity needed.

Norwegian Participation

20. As already indicated, the proposed Norwegian financing of the tea roads in Rungwe and Usumbara would be complementary to but separate from the IDA credit and would be covered by separate legal arrangements between Norway and Tanzania. To cover the unlikely eventuality of the Norwegian assistance not materializing, our own Development Credit Agreement would include the general provision that Tanzania would make arrangements satisfactory to the Association for the financing, construction and maintenance of the Rungwe and Usambara roads. It would also include the standard provisions regarding the inspection by IDA of the project (i.e. including the

NORAD-assisted roads), the supply of information, and other such matters concerning project execution and supervision. It is hoped that, in accordance with Norway's normal procedure, the goods and services to be financed by Norway would be procured on the basis of international competitive bidding. However, this and other matters of mutual interest to Norway and IDA would be discussed at the time of negotiations, when NORAD proposes to send a representative to Washington.

Marketing Prospects

21. At full maturity in 1984 the acreage planted under the project would produce an estimated 9.5 million kilograms of tea. By that time total Tanzanian tea output should amount to around 22 million kilograms, more than double the present level. The bulk of this additional production would be exported. Despite this prospective substantial increase in Tanzanian exports, no major difficulty is expected in marketing the higher crop. It is estimated that in the early 1980's Tanzania will still account for only about 4 percent of total world exports. In addition, in common with tea produced elsewhere in East Africa, Tanzanian tea is popular with blenders because of its quality; prices obtained by Tanzanian tea at the London auctions have recently been among the highest paid for tea from all producing countries. Demand should remain strong provided quality is maintained.

Economic Rate of Return

22. The overall economic rate of return on the project is estimated at 17 percent, with the return in each of the four areas concerned ranging from 24 percent in Rungwe to 8 percent in West Usambara. The return for West Usumbara is acceptable for an agricultural project in Africa, particularly a project of this kind which will have a significant employment impact and may among other things help to reduce migration to the towns.

IV. THE ECONOMIC SITUATION

23. An economic and preinvestment studies mission visited Tanzania, Kenya and Uganda during October and November, 1970. Volume I of the mission's report (No. AE-16) which deals with recent economic developments within the East African Community, Kenya, Tanzania and Uganda was distributed to the Executive Directors on July 16, 1971. The report confirms that Tanzania has experienced difficulty in raising resources on an adequate scale to finance its investment program and that an increase in external assistance,including assistance with financing local expenditures, is required if the rising trend of development expenditure achieved in recent years is to be maintained.

V. RECOMMENDATION

24. I recommend that the Tanzanian Government be invited to send representatives to negotiate a credit of $10.5 million for the project substantially on the terms and conditions set forth in the attached Appraisal Report.

Michael L. Lejeune
Director

Attachment: Five-Year Lending Program

Attachment

Population: 12.9 m
Per Cap Inc: $95

TANZANIA - FIVE-YEAR LENDING PROGRAM

		($ million) Fiscal Years				
		1972	1973	1974	1975	1976
Rural Development I	IDA	5.0				
Rural Development II	IDA			7.0		
Tobacco II	IDA				7.0	
Tea I	IDA	12.0				
Tea II	IDA				7.0	
Forestry	IDA			7.0		
Livestock II	IDA		10.0			
Livestock III	IDA					10.0
Agriculture (unidentified)	IDA					5.0
Tanzania Investment Bank I	IBRD		3.0			
Tanzania Investment Bank II	IBRD				5.0	
Education IV	IDA		7.0			
Education V	IDA				10.0	
Power III	IBRD			5.0		
Power IV	IBRD					25.0
Urban Development	IDA					5.0
Highways III	IDA	6.0				
Highways IV (Maintenance)	IDA			10.0		
Highways V	IDA					12.0
Unallocated	IDA				5.0	
Operations Program	IBRD	-	3.0	5.0	5.0	25.0
	IDA	23.0	17.0	24.0	29.0	32.0
	Total	23.0	20.0	29.0	34.0	57.0
	No.	3	3	4	5	5

Eastern Africa Department
July 29, 1971

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

August 3, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Nigeria - Second Education Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated August 3, 1971 from the Western Africa Department, entitled "Nigeria - Proposed Second Education Project" (LC/O/71-92).

2. Comments, if any, should be sent to reach Mr. Mirza (ext. 4521) by 5:00 p.m. on Friday, August 6.

3. It is planned then, if the Committee approves, to inform the Government that the Bank is prepared to begin negotiations for the proposed loan on the terms and conditions referred to in the attached memorandum.

J. Chaffey
Acting Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
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CONFIDENTIAL

LC/0/71-92

August 3, 1971

LOAN COMMITTEE

Memorandum from the Western Africa Department

NIGERIA - Proposed Second Education Project

Introduction

1. The attached draft appraisal report "Appraisal of a Second Education Project in Nigeria" (PE-33, dated July 28, 1971) recommends a \$14 million loan to the Federal Republic of Nigeria to finance the \$13 million estimated foreign exchange component and \$1 million estimated interest and commitment charges during construction of a \$22.6 million project for the reconstruction and expansion of 20 secondary schools in the East-Central, Rivers and South-Eastern States and of 7 primary teacher training colleges in East-Central State. The project also includes 23 man-years of technical assistance for technical teacher training, curricula development and project implementation units. The first Education Project (Credit 72-UNI) is now making satisfactory progress after an initial delay due to the late appointment of consultant architects and the civil war. The part of the credit allocated to the former Eastern Region is now being reactivated and we are awaiting the Government's request for a modification of the project before taking further action.

The Economy

2. The last economic report "The Current Economic Position and Prospects of Nigeria" (AW-22a) dated January 21, 1971. was distributed to the Executive Directors on January 29, 1971 and considered, together with Nigeria's Second National Development Plan (1970-74) at the Consultative Group Meeting held on May 3 and 4, 1971 in Paris. The Report and Recommendation of the President on the Rehabilitation Program Loan (R71-67 dated April 2, 1971) contained a brief recent analysis of Nigeria's current position and prospects, which confirmed that Nigeria's need for external capital remained large and that Nigeria was creditworthy for substantial borrowing on conventional, but preferably concessional, terms.

3. Following the \$80 million Program Loan approved in April, 1971, the Bank is currently engaged in substantial project preparation work in support of the government's Development Plan. Three missions have recently reviewed the agriculture, education and transport sectors and their reports, expected to be available shortly, will provide essential

ingredients for an economic mission now planned for October, 1971. The reports will also be the basis for a project list, the preparation of which is expected to be completed by the end of 1971, in time for the next Consultative Group meeting scheduled for May 1972. While the Bank's own fiscal year 1972 lending program for Nigeria is not yet entirely firm, loans for agriculture, power, highways and the proposed Second Education Project are expected to be ready for approval during the current fiscal year. Assuming the intensive preparatory work now in progress results in a pipeline of priority projects, the Bank expects to commit an average of about $100 million per annum through the balance of Nigeria's Second National Development Plan.

The Project

4. The objectives of the proposed project are twofold: rehabilitation and reform.

5. The civil war caused extensive damage to educational facilities in the three eastern States. While UNICEF, UNESCO and bilateral agencies are supporting reconstruction of primary schools and the national university, most secondary schools and the teacher training colleges in East Central State have not yet received any assistance. Their unsatisfactory condition is adversely affecting enrollments and the quality of education and is aggravating the existing shortage of secondary school graduates and qualified teachers. The eastern States limited budgetary resources, unless supplemented by external assistance, are inadequate for rapid reconstruction and expansion of these vital institutions.

6. While reconstruction and expansion are immediate needs, curriculum reform is no less urgent. The Nigerian secondary school system, like that of many developing countries, has expanded with little reference to the country's manpower requirements or the universities' absorptive capacity. Most secondary school graduates, with a general academic education, are ill-prepared for available employment. The eastern States therefore propose to combine reconstruction of selected secondary schools with their conversion into comprehensive schools on the basis of a recently enacted curriculum reform, an approach which will maximize economies of scale in construction and procurement.

7. The project will also include consolidation of 42 small teacher training colleges in East-Central State into 10 state institutions, which will simultaneously be expanded, and three technical assistance components, the details of which are described in the Appendix to the appraisal report. The Bank and the government are currently exploring the possibility of the UNDP financing the technical assistance; if it agrees to do so then the loan would be reduced to about N£13.1 million.

Issues

8. In view of the project's urgency and past experience indicating the need for prompt action on this subject, the Bank proposes to encourage the Nigerians to move ahead with the selection of consultant architects, the employment of which will be a condition of signing of the loan. While the loan is currently planned for presentation to the Directors in October, the early employment of consultants may result in some small expenditures before the loan is signed. In this event, I recommend that such expenditures be financed retroactively from the proposed loan. These expenditures are not expected to exceed $100,000.

Recommendation

9. I recommend that the Federal Government of Nigeria be invited to send representatives to Washington to negotiate a $14 million loan for a term of 25 years, including 10 years of grace on the conditions outlined in paragraphs 6.01-03 of the attached appraisal report.

Bruce M. Cheek
Deputy Director

Population: 62.6 m
GNP Per Cap: $70

P & B 6/16/71

IVa. NIGERIA - 5 YEAR OPERATIONS AND LENDING PROGRAMS
(By Fiscal Year - Amounts in $ millions)

OPERATIONS PROGRAM

			1971	1972	1973	1974	1975	1976
7-NIR-AC-01	Agricultural Credit	IBRD			5.0			
7-NIR-AC-02	Agricultural Credit II	IBRD					10.0	
7-NIR-AL-01	Livestock	IBRD		5.0				
7-NIR-AL-02	Livestock II	IBRD				10.0		
7-NIR-AL-03	Livestock III	IBRD						15.0
7-NIR-AP-01	Cocoa - Western State	IBRD	7.2					
7-NIR-AP-02	Cocoa - Western State II	IBRD				15.0		
7-NIR-AP-03	Tree Crops	IBRD			10.0			
7-NIR-AX-01	Agriculture Unidentified	IBRD					25.0	
7-NIR-AX-02	Agriculture Unidentified II	IBRD						20.0
7-NIR-DD-02	DFC - NIDB II	IBRD	10.0					
7-NIR-DD-03	DFC - NIDB III	IBRD			12.0			
7-NIR-DD-04	DFC - NIDB IV	IBRD					12.0	
7-NIR-EE-02	Education II	IBRD		10.0				
7-NIR-EE-03	Education III	IBRD			25.0			
7-NIR-EE-04	Education IV	IBRD					20.0	
7-NIR-PH-03	Power V	IBRD				25.0		
7-NIR-PP-01	Power IV	IBRD		35.0				
7-NIR-GG-01	Rehabilitation Program Loan	IBRD	80.0					
[illegible]IR-II-01	Small-Scale Industry	IBRD			3.0			
7-NIR-IX-01	Industry Unidentified I	IBRD				10.0		
7-NIR-IX-02	Industry Unidentified II	IBRD						10.0
7-NIR-TH-05	Roads - Federal & State	IBRD		15.5				
7-NIR-TH-06	Roads VI	IBRD			20.0			
7-NIR-TH-07	Roads VII	IDA			20.0			
7-NIR-TX-01	Roads - Unidentified I	IBRD					25.0	
7-NIR-TX-02	Roads - Unidentified II	IBRD						30.0
7-NIR-TA-01	Airports	IBRD					5.0	
7-NIR-TP-02	Ports II	IBRD			15.0			
7-NIR-TR-02	Railways II	IBRD				40.0		
7-NIR-XX-01	Unallocated	IBRD						25.0

		Total								
	1964-68	1969-73	1972-76							
IBRD	144.0	308.8	452.5	IBRD	97.2	65.5	90.0	100.0	97.0	100.0
IDA	35.5	20.0	20.0	IDA			20.0			
Total	179.5	328.8	472.5	Total	97.2	65.5	110.0	100.0	97.0	100.0
No.	6	19	28		3	4	8	5	6	5

LENDING PROGRAM (11/23/70)

IBRD	144.0	309.2	454.5	IBRD	98.6	65.0	89.5	100.0	100.0	100.0
IDA	35.5									
Total	179.5	309.2	454.5	Total	98.6	65.0	89.5	100.0	100.0	100.0
No.	6	16	27	No.	3	3	6	6	6	6

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

July 28, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Kenya - Fourth Highway Project

1. The Committee is requested to consider, without meeting, the attached memorandum of July 28, 1971 from the Eastern Africa Department, entitled "Kenya: Fourth Highway Project" (LC/O/71-91).

2. Comments, if any, should be sent to Mr. Kaji (ext. 4917) by 5:00 p.m. on Monday, August 2, 1971.

3. It is planned then, if the Committee approves, to inform the Government that the Bank is prepared to begin negotiations for the proposed credit on the terms and conditions referred to in the attached memorandum.

J. Chaffey
Acting Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
Controller

Copies for Information:

President
The Economic Adviser to the President
Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

CONFIDENTIAL

LC/O/71-91

July 28, 1971

LOAN COMMITTEE

Memorandum from the Eastern Africa Department

KENYA: Fourth Highway Project

I. INTRODUCTION

1. The Bank Group has extended Kenya seven loans and credits, totalling $65.2 million, for road development. The major emphasis of Kenya's 1970-74 Road Development Program, as well as our past lending, has been towards expansion and improvement of the feeder and minor access road network in the rural areas. The proposed project is a part of this program and a continuation of the developments initiated under our past operations.

2. In addition to the proposed project, the lending program for FY 72 contains a proposed loan of about $20 million for the Nairobi Airport Project, which is scheduled for appraisal in mid-August. The 1972-76 Lending Program for Kenya is attached.

II. THE PROJECT

3. The attached appraisal report (No. PTR 92) recommends an IDA Credit of $22 million for financing the proposed project comprising:

(a) construction, reconstruction or improvement of

- (i) five feeder roads totalling 158 km
- (ii) 995 km of tea collection roads
- (iii) 429 km of access roads in settlement areas
- (iv) three trunk roads sections totalling 71 km;

(b) construction and equipping of four vehicle weighing stations; and

(c) retention of consultants for completion of engineering and supervision of construction.

4. Kenya follows the policy of stage construction under which the geometric and pavement design standards adopted are such that it is possible progressively to upgrade a road to meet increased traffic needs by successive increases in the thickness of the bituminous overlay. While the design standards for foundations, gradients, curves, etc. adopted under such policy are higher than that required to meet the immediate traffic needs, the justification for this approach is that it permits successive upgrading over a period of time without necessitating scrapping of the existing road which would be the case if standards adopted were limited to meeting only immediate needs. Many of the feeder and trunk roads included in the proposed project are either extensions of roads constructed under past projects, or the next step in the program of stage construction. The bulk of rural access roads included in the project are extensions of development schemes initiated under past projects.

5. The total cost of the project is estimated at US $42 million, of which foreign exchange component is estimated at US $28 million (67%). The Kingdom of Sweden has offered to provide Kenya up to $6 million to finance a part of the foreign exchange costs, the balance of which will be covered by the proposed IDA credit of $22 million.

6. The proposed project will provide infrastructure required for agricultural development. The estimated economic rate of return ranges between 12% to 30% on individual project items and averages 19% on the project as a whole.

Project Execution and Procurement

7. As in the case of our previous projects, the Ministry of Works (MOW) will be responsible for execution of the project. Consultants, acceptable to the Association, will assist in construction supervision.

8. Construction of all project roads, except 414 km of access roads in settlement areas, will be carried out by contractors. Contracts will be awarded on the basis of international competitive bidding. The only proposed exception to this is the contract for paving a 23 km feeder road estimated to cost about US $400,000. The Government proposes to negotiate this contract as an extension to the ongoing contract for the gravelling of the same road, which was awarded after international competitive bidding under Loan No. 639 KE (Third Highways Project). It is expected that because the contractor has already mobilized for work on this stretch of road, this procedure will permit Kenya to obtain unit prices lower than can be expected from any new contactor. The terms of such a negotiated contract would be subject to our approval and I recommend that if it is demonstrated that the negotiated unit price is indeed less than current bid prices for similar work, we waive the requirement for international competitive bidding on this contract.

9. Construction of 414 km of the access roads in settlement areas, which would account for less than $700,000 of the proposed Credit, will be carried out by the Ministry of Works' own construction units utilizing labor from the National Youth Service (NYS). Construction of such low standard roads, which are widely dispersed, is unlikely to attract reasonable bids from contractors. The proposal to utilize departmental units is therefore appropriate. Such departmental units employing NYS labor were also utilized for the construction of settlement roads financed under Loan No. 639 KE (Third Highways Project). Though there were some initial administrative and organizational difficulties, the recent introduction of double work shifts and a program of incentives has improved performance and the standard of the work completed by such units is satisfactory. During negotiations we shall discuss with the Government the effectiveness of the measures introduced to improve the performance of departmental construction units and obtain assurances that the performance levels achieved will be maintained.

10. The project provides for a small amount of construction equipment and spare parts (US $383,000) for the MOW construction units. It is proposed that this equipment be procured under the contracts recently awarded after international competitive bidding under Credit No. 224 KE (Highway Maintenance Project). In view of the small amount involved, this procedure is considered acceptable.

Retroactive Financing

11. One of the settlement roads (Wanjohi-Geta) to be constructed under the project by MOW Construction Units is situated in an area where a MOW unit is currently carrying out construction work on a road financed under the Third Highways Project (Loan No. 639 KE). This work is expected to be completed by September, 1971 and it would be economical to permit the unit to remain in the area and continue work on the road included in the proposed project before moving on to another area. This could entail foreign exchange expenditures of up to $170,000 before signing of the proposed credit and the Government has requested retroactive financing up to $170,000 for expenses incurred after September 30, 1971. I recommend we agree to this request.

Enforcement of Vehicle Regulations

12. Progressive increase in the size of vehicles and lax enforcement of weight regulations has resulted in axle loadings in excess of those for which the roads were designed and consequent failure of important sections of certain trunk roads. The Government has, under past loan and credit agreements, provided assurances that vehicle weight limitations would be enforced. The MOW and the Kenya Police have now drawn up a long-term plan for establishing an effective highway traffic law enforcement agency. This plan calls for the construction of permanent weighing stations at four strategic

points in the road network and the establishment of special highway patrols to facilitate enforcement of the regulations. Six weighbridges, of which four weighbridges have already been purchased by the Government out of its own resources, will be installed by the MOW under the project. While some progress has also been made in equipping the highway patrols, there is a need for working out a firm timetable for implementing the plan. During negotiations we shall agree on such a timetable and obtain assurances that it will be adhered to.

Swedish Participation

13. The proposed Swedish Credit would be made to the Government on IDA terms and would be disbursed pro rata with the proposed IDA Credit. Documentation for the financing will follow the pattern of other projects jointly financed with Sweden. It is expected that the documents for the proposed Swedish Credit will be signed at the same time as the IDA Credit documents, and that the Swedish Credit will be made effective prior to, or simultaneously with, the effectiveness of the IDA Credit.

III. THE ECONOMY

14. An economic report on Kenya (Report No. AE-16a Volume 1) was distributed on July 16, 1971. The report states that a good start has been made in implementing the 1970-74 Development Plan and that by the end of 1970 economic growth was approximately in line with the Plan target, despite a poor agricultural season in 1969.

15. Kenya has in the past received large amounts of external assistance, generally on favorable terms. On the basis of its generally sound policies and plans for the future, Kenya will continue to require and merit substantial external assistance. Although debt service payments in 1969 absorbed only 6.8% of foreign exchange earnings during the year, it is projected that the debt service ratio may be in excess of 11% by 1980. In view of its low per capita income ($132) and limited prospects for its major export commodities, it is desirable that Kenya should obtain the major proportion of external assistance on concessional terms.

IV. RECOMMENDATION

16. I recommend that the Association invite representatives of the Republic of Kenya to negotiate a Development Credit of $22 million, substantially on the terms and conditions set forth in paragraphs 6.01 to 6.03 of the Appraisal Report.

Michael L. Lejeune
Director

Attachment

Population : 10.2m.
GNP Per Cap.: $130

KENYA - 5 YEAR OPERATIONS PROGRAM
(By Fiscal Year - Amounts in $ millions)

		1972	1973	1974	1975	1976
Agricultural Credit	IDA		3.0			
Agricultural Credit	IDA					6.0
Cotton	IDA			3.0		
Irrigation	IDA					10.0
Livestock II	IDA			8.0		
Horticulture Devt.	IDA		3.0			
Agric. Unidentified	IDA				4.0	
Agric. Unidentified	IDA					5.0
DFC	IBRD		2.0			
DFC	IBRD				3.0	
Education III	IDA			7.0		
Education IV	IDA					10.0
Power	IBRD			5.0		
Gtaru Power	IBRD					35.0
Tourism	IBRD		7.0			
Nairobi Airport	IBRD	20.0				
Highways IV	IDA	20.0				
Highways V	IBRD/IDA				25.0	
Urban	IDA			5.0		
Water Supply	IBRD					10.0
	IBRD	20.0	9.0	5.0	13.0	45.0
	IDA	20.0	6.0	23.0	19.0	31.0
	TOTAL	40.0	15.0	28.0	32.0	76.0
	No.	2	4	5	3	6

Eastern Africa Department 7/23/71

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

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July 27, 1971

B 1106

MEMORANDUM TO THE LOAN COMMITTEE

Thailand: Electricity Generating Authority

1. The Committee is requested to consider, without meeting, the attached memorandum of July 27, 1971 from the East Asia and Pacific Department, entitled "Thailand - Proposed $25 million Loan to the Electricity Generating Authority of Thailand" (LC/O/71-90).

2. Comments, if any, should be sent to Mr. Homsi (ext. 4256) by 5:00 p.m. on Friday, July 30.

3. It is planned then, if the Committee approves, to inform the Government that the Bank is prepared to begin negotiations for the proposed loan on the terms and conditions referred to in the attached memorandum.

J. Chaffey
Acting Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
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Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

CONFIDENTIAL
LC/O/71 - 90

July 27, 1971

LOAN COMMITTEE

Memorandum from East Asia and Pacific Department
THAILAND - Proposed $25 million Loan to the
Electricity Generating Authority of Thailand

1. Attached is an appraisal report (PU-75) dated July 7, 1971, recommending a loan of $25 million to the Electricity Generating Authority of Thailand, (EGAT), to help finance the cost of imported equipment and engineering services in connection with an oil-fired 310 MW thermal generating unit to be installed at the South Bangkok Power Station. The proposed loan would be guaranteed by the Kingdom of Thailand.

Economic Situation

2. Thailand's economy has taken an adverse turn in the last two years, after an unusually favorable record of economic growth, financial stability and growth during the 1960's. Between 1965 and 1969, (Thai fiscalyears begin on October 1 and end on September 30), the Thai economy grew at an annual rate of 9 percent; exports rose by 8.7 percent annually, prices were fairly stable and foreign exchange reserves increased from $354 million in 1960 to $874 million at the end of 1969 - equivalent to about nine months' imports. Many factors contributed to the achievements of the 1960's, but especially favorable markets for Thailand's main export, rice and large inflows of funds from the United States in the forms of aid and military expenditures related to the conflict in Indo-China.

3. The recent adverse trend of the economy is attributable to the unfavorable developments of the last two years in the international rice market and to the reduction in U.S. aid and expenditures in Thailand. Because of these developments, receipts from exports did not grow as fast as had been expected while imports continued to rise. As a result, the loss of foreign exchange reserves in 1970 exceeded $128 million, more than twice the loss of 1969, for a total loss of $176 million in 1969 and 1970.

4. The same pattern of the last two years is continuing in 1971. It appears to reflect not only the basic, and possibly extended turn for the worse in foreign receipts, but also Thai reluctance to accept austerity measures which the changed circumstances would seem to call for.

5. The central government accounts for FY 1970 show a slightly better outcome than had been expected last summer, but expansionary

financing of the overall cash deficit of Ø4.32 billion ($207.7 million) was still substantial. The Government drew down its cash reserves and borrowed record amounts from the Bank of Thailand. Net external borrowing reached only Ø34 million ($1.6 million) and domestic borrowing from the non-bank public fell far short of expectations. As a result, recourse to expansionary financing was much larger than envisaged. Revised estimates for FY 1971 indicate an even larger government cash deficit of Ø6.63 billion ($318.7 million). Although this estimate may be too high, a significant deterioration of the fiscal position appears inevitable this year, in part due to increased military spending. The effect of the revenue measures - mainly increases in customs duties - taken in July 1970 seems less than expected, and political opposition to effective measures appears as insuperable as ever.

6. On the private front, there is a reluctance to curb the momentum of investment generated during the sixties, and private, as well as public credit expansion have continued at high rates.

7. All this amounts, in effect, to a willingness to live, at least temporarily, on the large reserve accumulations of the sixties rather than face up to the economic problems and the political difficulties of restrictive financial and economic policies. The reserve position is still strong - $745 million at the end of 1970 - but the trend, and the absence of measures to check the trend, are disturbing. Should the present trend continue, Thailand's foreign exchange reserves are expected to decline further to about $540 million by the end of 1972, equivalent to less than five months' imports.

8. An economic mission is now in Thailand to review the Third National Economic and Social Development Plan, (1972-1976) which is scheduled to begin on October 1, 1971. A number of sector missions are also reviewing agriculture, education, industry, tourism, and later this year, transportation. In addition, a mission is reviewing the North East Economic Development Plan (NEED Plan) and hopes to identify projects suitable for Bank financing in the North East. The economic mission should be able to suggest a program of economic growth with stability; the program would be discussed with the Thai authorities before the mission's return, and later on this year, in greater detail, prior to the Consultative Group meeting in December. It is hoped that a program can be devised which might stem the outflow of reserves without seriously impairing economic growth and, if so, that the Government will be able to accept the necessary remedial policies. If such policies are adopted, and if, as seems feasible, the Thai economy moves towards a more aggressive export policy, the deterioration of the balance of payments may be corrected. On the domestic front, it should be possible to increase taxation and thereby reduce, in the absence of unexpected military requirements, the budget deficit to manageable proportions. In the long run, Thailand has shown itself capable of prudent economic management, although major policy decisions are made slowly. The strong reserve position allows Thailand some time in

which to deal with the problems it faces, and although service on external public and private debt - 17 percent of exports of goods and services - is a rather heavy burden on the balance of payments, it is nevertheless a manageable one.

Lending Program

9. There was only one loan to Thailand in FY 1971, $12.5 million for the expansion of Bangkok Port. Construction under the loan has been delayed for nearly a year because of difficulties in evicting squatters from the project area. The Port Authority is confident that this problem will be resolved through court action, which has already started. Bids for the construction of new berths have recently been opened.

10. Our lending program for FY 1972 includes, in addition to the proposed project, three other projects in education, telecommunications and transportation: The Kasetsart University project ($13.5 million) has been fully appraised, and will be submitted to the Loan Committee soon. The Telecommunications project ($30 million) will be jointly appraised with ADB in September, as ADB has expressed an interest in financing part of the project. The Fifth Highway Project ($25-35 million) is to be reappraised in October, this year. All these projects have a high probability rating, and are expected to reach the stage of Board consideration in the current fiscal year, as we expect that legislation authorizing the Government to borrow from the Bank at our current interest rate will be enacted by October. Total lending for FY 1972 is therefore likely to reach the range of $90 - 100 million, depending on which parts of the Telecommunications project ADB is prepared to consider, and on the findings of the reappraisal mission in connection with the Fifth Highway Project. Attached is an Annex showing the Lending Program for Thailand.

Power Sector and Project

11. Of gross lending of about $394 million to Thailand, $130 million has been for power and multipurpose projects ($112.5 million) including power such as the Bhumipol and Sirikit dams. The power sector of Thailand was reviewed by a mission which visited the country in November and December, 1970. The mission's report, entitled "Thailand - Power Sector Review" is dated June 29, 1971.

12. The growth of power consumption in Thailand has been very rapid, averaging 27% per year since 1961, with annual increases of about 30% in the late 1960s. This rapid increase reflects the growth of the Thai economy in general, and of the industrial sector in particular. In fact, power sales to the industrial sector have increased from nearly 42% in 1964 to about 62% in 1969. Power generation in 1969 was mostly by thermal means (71%) with hydro generation accounting for only

29% of total public power generation. Notwithstanding the very rapid growth of the power sector, only about 17% of the population of Thailand had an assured power supply in 1969; and in the rural areas, only 10.8% of the population had electrical service.

13. The proposed loan would finance the cost of acquiring and installing the 4th unit at the South Bangkok Thermal Station, and the cost of related engineering and supervision services. The project follows upon Loan 655-TH ($46.5 million, of 1970) which includes $24.1 million forunit number Three being installed at the South Bangkok Thermal Station. When bids were invited for the third unit EGAT's specifications stipulated that bidders should include options for the supply of an identical fourth unit. The procurement procedures were in accordance with the Bank's requirements for international competitive bidding and were carried out with the Bank's agreement. EGAT intends to exercise its option for the 4th unit in November 1971. No retroactive financing is involved, and the procurement arrangements have been reported to the Executive Directors in the Monthly Operational Summary.

14. The total estimated cost of the project is $41.1 million, of which the proposed loan of $25.0 million would cover all the foreign exchange requirements except for $1.7 million in foreign exchange for civil works. EGAT proposes to carry out the civil works with its own forces and without international competitive bidding for imported materials. The proposed loan includes $1.7 million for engineering and supervision by consultants. Contingencies of $0.5 million, while on the low side, are considered sufficient as the price of equipment to be purchased under the option is known. The internal financial rate of return of the project is estimated at 23% after making allowances for price increases in the cost of imported fuel oil.

15. It is estimated that EGAT's total investments and working capital requirements during the construction period (1972-1976) of the project will total about $384 million; of this EGAT is expected to generate about $129 million (33.6%) through retained earnings and depreciation funds, leaving about $255 million (66.4%) to be financed from external sources. This amount includes the proposed loan; about $36 million to be disbursed under Loan 655-TH, and an estimated loan of $25 million for the Quai Yai project which is included in our lending program for FY 1973, but which is expected to slip to FY 1974 because of technical difficulties in project preparation. In view of its sound financial position, EGAT should have no difficulty in obtaining the funds necessary for its expansion on reasonable terms, either from the Government or from other sources.

16. The project will be administered by EGAT, which was created in 1969 by the merger of three generating authorities - the Yanhee Electricity Authority (YEA), the Lignite Authority and the Northeast Electricity Authority. The Act establishing EGAT is similar to the

former YEA Act, and the officers of the former YEA hold the same positions in EGAT. All power projects financed by the Bank in Thailand, whether under loans made to YEA or to EGAT, have been carried out satisfactorily. The undisbursed balance of Loan 655-TH amounted to $42.3 million on June 30, 1971. Four other loans have been fully disbursed.

17. The Government of Thailand has proposed that EGAT acquire the assets of the Chemical Fertilizer Company of Thailand (Chemferco) which has been in difficulties for some time. Chemferco uses as raw material and fuel lignite mined by EGAT. At the suggestion of the Bank, the Government has agreed to a study of all aspects of Thailand's fertilizer needs, and has further agreed to defer any action regarding the proposed acquisition of Chemferco by EGAT pending the outcome of the proposed study. Terms of reference for the study will be prepared by the agricultural and industrial sector review missions which are now in Thailand.

18. The Government's authority to guarantee loans made by the Bank to EGAT is not impaired by the legislation now in force limiting Government borrowing from the Bank to an interest rate of 7%. As EGAT, and not the Government, is the proposed borrower, the present legislation is not a constraint.

Recommendation

19. I agree with the conclusions of the appraisal report and recommend that the Government of Thailand and EGAT be invited to send negotiators to Washington to negotiate a loan for $25 million for a term of 20 years including a 5-year grace period.

Douglas J. Fontein
Deputy Director

Attachment

Attachment

Population: 34.1 m) 1/
GNP Per Cap: $184)

THAILAND - 5 YEAR OPERATIONS PROGRAM
(By Fiscal Year - Amounts in $ millions)

OPERATIONS PROGRAM

			1971	1972	1973	1974	1975	1976
6-THL-AC-02	Agricultural Credit I	IBRD					10.0	
6-THL-AI-07	Irrigation - Pitsanuloke	IBRD			27.0			
6-THL-AI-08	Irrigation - Uttaradit	IBRD						27.0
6-THL-AD-01	Chao Phya Devt.	IBRD			5.0			
6-THL-AX-02	Agric.Unidentified I	IBRD			5.0			
6-THL-AX-03	Agric.Unidentified II	IBRD				10.0		
6-THL-AX-04	Agric.Unidentified III	IBRD					5.0	
6-THL-CC-01	Telecommunications I	IBRD		30.0				
6-THL-CC-02	Telecommunications II	IBRD				10.0		
6-THL-DD-03	DFC - IFCT II	IBRD				5.0		
6-THL-DD-04	DFC - IFCT III	IBRD						10.0
6-THL-EE-02	Kasetsart Univ.	IBRD		13.5				
6-THL-EE-03	Education - Agric.& Fish.	IBRD				10.0		
6-THL-EX-01	Education - Unident.I	IBRD			10.0			
6-THL-EX-02	Education - Unident.II	IBRD						10.0
6-THL-IL-01	Industrial Estate I	IBRD				5.0		
6-THL-PT-01	Power VI - S.Bkk.Thermal	IBRD		25.0				
6-THL-PH-04	Quai Yai Dam & Power	IBRD			25.0			
6-THL-QX-01	Tourism Unidentified	IBRD				5.0		
6-THL-TH-05	Highways V	IBRD		25.0				
6-THL-TH-07	Highways VI	IBRD					30.0	
6-THL-TP-04	Port - Bangkok III	IBRD	12.5					
6-THL-TP-06	Port - Deepwater	IBRD				20.0		
6-THL-UT-01	Urban Transportation	IBRD					10.0	
6-THL-WE-01	Sewerage - Bangkok	IBRD				5.0		
		IBRD	12.5	93.5	72.0	70.0	55.0	47.0
		No.	1	4	5	8	4	3

	Total 1964-68	1969-73	1972-76
IBRD	132.5	247.5	337.5
	8	12	24

1/ Preliminary Estimates

East Asia and Pacific Department
July 19, 1971

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

July 27, 1971 73-1108

MEMORANDUM TO THE LOAN COMMITTEE

Thailand - Second Education (Kasetsart University) Project

1. The Committee is requested to consider, without meeting, the attached memorandum of July 27, 1971 from the East Asia and Pacific Department, entitled "Thailand - Proposed $13.5 Million Loan to the Kingdom of Thailand for a Second Education (Kasetsart University) Project" (LC/O/71-89).

2. Comments, if any, should be sent to Mr. Homsi (ext. 4256) by 5:00 p.m. on Friday, July 30.

3. It is plannned then, if the Committee approves, to inform the Government that the Bank is prepared to begin negotiations for the proposed loan on the terms and conditions referred to in the attached memorandum.

J. Chaffey
Acting Secretary
Loan Committee

- DISTRIBUTION -

Committee:

Mr. J. Burke Knapp, Vice President, Chairman
Mr. S.R. Cope, Deputy Chairman
Mr. S. Aldewereld, Vice President
General Counsel
Director of the Development Services Department
Directors of the Area Departments
Deputy Director, Projects
Directors of the Projects Departments
Director, Development Finance Companies Department
Director of the Economics Department
Controller

Copies for Information:

President
The Economic Adviser to the President
Sir Denis Rickett, Vice President
Mr. M. Shoaib, Vice President
Directors, other Departments
Executive Vice President (IFC)
Vice President (IFC)

CONFIDENTIAL
LC/O/71-89

July 27, 1971

LOAN COMMITTEE

Memorandum from East Asia and Pacific Department

THAILAND - Proposed $13.5 Million Loan to the

Kingdom of Thailand

for a Second Education (Kasetsart University) Project

1. Attached is an appraisal report (PE-32), dated July 2, 1971, recommending a loan of $13.5 million to the Kingdom of Thailand to assist in improving and expanding university training and research in agriculture and related fields at Kasetsart University (KU).

Economic Situation

2. Recent developments in the Thai economy are described in a memorandum dated July 21, 1971, submitted to the Loan Committee in connection with a proposed loan of $25 million to the Electricity Generating Authority of Thailand (EGAT). Despite a slowdown in the economy and a decline in foreign exchange reserves, the question of creditworthiness does not arise, and Thailand is well able to borrow substantial amounts externally. An economic mission is now in Thailand to review the Third National Economic and Social Development Plan (1972-1976) which begins on October 1, 1971.

Lending Program

3. A copy of the five-year lending program for Thailand is attached. Projects which are expected to be presented to the Executive Directors in FY 1972 are described in the memorandum of July 21, 1971, to the Loan Committee, in connection with the proposed loan to EGAT. Beyond FY 1972, the lending program includes three other education projects which the economic mission presently in Thailand is expected to identify. A sector survey mission from UNESCO which visited Thailand in 1970 had identified a number of projects for external financing. However, ADB expressed an interest in financing the projects which UNESCO considered to have high priority, and offered to consider making "soft" loans for this purpose. A member of the economic mission will visit ADB for discussions of the status of these projects in August.

Agricultural Sector and the Project

4. Agriculture is the leading sector of the Thai economy, providing about 32 percent of GDP and employing almost 80 percent of the labor force.

Eight of Thailand's nine principal exports derive from agriculture, and rice, alone, accounts for some 20 percent of merchandise exports. In the last two decades agriculture achieved a commendable growth rate, attributable more to the expansion of cultivated area than to increases in yields. As undeveloped fertile lands become scarcer, this condition is beginning to change. Moreover, with increasing self-sufficiency in Thailand's traditional markets, the outlook for rice exports is not particularly good. In the circumstances, future growth will have to rely more on the intensification of methods of production and on diversification of output. The proposed loan will assist Thai agriculture by providing the trained manpower necessary to expand extension services, improve research and upgrade agricultural education in general. The Third National Economic and Social Development Plan, which is scheduled to come into effect in October, 1971, is expected to propose a major shift in agricultural policy, away from large projects towards the completion of existing facilities and the intensification of production. This change in policy will require greater on-farm advice and technology, and these will have to be provided by a larger and better extension service.

5. The proposed loan would be the Bank's second education loan to Thailand. The first, 471-TH of October, 1966, provided $6 million for vocational education. After a slow start, it is now proceeding well, although a second postponement of the closing date may be necessary to allow the project authorities to complete their procurement program. Kasetsart University is Thailand's main center of higher education in agriculture, providing about 70 percent of agricultural graduates in Thailand. Other universities with agricultural curricula exist at Khonkaen and Chiengmai, in the Northeast and North, respectively, and in Bangkok, at Chulalongkorn University. These universities, however, are multidisciplinary, and in fact, Kasetsart University is the main source of staff for their faculties and for agricultural vocational education throughout the country. Kasetsart graduates also serve in Thailand's extension services and in the agribusiness sector of the economy.

6. The Bank was first approached for a loan for this project in August, 1968, following which reconnaissance missions visited KU in 1968 and 1969 to develop the project content to the stage where it could be prepared. Project preparation was undertaken by FAO but delay in its completion occurred due to disagreements on the pace of the university's development in a rural environment. The university is located just outside Bangkok, at Bangkhen, and although it had acquired some 3000 acres in the country at Kamphaengsaen, about 80 km northwest of Bangkok, KU believed that its near-term expansion should take place at the Bangkhen (Bangkok) campus, with the development of Kamphaengsaen to follow in a subsequent stage. Conversely, the preparation mission held that agriculture could not be taught in an urban environment without adequate opportunities for field work, and suggested that the development of a campus at Kamphaengsaen form part of the project. These disagreements were eventually resolved, and the project was appraised in October, 1970.

7. The project is based on KU's development plan (1968-1974) prepared with assistance from the Rockefeller Foundation. Under the Plan, total enrollment will increase from 3,800 in 1970 to 5,800 in 1980; the number of teachers will increase and their qualifications and experience will be improved under a staff development plan; research, teaching and training facilities will also be improved. The project would expand total enrollment by 1,520 students, providing 1,545 new places at the University's present campus at Bangkhen, and 1,520 places at a new campus to be developed at Kamphaengsaen. The places would be provided in new laboratories in the Faculties of Agriculture (both campuses), Fisheries and Forestry (both at Bangkhen), Veterinary Science and Engineering (both at Kamphaengsaen), Economics (both campuses) and Arts and Sciences (Bangkhen). In addition, 1,100 lecture room places would be constructed and boarding facilities would be provided for 1,550 students at Kamphaengsaen where 380 units of staff housing would also be provided. Administration and communal facilities to be provided under the proposed loan include administrative offices, two central libraries, two dining halls, central maintenance and storage facilities, two health centers, one multipurpose hall, one student union building and a primary school to serve children of staff assigned to Kamphaengsaen and at the same time allow teaching experience to be acquired by candidates for teaching certificates. It is expected that the primary school will be opened to other residents of Kamphaengsaen as well.

8. The technical assistance component of the proposed loan is fairly large; 42 man-years of technical assistance are provided for curriculum development, university management, project implementation, and studies on: (i) agricultural education training and extension services; and (ii) veterinary education. The studies are described in paragraphs 9 and 10 below. In addition, 400 man-years of fellowships are provided to upgrade the staff of the university. The total cost of the project is equivalent to $27 million, of which the proposed loan of $13.5 million would finance the estimated foreign exchange component.

9. At present there are two faculties of veterinary education in the Bangkok area, at Kasetsart and Chulalongkorn universities. Both the project preparation mission (FAO) and the Bank's appraisal mission questioned the Thai's position that more than one faculty of veterinary education is needed in Thailand. To assist the authorities in examining this matter, the proposed loan includes one man-year of technical assistance for a study of veterinary education and training, veterinary services and employment opportunities and requirements for veterinarians. It is agreed that this review of veterinary education and training would include <u>inter alia</u> a recommendation as to the advisability of continuing two faculties.

10. Agricultural education institutions, including universities, suffer from a lack of an adequately trained staff, practical orientation and experience with modern agricultural techniques. These weaknesses are reflected in the government's extension services, the staff of which tend to be administrators rather than extension workers. In view of the great

importance which agricultural training and extension have for Thailand, the proposed loan includes three man-years of technical assistance for a study of all levels of agricultural training, and of agricultural extension services. Both studies will be undertaken under the auspices of the Ministry of Agriculture.

11. Following a Loan Committee meeting of May 7, 1971, discussions were held in Bangkok in May, 1971, with the Government and the University authorities, and preliminary agreement was reached on the steps to be taken by KU in advance of the proposed loan. To help finance the recruitment of an adviser, campus planners and executive architects, and the start of the two studies, the Government and KU were informed that the Bank would agree to recommend to the Executive Directors that $200,000 be included in the proposed loan for retroactive financing. The Government agreed to advance this amount to the University and the Ministry of Agriculture.

12. Legislation now in effect in Thailand does not permit the Government to borrow from the Bank at more than 7 percent interest. The Ministry of Finance has advised the Bank that proposed legislation, permitting the Government to borrow from external sources without regard to interest rates has recently been approved by the Cabinet and the Juridical Council. The Ministry of Finance confidently expects their action to lead to enactment of satisfactory legislation by October 1, 1971, when the Third National Economic and Social Development Plan is scheduled to take effect.

13. In order to present the proposed loan to the Executive Directors in the first half of October, negotiations would have to take place in late August or early September. Because of the several government entities involved, negotiators for the proposed loan will have to represent not only KU and the Ministry of Finance, but the Ministry of Agriculture and, quite probably, the National Education Council. Designating a negotiating team is always a fairly lengthy process in Thailand and requires more than a month since the team and their terms of reference must be agreed by the Cabinet. Invitations to negotiate should, therefore, be sent in the near future.

Recommendation

14. I agree with the recommendations of the appraisal report and recommend that the Government and Kasetsart University be invited to send representatives to Washington in late August or early September to negotiate a loan of $13.5 million for a term of 30 years, including a 10-year grace period, with the understanding that the proposed loan would not be presented to the Executive Directors until enactment of satisfactory legislation enabling the Government to borrow from the Bank at 7¼% interest.

Douglas J. Fontein
Deputy Director

Attachment

Attachment

Population: 34.1m)1/
GNP Per Cap: $184)

THAILAND - 5 YEAR OPERATIONS PROGRAM
(By Fiscal Year - Amounts in $ millions)

OPERATIONS PROGRAM			1971	1972	1973	1974	1975	1976
6-THL-AC-02	Agricultural Credit I	IBRD					10.0	
6-THL-AI-07	Irrigation - Pitsanulohe	IBRD			27.0			
6-THL-AI-08	Irrigation - Uttaradit	IBRD						27.0
6-THL-AD-01	Chao Phya Devt.	IBRD			5.0			
6-THL-AX-02	Agriculture Unidentified I	IBRD			5.0			
6-THL-AX-03	Agriculture Unidentified II	IBRD				10.0		
6-THL-AX-04	Agriculture Unidentified III	IBRD					5.0	
6-THL-CC-01	Telecommunications I	IBRD		30.0				
6-THL-CC-02	Telecommunications II	IBRD				10.0		
6-THL-DD-03	DFC - IFCT II	IBRD				5.0		
6-THL-DD-04	DFC - IFCT III	IBRD						10.0
6-THL-EE-02	Kasetsart University	IBRD		13.5				
6-THL-EE-03	Education - Agric. & Fisheries	IBRD				10.0		
6-THL-EX-01	Education - Unidentified I	IBRD			10.0			
6-THL-EX-02	Education - Unidentified II	IBRD						10.0
6-THL-IL-01	Industrial Estate I	IBRD				5.0		
6-THL-PT-01	Power VI - S.Bangkok Thermal	IBRD		25.0				
6-THL-PH-04	Quai Yai Dam & Power	IBRD			25.0			
6-THL-QX-01	Tourism Unidentified	IBRD				5.0		
6-THL-TH-05	Highways V	IBRD		25.0				
6-THL-TH-07	Highways VI	IBRD					30.0	
6-THL-TP-04	Port-Bangkok III	IBRD	12.5					
6-THL-TP-06	Port - Deepwater	IBRD				20.0		
6-THL-UT-01	Urban Transportation	IBRD					10.0	
6-THL-WE-01	Sewerage - Bangkok	IBRD				5.0		
		IBRD	12.5	93.5	72.0	70.0	55.0	47.0
		No.	1	4	5	8	4	3

	Total 1964-68	Total 1969-73	Total 1972-76
IBRD	132.5	247.5	337.5
	8	12	24

1/ Preliminary Estimates

East Asia and Pacific Department
July 21, 1971