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Central America
Eco. Integration

THE CENTRAL AMERICAN COMMON MARKET

BRIEFING NOTES

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Section 1

CENTRAL AMERICA--A BRIEF OVERVIEW

The Central American Common Market (CACM) area includes Guatemala, Honduras, El Salvador, Nicaragua, and Costa Rica, a total area of 441,000 square kilometers, roughly the size of the State of California. The total population is about 16.3 million and the average per capita GNP as of 1973 was around $460 (Table 1). Principal exports from the region include cotton, coffee, bananas, beef, sugar, and wood. The first three constituted 70-80 percent of exports in the 1960s and around 50 percent in the early 1970s, reflecting the increased trade in manufactures. Coffee, the leading regional export, was largest in value for Costa Rica, El Salvador and Guatemala; it was second largest for Honduras and Nicaragua. About 75 percent of the region's exports by value was destined to third country markets by the end of the 1960s, a marked decline from the 90-95 percent share in the early 1960s before internal CACM trade had grown to its present importance. Total GNP of the region in 1972 was US$6.6 billion, slightly more than the GNP of Puerto Rico and slightly less than that of Peru, which helps explain the difficulties manufacturers sometimes encounter in obtaining adequate economies of scale, even on a regional basis.

Within the Central American Common Market, the country with the largest area is Nicaragua, which is about six times the size of El Salvador, the smallest. Correspondingly, El Salvador, with 190 persons per square kilometer, is the most densely populated, while Nicaragua, with only 18 persons per square kilometer, is the least. In absolute terms, Costa Rica has the smallest population, while Guatemala has the largest (12.1 percent vs. 33.2 percent of the total CACM population).

The economies of Central America also show a wide range of diversity. The highest per capita income in 1973 was $710 in Costa Rica; El Salvador and Honduras were the poorest with $350 and $320 per capita respectively. In terms of total gross national product, Guatemala is the largest with $2,340 million or 35 percent of the regional total, and Honduras is the smallest with $860 million or 13 percent of the total. As of 1973, Guatemala and El Salvador each had roughly 1/3 of intra-CACM exports. These shares represent a major change from 1960 when the shares were 17 percent and 41 percent respectively. Since then Guatemalan exports to CACM have grown very rapidly (29% p.a.); although El Salvador's CACM exports grew by a very respectable 18.7 percent per year from 1960 to 1973, this was not enough to maintain its share. El Salvador, Costa Rica and Nicaragua show roughly equal degrees of industrialization--18-20 percent of GDP is industrial value added; Guatemala lies in the middle with about 16 percent while Honduras trails with 14 percent of GDP coming from this source.

Data related to social equity for the region are scarse and unreliable, but there is nc doubt that the distribution of land is highly skewed, and that with the exception of Costa Rica, income distribution

Table 1

CENTRAL AMERICA: Population, Income and Area

Country	Population 2/			Area		Population Per Km² 1975	Income Per Capita 1/	
	Thousands 1975	Percent 1975	Growth p.a. 1965-72 1/	Km² (ths)	Percent		(US$) 1972	Growth p.a. 1965-72 (Percent)
Central America	16,279	100.0	2.73 3/	411.4	100.0	39.6	460 3/	2.0 3/
Guatemala	5,400	33.2	2.1	108.9	26.5	49.6	500	2.2
El Salvador	4,006	24.6	3.3	21.1	5.1	189.9	350	1.2
Honduras	2,832	17.4	2.9	112.1	27.2	25.3	320	1.7
Nicaragua	2,071	12.7	2.5	118.4	28.8	17.5	540	1.5
Costa Rica	1,970	12.1	2.9	50.9	12.4	38.7	710	4.1

1/ 1974 World Bank Atlas and Economic Analysis and Projections Dept.

2/ IBRD, Economic Analysis and Projections Dept. and Country Economists.

3/ Weighted average.

10/75

follows a similarly uneven pattern. In the rural areas of Nicaragua, for example, the top 5 percent has an average income over 50 times that of the bottom 20 percent and in the urban areas the ratio was 26 to 1. In Chile, for comparison, the overall ratio is only 15 or 20 to 1. Similarly, 50 percent of the land in El Salvador is found in only 1.5 percent of the holdings. Literacy rates vary widely within the region--from over 90 percent in Costa Rica to less than 50 percent in Guatemala.

In summary, while the average per capita incomes in Central America are relatively high compared to many countries, the income is poorly distributed and the absolute size of the national economies is so small by world standards that, even if they were to have a smoothly functioning regional integration scheme, the question of scale requirements of new industry would still arise.

Section 2

HIGHLIGHTS IN THE HISTORY OF CENTRAL AMERICAN INTEGRATION

Central America's identity as a geographical, political and economic unit goes back at least to the Spansih Colonial era. It was governed by Spain as the Captaincy General of Guatemala until 1821, when, in the wake of the revolution against Spain in Mexico, members of the ruling classes in Central America declared the area's independence from Spain. In 1823 the United Provinces of Central America was established, but this early attempt at regional integration broke up in 1840. During the next 100 years, the Central American republics went their separate ways; although there was substantial foreign investment in tropical products and occasional US military intervention between 1909 and 1933, there was little interaction among the countries themselves.

Following the Second World War, however, interest in regional integration revived, fostered in large part by the Economic Commission for Latin America (ECLA). The remainder of this section outlines some of the important events which have shaped Central American integration since the mid 1940s.

1948 The Supreme Council of Central American Universities was established, marking the first concrete step towards Central American integration along non-political lines.

1951-57 Bilateral treaties establishing free trade zones were signed between various Central American countries.

1952 The Economic Cooperation Committee for the Isthmus of Central America (ECC) was established. This Committee operated under the auspices of the ECLA office in Mexico, which was the first of several international agencies which have worked to promote Central American integration; such external assistance was very important in shaping and financing the Common Market organizations which exist today.

1958 The Multilateral Treaty for Free Trade and Economic Integration was signed. This, the first trade treaty signed by all five Central American countries, was designed to establish internal free trade. However, the initial list of freely traded items was small, and though a full customs union was envisaged within ten years, negotiations were painfully slow and fell far short of this goal.

1958 The Convention on a System of Central American Industries was signed which established "Integration Industries." This was designed to give special incentives to factories which, for reasons of economies of scale, would require access to the entire Central American market. Because the negotiations, which must be undertaken separately for each plant, have been very difficult, only three "integration industry" plants have actually been established.[1]

1959 The Central American Convention on the Equalization of Import Tariffs was signed to augment the free internal trade of the 1958 Multilateral Treaty with a common external tariff (CET).

1960 The Tripartite Treaty of Economic Association was signed by Guatemala, El Salvador and Honduras following the failure under the 1958 Multilateral Treaty to establish significant internal free trade. The Tripartite Treaty approached liberalization of intra-regional trade from the opposite direction by immediately putting all but a few goods on an internal free trade basis, rather than by listing only a few and negotiating the rest over time.

1960 The General Treaty on Central American Economic Integration (Treaty of Managua) was signed in December, thereby including, in addition to the signatories of the Tripartite Treaty, Nicaragua and, by 1962, Costa Rica. Agreement on this treaty helped resolve the conflicts which resulted from the exclusion of Nicaragua and Costa Rica from the Tripartite Treaty, and it marked the beginning of effective economic integration in the area.

1960 The Permanent Secretariat for Central American Economic Integration (SIECA) was established to serve as a nucleus of technicians with executive authority to implement the decisions made by the Economic and Executive Councils of the CACM. SIECA has continued to be a vital focus and source of integration efforts in the region. (See Annex A.)

1960 The Central American Bank for Economic Integration (CABEI) was established by the signing of the 1960 Treaty of Managua and came into operation in September 1961 with four member countries; Costa Rica joined in September 1963. It was established to promote economic integration and balanced economic development in Central America. It finances only projects which are "regional" in nature and has been active in the fields of infrastructure, industry, tourism, and housing.

1962 The Convention of Fiscal Incentives for Industrial Development was signed in San Jose, but was not finally ratified until 1969, three years after an ammending agreement was signed which permitted Honduras to grant special fiscal incentives in light of its relatively disadvantaged status. The draft regulations (known as REIFALDI) for the implementation of the fiscal incentives agreement were approved in 1970, but were never implemented in full. Changes are now under discussion. This convention could be of vital importance, for it puts a limit on the incentives which can be offered and on their duration (up to 10 years depending on priority); in the past, fiscal incentives have been designed to foster the competitive position of

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1/ These include Ginsa (tires) in Guatemala, and 2 Nicaraguan plants producing caustic soda and toxaphene (insecticide).

individual countries and have resulted in serious losses of tax revenues to the Central American countries.

1963 The Special System for the Promotion of Productive Activities was established. This system, also known in Spanish as the "etereo" or ethereal system (its provisions, not based on substantial staff work, seemed to be pulled out of thin air), was a response to the general failure to reach agreements on specific "Integration Industry" plants. The etereo system offered various fiscal and tariff incentives to any firm which could provide at least 50 percent of Central American Common Market requirements in its product line.

1968 The San Jose Protocol was signed, imposing a 30 percent surcharge on the common external tariff as an emergency measure to protect the balance of payments of the member countries. This continues to be an important source of revenue to the CACM countries.

1969 Honduras/El Salvador hostilities broke out, aggravating tensions which still pose major problems to the Central American Common Market. The underlying cause seems to have been the pressure on the land in El Salvador which led to substantial movements of Salvadoreans to the relatively empty land in Honduras. The relative industrial underdevelopment of Honduras and the depression in Honduras during this time which made jobs scarce and created antagonism towards the Salvadoreans working in Honduras also contributed to the friction.

1970 Honduras effectively withdrew from the Central American Common Market; it declined to work with the official Economic and Executive Councils (the governing boards of the CACM), to follow the common external tariff, to allow free entry of member country goods, or to allow the passage of Salvadorean goods through its territory. It, nevertheless, recognizes the need for the CACM and has continued to work with it de facto through meetings of government officials (presidents, ministers and vice-ministers), and has established bi-lateral treaties with all CACM members except El Salvador. These treaties contain essentially the same provisions as are in the General Treaty. Very significantly, however, they provide for free entry of Honduran goods to the other countries and duties up to 25 percent on goods entering Honduras (i.e., non-reciprocal preferential treatment).

1971 A Normalizing Commission was established in June consisting of the Presidents and Ministers of Economy from each country except Honduras. The commission was to resolve the conflicts besetting the CACM and to re-establish its normal operations. This effort was followed by the work of the High Level Commission which, though operating at a slightly lower level, includes Honduras and seems to have been much more productive (see below, 1973).

1972 The Secretariat for Central American Economic Integration (SIECA) issued a study titled The Integrated Development of Central America in the Present Decade: Bases and Proposals for Improving and Restructuring the Central American Common Market. This study, covering over 2,000 pages, discusses past developments and future perspectives and presents proposals dealing with trade, tariffs, industrial development, agriculture, physical integration, social development, monetary integration, external commercial policy, integrated development financing, public finance, CACM institutions, and international technical cooperation.

1973 The High Level Committee (CAN--Comité de Alto Nivel) held its first "period of sessions" in Guatemala in October to begin work on consensuses for revitalizing the CACM based on the SIECA proposals of 1972. These sessions have been the recent focus of Central American integration activity during 1974 and 1975. This reflects both the state of suspense into which the official organs of the CACM, such as the Economic Council, have been thrown by the Honduras/El Salvador conflict and, at the same time, the active efforts being made to get the CACM going again. The countries want to recover the momentum which was lost because of the Honduran withdrawal from the CACM free trade arrangements and because of the exhaustion of much of the "easy" industrial import substitution which fueled rapid regional growth during the 1960s. To date there have been about 15 CAN meetings, most of which resulted in consensuses that, it is hoped, will lead to a new treaty for the CACM, one reflecting the important economic changes which have taken place in Central America since the present General Treaty was drafted some 15 years ago.

1974 A study titled "Perspectives for the Development and Integration of Agriculture in Central America" was issued by SIECA and FAO. This study, prepared by the FAO Consulting Group for Central American Economic Integration (GAFICA), provides perhaps the most complete analysis available to date of a sector which has long been neglected in Central America.

1974 The Central American Bank for Economic Integration (CABEI) announced a plan to begin financing agricultural development in Central America. This represented an important addition to CABEI activities, which had previously focused on infrastructure, housing and industry.

1974 In November the five Ministers of Agriculture met for the first time as a group and, in the Charter of San Jose, recommended that they continue working together on Central American agricultural development.

1974 A draft Treaty Creating the Central American Economic and Social Community was issued by SIECA. This document, basically a staff proposal based on the 1972 SIECA study mentioned above is very ambitious, laying out a comprehensive plan for integration not only in traditional economic areas such as external trade and fiscal incentives, but in social areas as well such as employment, social security, and education. It tends to be idealistic and long term (it envisions implementation over a 25 year period). The final results will probably be significantly more modest.

1975 The Ministers of Agriculture, meeting together in April for a third time, outlined a plan of cooperation in Basic Grains, calling for regional self-sufficiency by 1980. They also referred to SIECA the preparation of a comprehensive study on "the Human Factor in Integrated Rural Development," a study of the present status of rural people in Central America and the improvement of rural life.

1975 Fieldwork on the Tripartite Agricultural/Rural Sector Survey was completed in May through the joint efforts of the World Bank, the IDB and AID; the final reports on each of the five countries are expected in six months. This survey, which focuses on the present status of agriculture in each of the countries individually and on potential projects which might be suitable for future financial or technical support from the agencies involved, is expected to be followed in the near future by a regional survey which would emphasize an inter-country approach to rural development.

Section 3

THE IMPACT OF ECONOMIC INTEGRATION

Today the Central American republics enjoy per capita income levels averaging about $460 and moderate rates of industrialization. Ten to fifteen years ago, before the Central American Common Market began, real per capita incomes were only two-thirds to three-fourths of the present levels, as was the share of industry in GNP. Real Central American GNP grew by almost 6 percent per year from 1960 to 1972 and, even with fairly high rates of population growth, per capita incomes increased by about 2.5 percent per year. Manufacturing showed the most rapid growth, expanding by about 8 percent per year, in real terms, while agricultural output trailed at only 4.4 percent per year.

The most striking growth rates are found in the expansion of intra-regional trade. Primary product trade increased four-fold in current terms between 1958 and 1968, while that in manufactured products increased in excess of 17 times, reflecting the strong industrial bias of the Central American integration effort. These growth rates, however, hide a very important fact: partly because of the small initial base, and partly because the easy trade expansion was soon accomplished, the rate of growth during the second half of the 1960s (17 percent p.a.) was significantly slower than that of the first half (35 percent). The very slow rates of growth in CACM trade in the early 1970s were certainly caused in part by the El Salvador/Honduras conflict; however, the trend towards slower growth was already visible in the late 1960s. The growth of total CACM exports, which averaged about 10.0 percent p.a. from 1960 to 1968, was of course much slower than the 30 percent annual growth of intra-CACM trade because of (a) the low base from which the latter began, and (b) the external protection and internal free trade which made the local markets more attractive. In 1960, for example, only 7 percent of CACM exports went to other CACM countries; by 1970 this had risen to 26 percent. Nevertheless, despite the diversion of trade from third country markets to other CACM countries, there was still a significant net expansion of trade; exports to the rest of the world grew by over 6 percent p.a. from 1960 to 1968, and this provided the foreign exchange which was vital to the development of Central American trade and industry. Without this, it would have been difficult to purchase the necessary foreign equipment and material inputs. The Central American countries are fairly open economies, with trade representing up to 35 percent of GNP or more.

All CACM countries have benefitted from the growth of CACM trade, but the present pattern of shares in intra-regional imports and exports is still quite uneven. As is shown by the following Matrix of Intra-CACM Trade (Table 2), in 1972 Guatemala and El Salvador had the largest absolute levels of trade, both in terms of share in total imports and exports (25-35 percent) and in terms of trade among specific countries. Guatemala and El Salvador each exported to the other nearly $50 million of goods, which was substantially greater than the next highest level of bilateral trade--$28 million of exports

Table 2

MATRIX OF INTRA-CACM TRADE - 1972

(in millions of US dollars)

Exporter \ Importer	Guatemala	El Salvador	Honduras	Nicaragua	Costa Rica	Total
Guatemala	--	47.7	9.4	21.0	28.2	106.3
El Salvador	45.8	--	--	16.6	22.8	85.2
Honduras	1.3	--	--	4.0	1.8	7.1
Nicaragua	8.7	13.5	7.8	--	26.6	56.6
Costa Rica	13.1	14.1	5.2	19.2	--	51.6
Total	68.9	75.3	22.4	60.8	79.4	306.8

(in percent of total)

Exporter \ Importer	Guatemala	El Salvador	Honduras	Nicaragua	Costa Rica	Total
Guatemala	--	15.5	3.1	6.8	9.2	34.6
El Salvador	15.0	-	-	5.4	7.4	27.8
Honduras	0.4	-	-	1.3	0.6	2.3
Nicaragua	2.8	4.4	2.5	-	8.7	18.4
Costa Rica	4.3	4.6	1.7	6.3	-	16.9
Total	22.5	24.5	7.3	19.8	25.9	100.0

from Guatemala to Costa Rica. Due to the El Salvador/Honduras conflict, there was of course no official trade registered between these countries, but even with the rest of the CACM countries, Honduras had very little trade--only 7.3 percent of the intra-CACM imports and only 2.3 percent of the exports. This imbalance in shares of trade with respect to Honduras is dealt with in the first section (Regional Balance) of Section 4 below.

A major cause of the expansion of trade within the CACM and of the consequent growth of the Central American economies was the tariff protection which shielded the Central American investors. When the Common External Tariff (CET) was established in 1959, it was set between the average for the region and the highest in the region for individual items, resulting in an increase in the average from 42 percent up to 48 percent by one estimate, and from 35 percent up to 45 percent by another. The highest average CET tariff applies to non-durable consumer goods (106 percent); within this category, clothing and textiles have a 137 percent rate. This structure, of course, creates a strong bias towards the import of capital equipment, leading to capital intensive technologies, restricted employment generation and limited development of intermediate goods industries. The effective protection to domestic value added implicit in the nominal tariffs on consumer goods in particular appears to be very high, but at present we do not have data on actual rates of effective protection in the CACM.

A recent study under the joint auspices of the Brookings Institute and SIECA concludes that the main benefit of the CACM has been the saving of scarce foreign exchange (local currencies are used in intra-regional payments). In addition there were some benefits from trade creation. But perhaps even more important were the economies of scale made possible by the larger common market and the employment generated by the increased industrial activity. The economies of scale have also led to some intra-industry specialization among the countries. El Salvador and Guatemala have reaped the greatest benefits from the CACM. Honduras has benefitted the least, but does not appear to have been hurt in absolute terms although, in relative terms, it has not kept up with its neighbors (this is discussed under "Regional Balance" in Section 4).

Despite the often rather high nominal tariffs, it appears that a large part of Central American industry is reasonably competitive with imports. Domestic goods are often sold at prices less than the c.i.f. price plus tariff of potentially competing imports, and sometimes even at less than the c.i.f. price (e.g., cotton shirts, yarn, wire). In other words, much of the protection is not used fully and serves only to keep foreign producers from taking part of the local market away from domestic producers. Internal competition seems to be sufficient to keep prices down close to world levels for some products, but others are being sold at 50 to 75 percent above the world market prices. Although inefficient production (due partly to suboptimal scale) is certainly responsible for some of this extra cost, excess profits in a protected market where there is little competition in many lines is certainly a major factor. Data on profits are exceedingly weak, but one survey showed pre-tax profits as a percent of fixed assets of at least 30 percent per year.[1/] Some firms reportedly recover their capital in only two years. The rates of protection afforded different products vary widely, creating serious distortions in terms of the relative profitability and investment attractiveness of various goods. These distortions could be alleviated by instituting a more even scheme of nominal tariffs among the various products and by reducing and coordinating the fiscal incentives offered by individual countries.

Although many Central American industries appear to be relatively efficient, fiscal incentives such as exemptions from import taxes on equipment and materials which are purchased at favorable foreign exchange rates, have led to a relatively capital intensive industrial development that has not generated the employment that would have been possible with more labor-intensive products and production techniques. Also, many firms are engaged in finishing, packaging and assembly operations which have very low value added and high import content. Because of the low value added and substantial rates of nominal tariff protection, the effective rate of protection on such products, i.e, the protection offered to value added and thus to domestic production, is often very high. The concessional tariff rates on the imported inputs have tended to reduce the prices of these goods compared to what they would have been if imported complete at the full tariff. The expanded consumption of these import-intensive products within the region may have been a significant factor in the balance of payments problems which periodically plague the CACM.

In summary, the Central American Common Market stimulated a rapid expansion of intra-regional trade and industrial development within the area, but growth is now much slower. The El Salvador/Honduras dispute is part of the problem, but the causes lie deeper in the important changes which have--and have not--taken place in the individual national economies. The entire common market institution needs to be revised to meet today's circumstances. Some major areas of potential change and adaptation are discussed in the following section.

1/ This is close to the after-tax return as well; it is estimated that taxes take only 4-6 percent of industrial profits.

Section 4

INTEGRATION ISSUES

This section lays out eight basic issues facing the Central American Common Market today:

a. Regional Balance
b. Sectoral Balance and Agriculture
c. Industrial Incentives
d. The Selection of New Industries
e. Export Promotion
f. New Treaty for the Central American Economic and Social Community
g. SIECA (Permanent Secretariat)
h. CABEI (Central American Bank for Economic Integration)
i. Infrastructure

a. Regional Balance

There are potentially serious imbalances in the growth of individual countries within the CACM. Some of these were reflected in the country data given in Section 1, which show in particular the relative underdevelopment of Honduras. One important consequence of this imbalance has been the growing trade deficits which Honduras, Nicaragua, and more recently, Costa Rica have been running with the more industrially advanced Guatemala and El Salvador. This trend is perhaps most notable in the case of Honduras, which moved from a healthy positive balance of payments with the rest of the CACM in 1960 to a $22.6 million deficit in 1969 (this was equal to over two-thirds of the international reserves of Honduras in that year). During this same period, the per capita GDP of Honduras fell from 81 percent of the CACM average to 71 percent, and its exports fell from 23 percent to 12 percent of the CACM intra-regional total. It is of course not essential that Honduras have a positive balance of trade with the other Central American countries, or even that it have a neutral balance; it could make up for an intra-CACM deficit with a rest-of-the-world surplus. In some years Honduras has in fact had a positive balance on merchandise account with the rest of the Central American countries but the deficit with the rest of the Central American countries is still a valid concern to the extent that it means that Honduras is buying goods at a higher cost within the CACM than it would have to pay outside and is not, at the same time, able to sell its products at a premium over world markets to other CACM countries.

The trade deficit with the rest of the CACM, coupled with the relatively low level of industrial development in Honduras, have led it to demand special preferential treatment. In fact, it has been said that Honduras does not want equal opportunity; it wants equality, and it wants it as soon as possible. To attain this would of course mean significant sacrifices by the other CACM countries, but there is an outside chance that they may be willing to accomodate Honduras--at least part way--in the expectation that their short term sacrifices for Honduras will be more than compensated for by the more rapid growth which each country will enjoy if the Common Market can be made to function to its full potential. It is important to note that the new draft treaty for a Central American Economic and Social Community makes provision for "special preferences" to Honduras, without specifying what these should be. The shape which these take and their acceptability to Honduras will be important factors in the future success of the CACM.

The border dispute of Honduras with El Salvador must still be resolved, of course, but there is some chance that, if appropriate trade and development concessions are offered to Honduras, the settlement might be facilitated. Some of the measures which have been suggested are (1) preferential treatment of Honduran exports; (2) duties on Honduran imports from the CACM; (3) location of integration industries in Honduras; and (4) preferential fiscal incentives such as provided for in the 1966 amendment to the Fiscal Incentives Agreement. Measures such as these should help Honduras overcome its present state of industrial underdevelopment. This would in turn make it possible for Honduras to produce goods which will be attractive to the other Central American countries--part of the present problem has arisen because Honduras does not have the capacity to supply the exports it would like to sell to others in the CACM group.

b. Sectoral Balance and Agriculture

The CACM since its very origin was oriented to industrial development through import substitution; integrated agricultural development has received little if any serious attention. All important agricultural products were exempted from the general provisions of the 1960 Treaty of Managua and were made subject to multilateral agreements. The only such agreement which has actually been ratified is the Limon Protocol of October 1965. This recommended regional coordination in agricultural policy related to basic grains, but has never been implemented. In effect, trade in agricultural products has continued to be subject to special agreements and import/export controls, most of which have been established on a crop-by-crop basis.

CACM's industry-oriented strategy has been quite successful in generating GDP growth in Central America, but has not generated comparable development in the agricultural sector or improvements in the welfare of the rural poor. As indicated earlier, the agricultural sector in Central America has not stagnated, though it has grown more slowly than average. For the region as a whole from 1960 to 1970, GDP grew by 5.7 percent p.a. in real terms; agriculture during the same period grew by 4.4 percent while industry grew by 8.5 percent. Of this agricultural growth, most was due to the development of export rather than domestic markets. Concern about the agricultural sector has been accentuated in recent years by the need to import basic food products and by the very low average level of income earned by the 60 percent of the Central American people engaged in agriculture.

The Central Americans are now examining ways of reorienting the Common Market so that the agricultural sector may grow more rapidly, thereby improving the standard of living among the rural poor. This immediately raises very fundamental and politically sensitive issues, which is one of the main reasons that, to date, the CACM has focussed on the less sensitive industrial development. While industrial development primarily meant additional wealth for the upper classes, effective agrarian development and regional integration will almost certainly involve taking land away from these favored groups and making it available to the poor. Because of the political implications of agricultural policy, most of the efforts to date have been oriented more to action at the national level, perhaps with some coordination among the countries in terms of approach, than to action on a truly regional basis. Before discussing national level action, though, a few examples of actual and potential regional-level action might be mentioned.

There is almost no concrete example of integrated rational agricultural development to date. The Ministers of Agriculture did announce in April of this year the goal of regional self-sufficiency in Basic Grains by 1980, but so far, little action has taken place, and it is still quite unclear whether or not this is a feasible or desirable goal. Several problems arise:

First, although the declaration indicates that the self-sufficiency is to be on a regional basis, discussions with agriculture authorities indicate that many of the countries plan to pursue this goal on a national basis. Although the geographic conditions in the five nations are similar, an attempt to obtain national self-sufficiency in all basic grains would run the risk of uneconomical production.1/ In El Salvador, where there is a serious constraint on arable land because of the high population density, horticultural products, which use land intensively, would probably be more economically efficient than basic grains, provided the required processing industries were developed and regional marketing was pursued. On the other hand, countries such as Nicaragua and Honduras have substantial unexploited agricultural potential which, if developed, might enable them to become major sources of basic grains for regional consumption. Second, wheat is excluded from the "basic grains" concept, which include only maize, beans, rice and sorgum. The concept of self-sufficiency in basic grains is therefore a misnomer, for wheat is an important regional import. This exclusion may be best, however, as Central America has only limited possibilities for its economical production. Finally, regional self-sufficiency in Central America will always be a precarious proposition because of the periodic droughts until better irrigation systems exist to make the region more drought resistant or until the region can establish buffer stocks to tide it through the drought years.

Another general area of regional action where some progress has been made is in international commodity agreements. Central America concentrated with the International Coffee Agreement for many years. More recently, in March 1974, four banana-producing countries--Costa Rica and Honduras from the CACM plus Colombia and Panama--agreed to implement an export tax ranging from US$0.40 to US$1.00 (equivalent to 1 to 2.5 US cents per pound), effective in

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1/ Some economic efficiency on the regional level might of course be justified on the basis that the consequent diversification of agricultural production would limit the exposure of the region to t[illegible] fluctuations of international markets.

April 1974. Actual tax rates levied as a result of the so-called Panama Agreements range from $0.30 to $1.00. To date, there has been no apparent decline in demand as a result of the above tax measures; though the taxes raise the price of bananas, the absolute retail price increase is small, and bananas continue to be a relatively cheap fruit. The most important problems facing the Union of Banana Exporting Countries (UBEC) are the allocation of total supply among its members and the non-participation of other present or potential banana-producing countries, mainly Ecuador, but also Guatemala and Nicaragua.

Aside from the international commodity agreements and the April 1975 declaration on Basic Grains, whichalso included recommendations for coordinated regional policies on pricing, joint purchases, research, marketing and the like, the only other current regional effort is the study of rural people which SIECA is now undertaking. This study is intended to provide a comprehensive view of rural poverty, agricultural production problems, and means for improving life in this sector. As it should serve as the basis for future agricultural and social policy, it is a very important undertaking; it is not clear that SIECA has sufficient resources to carry it out within the year allotted.

A number of activities have been suggested which would be appropriate focal points for future regional agricultural development: Agricultural research in the area is very weak; the only center of any standing is in Costa Rica. A regional research center, if oriented closely to the needs of the farmers in the region and not to esoteric scientific research, could stimulate and assist the development of agricultural research and experiment stations in the individual countries. Marketing of agricultural products presents many regional problems such as storage, transport systems, buffer stocks, marketing facilities, and even standards for grading. A seed reproduction center to supply improved varieties, which would improve the presently very low yields, would be valuable. Technical training in agricultural practices is also badly needed; agricultural extension services in the countries must be expanded and improved.

Many of the above areas of activity might well be initiated at the national level without waiting for regional agreement. Other possible areas of national action oriented towards the poor and the rural sector would be (a) development of rural infrastructure such as farm-to-market roads and irrigation and drainage works; (b) reduction of the implicit subsidies which currently encourage overly capital-intensive production in the manufacturing and agricultural sectors, and (c) restructuring the land tenure and distribution systems. Some effort has already been made in Honduras on the latter point, as is discussed in the country note.

c. Industrial Incentives

The primary instrument used by Central American governments for promoting industrial investment has been fiscal incentives--exemptions from part or all of the normal taxes on imported capital equipment, imported material inputs, income, and capital stock. (Depending on the product and the priority assigned to the investment, the incentives result in exemptions from 25 percent to 100 percent of the normal tax liability for a period of two to ten years, with somewhat longer periods in Honduras as a special incentive because of its relatively less developed status.)

Two major problems have been created by the fiscal incentives. The first, as was discussed earlier, is the strong bias towards capital and foreign exchange intensive products and production technologies which was created by these incentives. The second, and at least in the short run the most critical problem, has been the serious drain on public revenues created by these incentives. The CACM countries have tried to outbid each other in granting fiscal incentives; in the process, tariff revenues, which generated about 50 percent of government revenues as recently as 1962, fell to 23 percent in 1969 and, over a similar period, fell from 21 percent to 12 percent of import value. Sales and excise taxes have been imposed to make up the revenue losses but the outlook for further increases is limited by political pressures, the already substantial role of these taxes in total central government revenues, and the restrictions imposed by the Common Market on sales and excise taxes which might tend to act as import taxes on goods produced in other CACM countries.

The loss of public revenues through fiscal incentives, accompanied by the absence of meaningful complementary reform in income tax administration, has resulted in levels of central government revenues, averaging 9-11 percent of GDP,1/ which are not sufficient to meet the current expenses of maintaining existing roads and other public infrastructure and to expand investment programs.

The CACM countries have been trying since the early 1960s to eliminate the competitive granting of fiscal incentives, but it was not until 1970 that an agreement was finally signed. In part because of the El Salvador/Honduras conflict, the regulations implementing this agreement still have not come fully into effect. Further steps need to be taken to enforce existing regulations and further to reduce the incentives offered by them as soon as possible. (A number of analysts have concluded that tariff protection on finished products has made local markets sufficiently attractive without these fiscal incentives and that the net effect of these incentives has been to drain the public exchequers and fill the coffers of the private industrialists). SIECA has taken a lead in calling for the elimination of general fiscal incentives, and has proposed to limit them to "basic" industries.2/ Even this causes concern, for as will be noted in the following section on the selection of new industries, the minimum efficient scale for many of the basic industries presently under consideration is substantially larger than the entire Common Market and would result in a further bias towards capital-intensive production.

d. The Selection of New Industries

The easy import substitution strategy has almost reached an end in Central America--there is already extensive production of finished products

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1/ These range from 8 percent in Guatemala to 14 percent in Costa Rica.

2/ Article 122, item (a) of the draft treaty for the Central American Economic and Social Community.

involving simple assembly, packaging and finishing where little value is added. Substantial scope remains in certain areas such as processing domestic agricultural products and raw materials, and these should be pursued, but Central America must now begin looking to the production of intermediate and basic capital goods. Yet it is precisely these categories in which the region has the least a priori comparative advantage. Therefore, particular care must be taken to choose industries in which reasonable efficiency can be obtained.

Within the context of the market and factor endowment conditions which exist in Central America, questions must be raised about a number of the proposals which recently have been made for the backwards integration of Central American industry. For example, SIECA issued in April of 1975 a study entitled Identification of Some Industries Which Could be Included in a System of Regional Industrial Programming. This contains preliminary evaluations of the following projects: pulp and paper, flat glass, iron and steel, fertilizers, ethylene, insecticides, systhetic fibers, carbon black, petroleum refining, aromatic hydrocarbons, methyl and ethyl alcohol, sodium based chemicals, and bleaches. Many of these projects require investments which would equal the total investment outlays of the host country for one or more years. Some would require a plant of a scale for internationally competitive production which could serve the demand of the CACM several times over. (As noted in Section 1, the GDP of all Central American countries combined, which is a rough indicator of the economic size of this market, is less than that of Peru and only slightly more than that of Puerto Rico.) Also, some plants would be based essentially on imported materials (e.g., synthetic fibers). This is particularly critical for the petroleum based industries which have been proposed, especially in light of the recent petroleum price increases, for Central America does not yet have any proven reserves of petroleum or gas of economically exploitable quality. This does not, however, rule out the possibility of energy-intensive plants such as aluminum reduction, for Central America does have substantial hydroelectric potential.

Although Central America may well find, either now or in the relatively near future, that a variety of these intermediate product industries are economically desirable, there is still substantial scope left for improvement of existing industry located in lines of demonstrated comparative advantage--industry which is basically labor using and based on locally available materials, and the expansion of this industry for exports to third country markets. Good prospects exist for precessing domestic foodstuffs and for manufacturing cotton goods, pulp and paper, wood products, shoes, and other leather products based on the region's extensive cattle production. It is distressing to note that imports to the region of shoes, clothing and printed products--all labor-intensive products--actually increased as a percentage of apparent consumption over the past decade.

One serious problem in the selection of new industries seems to be the lack of adequate economic criteria. SIECA, which has taken the lead in proposing new investments in the industrial sector, does not have the staff to handle the economic evalutation of projects, nor does the Central

American Institute for Industrial Technology and Research (ICAITI), which has worked with SIECA on the technical aspects of these proposals. There may, however, be some potential for such analysis in the Central American Bank for Economic Integration (CABEI), though this does not yet seem to have been brought to bear on the proposals. At present SIECA is using an employment generation criterion to justify the proposed projects, arguing that the backward and forward linkage effects of basic and intermediate plants generate much more employment than do, for example, agricultural processing industries. This line of analysis, however, does not take into account several factors: First, the investment cost per job is so high ($25,000 to over $200,000) that, even though the induced employment in other fields is greater, the net cost per job still works out higher than in the more labor intensive industries. Second, the analysis ignores the investment which would be required in the supplying and consuming industries to make jobs available there. Third, the jobs in consuming (downstream) industries could in many cases be based on imported materials. Economic rate of return analysis such as is used in the World Bank needs to be introduced in the evaluation of these investment proposals.

e. Export Promotion

As noted in Section 3 above, growth in exports to countries outside the CACM lagged far behind intra-CACM exports, growing at only one-fourth the pace from 1960 to 1968 (7 percent p.a. versus 30 percent p.a. in current terms). Although the growth of exports to third country markets has exceeded that of intra-CACM trade since the Honduras/El Salvador conflict in 1969 (15 percent versus 11 percent), there is still a strong need to expand outside exports to alleviate the general shortage of the foreign exchange which CACM countries need to purchase goods not produced within the common market. This scarcity has in turn tended to slow the growth of the CACM countries.1/

Although the CACM countries have already taken a number of steps to increase export earnings, these could be expanded and others could be initiated as follows: First, a more active export promotion effort could be made, especially in those products in which the CACM countries are most competitive (the scope is of course limited in certain primary products such as coffee and cotton by world market conditions). Second, new industrial investment could be oriented towards internationally competitive products to increase their availability for export; this export orientation would be particularly valuable in products requiring substantial scale for economic production. Third, a tariff drawback scheme on materials imported for export production could be instituted; however, because of the administrative difficulties of such schemes, an export processing zone approach might be better. A more general approach would be to impose a common external subsidy on manufactured products. This would be a counterpart to the common external tariff, and would easily be justified from an economic point of view as a means of granting an incentive to export production comparable to those granted to import

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1/ This, however, is a question of degree, for exports in current terms grew faster than GDP in Central America from 1969-1973 (15 percent vs. 10.4 percent p.a.).

substituting industries. A necessary complement to these steps would be the reduction of excessive incentives which make domestic markets more attractive than export markets.

f. Treaty Creating the Central American Economic and Social Community

The present Central American Common Market structure has been thrown into some disarray by the effective refusal of Honduras to work within its framework. This disarray is only partial, however, for most of the organizations such as SIECA and CABEI continue functioning normally. Though the situation has certainly improved over the past two or three years in terms of trade within the region compared to the period immediately following the El Salvador/Honduras conflict, the present situation in which Honduras deals individually with the other CACM members (excluding El Salvador) on the basis of bi-lateral treaties has not proven particularly satisfactory. There is a need for a new legal structure to bring the community back together.

In December of 1974, SIECA issued a draft treaty for the creation of a new "Central American Economic and Social Community." The major departure of this draft treaty from the General Treaty of 1960 under which the CACM nominally continues to function is the inclusion of social policies along with economic policies. The draft deals at considerable length with questions such as employment, food and nutrition, education, work, health, housing and social security. These are difficult areas from a political point of view as far as any integrated regional approach is concerned; the draft recognizes this, suggesting that the provisions of the treaty be implemented over a 25 year period.

Although the social questions are likely to be the most difficult, the traditional (economic) questions constitute the bulk of the 295 article document. The High Level Committee (CAN) which has been meeting fairly regularly for the past couple of years, has spent most of its time working out common positions on various major economic issues such as industrial planning, common tariffs, fiscal incentives to industry, physical integration, and the organizational structure of the new common market, is now beginning to work through the draft treaty per se to develop an agreed text.

The draft treaty has already generated substantial discussion outside the CAN as well. Two major questions seems to be the degree to which social integration would be carried and the extent to which decisions affecting the member countries would be delegated to the official organs of a restructured common market. On the social question, despite the fact that the present proposals appear to be more ambitious than are likely to be realized, certain academic and labor groups do not feel that the treaty has gone far enough. On the second point, it appears that certain countries, particularly Guatemala and Nicaragua, as well as the conservative elements in some of the others, are not willing at present to accept the delegation of a national authority to a regional body, to the extent implied by the draft treaty.

There seems to be an increasing pressure to scale down the objectives of the treaty to a document upon which agreement can be reached in the near term, leaving the more difficult issues of complete social integration to a later time. In fact, Guatemala has recently presented an alternative plan which calls for rapid progress on a draft treaty, but one with more "realistic" horizons, at least as far as juridical and political structures are concerned.

g. SIECA--Permanent Secretariat

SIECA is the secretariat of the CACM and is responsible for a major share of the studies and statistical data which are available on the CACM.[1] Its operating funds come almost entirely from contributions of the member governments and from the USAID Regional Office for Central American Programs (ROCAP). Some funds for special projects also come from IDB, UN and other bilateral technical assistance sources. SIECA generates only minimal revenues through the sale of publications.

SIECA has taken a lead in proposing new industries, as is indicated by its publication of the report entitled "Identification of Some Industries Which Could be Included in a System of Regional Industrial Programming." However, as SIECA lacks adequate staff for the preparation and appraisal of projects, this study depended heavily on West German technical assistance. A quick review of the report seems to indicate that SIECA could use further assistance in the economic, as opposed to the financial and technical, appraisal of projects. However, it is possible that such expertise should be developed within CABEI instead. In fact, it would seem quite sensible for CABEI to take a substantially more active promotional role with respect to industrial projects than it has taken in the past. This would leave SIECA free to pursue more general policy matters.

In light of the changing priorities in Central America, the lack within SIECA of adequate staff to deal with agricultural development is also of concern. To date, SIECA's only apparent involvement in agriculture of any significance is the study on the "Condition of Rural Man" which has just recently been undertaken. As noted above, there is some doubt that it has the financial resources and technical skills to carry out this very important and difficult task.

h. CABEI (Bank for Economic Integration)

The Central American Bank for Economic Integration (CABEI), an integration institution and the only financial institution servicing the CACM, has a special role with regard to industrial finance in Central America. Its objectives are to promote "the economic integration and balanced economic development" of its members. Industrial development was one of the main aims of the integration movement, and CABEI's Charter stipulates that it may finance industrial projects only if they are of "regional character" in the sense that they either contribute to intraregional trade or to exports outside the region or both. To interpret the "regional" requirement, CABEI has

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1/ Annex A lists some of the other important Central American organizations.

established the following guidelines: (a) projects must require markets in at least two member countries in order to operate efficiently (and sales in the second CACM country market must be at least 20 percent of the total if there are only two markets), or (b) project inputs must come, to some significant extent (at least 20 percent), from at least one member country different to that in which the project is located, or (c) projects must be sponsored by entrepreneurs from two or more member countries. If projects are to qualify under the extraregional export criteria, they must be able to compete in identified foreign markets, and not less than 50 percent of sales must be outside the CACM. These criteria have proved to be workable and have been applied reasonably consistently.

The "balanced economic development" objective has proved to be more difficult to translate into criteria which CABEI could use in its day-to-day operations, partly due to the difficulty of determining what balanced development is, and partly due to CABEI's need to largely rely on government agencies and private entrepreneurs to originate projects it can finance. CABEI has pursued an equitable distribution of its financing by emphasizing project promotion in the member countries whose industrial sector is least developed. Under this policy Honduras and Nicaragua had received proportionally more financing than other member countries up to June 30, 1975.

The distribution of industrial and tourism investment (the totals for which are shown in Table 3) among the five countries is as follows:

	Percent
Guatemala	18.5
El Salvador	15.9
Honduras	27.4
Nicaragua	23.5
Costa Rica	14.7
	100.0

CABEI's industrial and tourism operations have grown in recent years after some decline due to the suspension of CACM arrangements. This is partly a result of increased lending for tourism, although in the last two years there has been notable growth in lending for manufacturing as well.

Lending for industry and tourism is projected by CABEI to grow rapidly over the next five years and to total about US$175.0 million for this period. In the past few years soft loans from AID and IDB, which accounted for almost 70 percent of CABEI's total borrowing as of June 1973, have been of much less significance. The reduction in support from these two institutions reflects CABEI's growing financial strength and its ability to attract private capital. In the past two years CABEI has borrowed US$24.9 million from private US sources and has concluded an agreement for a US$40.0 million loan from Venezuela to be disbursed over a four-year period.

A possible Bank loan to CABEI to finance its industry and tourism program has been under consideration for several years. It has not been possible to develop an operation, however, because no satisfactory procedure has been found for providing member country guarantees for a Bank loan to CABEI, as required by Article III of the Bank's Articles of Agreement. Originally it was proposed that the five Central American countries provide direct joint and several guarantees to the Bank, but this proved to be unacceptable for a number of reasons, one of the principal ones being CABEI's conviction that other lenders would feel compelled to request similar guarantees. CABEI has previously been able to borrow without guarantees, and it feared that the independence of its operations might be compromised if it had to seek guarantees from its member countries in order to borrow. Although it was emphasized that the Bank's need for a guarantee was motivated strictly by legal requirements, there was some fear that it would reflect on CABEI's creditworthiness.

No solution has yet been found to this problem. The Bank and CABEI are now considering a proposal under which the Bank would lend directly to the countries which would place the loans in a trust fund to be administered by CABEI. Since the loan would not be directly to CABEI, this might eliminate the problem of other lenders insisting on similar guarantees. In the absence of legal requirements similar to those of the Bank, it seems unlikely that any other lender would wish to follow the same procedure simply to obtain a guarantee. Also, we are considering extending the commitment period of the loan to three or four years with half the loan to be released in a second tranche upon the satisfaction of specified conditions. If such a mechanism can be divised, it would reduce the very burdensome need to negotiate follow-up loans with the five governments every two years. CABEI is now attempting to determine whether such a proposal would be acceptable to the Central American countries.

Meanwhile, consideration is being given to other approaches to Bank involvement in the industrial sector in Central America in order to develop proposals for management consideration. In the past, requests for assistance have been received from a number of Central American development finance companies, and Bank support for such institutions might be an appropriate alternative to lending through CABEI. As an initial step, prospective recipient countries and institutions must be identified, and Bank objectives in undertaking such operations defined. With this in mind, a sector review is being carried out in Costa Rica and El Salvador, the countries which seem most likely candidates for initial operations. The review is focusing on an updating of our knowledge of financial and industrial policies and institutions of these countries and of their requirements for industrial finance in order to formulate an initial proposal for Bank lending. A similar exercise is about to be undertaken for Honduras, as part of a Bank economic mission to that country.

Table 3
CENTRAL AMERICAN BANK FOR ECONOMIC INTEGRATION (CABEI)
Industrial and Tourism Loan Approvals FYs 1962-75
(in US$ million)

	FYs 1962-67	FY 1968	FY 1969	FY 1970	FY 1971	FY 1972	FY 1973	FY 1974	FY 1975	TOTAL FYs 1962-75
TOTAL	41.5	4.5	8.9	10.9	18.9	11.9	12.7	25.3	46.8	184.2
Consumer Industries	22.9	1.3	5.7	5.2	10.7	7.6	4.4	7.0	11.4	76.2
Food Products	5.3	-	1.4	1.5	3.5	5.9	1.7	5.6	-	
Textiles	16.4	0.1	3.7	2.9	5.7	1.0	0.8	0.7	-	
Wood products and furniture	-	0.7	0.1	-	1.5	0.6	0.8	0.7	-	
Others	2.5	0.5	0.5	0.8	-	0.1	1.1	-	-	
Intermediate Industries	11.4	1.2	1.9	1.7	0.7	0.1	1.3	3.9	7.2	29.4
Chemicals	4.1	0.7	-	1.7	0.5	0.1	0.6	2.4	-	
Non-metalic minerals	6.0	0.5	1.9	-	-	-	0.6	-	-	
Pulp and paper	0.4	-	-	-	-	-	-	-	-	
Others	0.9	-	-	-	0.2	-	0.1	1.5	-	
Metal-Mechanical Industries	4.5	1.2	1.1	0.1	0.2	0.3	0.5	2.2	5.0	15.1
Metal products	0.5	1.1	-	-	0.1	0.1	0.1	2.2	-	
Machinery (including elect.)	2.6	-	-	-	0.1	-	0.3	-	-	
Transport equipment	0.2	-	-	-	-	0.1	0.1	0.1	-	
Others	2.3	0.1	1.1	0.1	-	0.1	-	-	-	
Mining	-	-	-	-	0.1	0.2	1.3	0.9	-	2.5
Hotels and tourism services	2.1	0.7	0.2	1.2	1.0	1.4	4.5	7.3	18.5	39.7
Transportation	-	-	-	2.0	1.8	-	0.3	0.8	3.5	8.4
Financial Institutions	0.7	-	-	0.7	4.4	2.3	0.4	3.2	1.2	12.9

i. Infrastructure

(1) Power Sector

Regional Integration: Because the national power markets in Central America are relatively small and considerable economies of scale could be achieved in power generation facilities through interconnection, the subject has received much attention. A regional group for Power Interconnection, on which national utilities are represented, has been functioning since 1969. The subregional office of the Economic Commission for Latin America (ECLA) in Mexico City has been very active in promoting interconnection. It has carried out studies since the late sixties of various possibilities for interconnection which have been shown to be economically attractive. To date, however, the only interconnection under construction is that between Honduras and Nicaragua, which was financed by Bank loans 841-HO and 840-NI in 1972 and which is scheduled for completion in 1976.

Since the rise in oil prices has stimulated plans for developing the region's substantial hydroelectric and geothermal resources, the subject of interconnection has become of considerably greater interest to the Central American countries. Interconnection would make hydroelectric projects in particular much more attractive by permitting larger projects to be developed than could be justified on the basis of individual national markets. Construction of the first such project, the 450 MW El Cajón hydroelectric project in Honduras, is expected to begin in 1976. A study to determine the financial and technical basis for sales of surplus power generated by El Cajón to Nicaragua in the 1980s will begin shortly. In addition, Honduras has begun discussing the possible sale of surplus El Cajón power to Guatemala. In other initiatives, Nicaragua and Costa Rica have recently obtained loans from CABEI for a joint study of an interconnection between their systems, and Guatemala and El Salvador are also discussing possible interconnection.

In early 1975 ECLA initiated, with support from CABEI and UNDP and in consultation with the Bank and IDB, a new study which will take into account the effects of the energy crisis and make recommendations on institutions, legal aspects, tariffs and other issues which must be resolved before further interconnections can be implemented. The Bank hopes to use the results of this study (which should be available in mid 1976) as a basis for a broader, long range study of regional power integration opportunities in Central America that would serve as a guide for making sectoral lending decisions. We have suggested that such a study might be financed by the UNDP and executed by the Bank upon completion of the ECLA study.

Central American Power Seminar: As part of its technical assistance to regional utilities, the Public Utilities Projects Department organized a seminar for high level staff from Central American countries, Panama and Ecuador which took place in Washington from September 2 to 6, 1975. Twelve participants came from the five CACM countries. The seminar reviewed various research and policy papers which the Bank has prepared in the energy and power fields over the recent past and discussed topics of particular relevance in the Central American context (interconnection, geothermal energy, rural electrification).

(2) Telecommunications

Regional Integration: The five Central American countries agreed on measures in the late sixties for improving telecommunication services within the region. The Bank was involved in the early stages of preparation and technical discussions but withdrew due to unresolved policy issues. (The Bank suggested a strong central organization but the Central American countries favored a looser structure.) A regional telecommunication commission (COMTELCA) was created in 1968 and made responsible for the planning, procuring, installing and supervising of the operation of the regional microwave network. The total cost of the first stage, around US$14 million, was financed by CABEI.

The network links the capitals of Guatemala, El Salvador, Honduras, Nicaragua and Costa Rica with extension lines to the Mexican border from Guatemala and to the Panamanian border from San Jose. It was put in operation in November 1971. Besides the high quality, broad band microwave link, which allows a maximum of 1040 circuits, a radio channel for TV transmission is also provided. Complementary to the transmission capabilities, each country has set up an automatic international telephone exchange (starting with Costa Rica in December 1973) which allows direct dialing within the region and to USA, Canada and Mexico.

In August 1974, COMTELCA prepared the feasibility study for the second stage expansion of the network between 1975 and 1977, based on a traffic growth forecast, with a cost estimate of some US$32 million. The member countries have discussed the proposal, reduced slightly its scope and submitted their individual applications to CABEI, which will take a decision on financing this expansion by the end of 1975.

USA - Central America Submarine Cable: The high volume of international traffic to and from the region has made it necessary to consider development of a reliable and economic transmission mode to the region. It has been argued that the Panamanian and Nicaraguan earth satellite stations, the Panamanian submarine cable and the Mexican land connection, could not satisfy future requirements, especially for the US-Central American traffic.

A joint venture was therefore proposed with the aim to lay a coaxial cable at a cost of some US$15 million between Florida and Puerto Barrios (Guatemala). The partners for the US half would be ATT, RCA and Western Union and for the Central American half, a multinational entity to be known as Empresa Centro Americana de Telecomunicaciones (EMCATEL). This entity would be owned equally by the Costa Rican, Guatemalan and Salvadorian telecommunications companies. The participation of the remaining two COMTELCA countries, i.e. Honduras and Nicaragua, is not yet clear. Honduras is unhappy about the cablehead location in Guatemala, and Nicaragua opposes the project due to fear of reduction in revenue from its earth satellite station.

Because of the opposition of Honduras and Nicaragua, COMTELCA cannot be put in charge of the project, which would be the optimal solution. The relations between COMTELCA and EMCATEL have yet to be defined.

(3) Highways

The past development of Central America along strictly national lines, with each country having closer links through trade to other regions of the world than to each other, has resulted in a transportation system basically connecting each country's seaports with its major producing and consuming areas. This orientation is gradually changing, however, particularly since the development of the Inter-American Highway following World War II and the 1963 agreement of the five Central American Governments on a plan for constructing a system of regional roads; this has been actively implemented over the past ten years.

Distances between trading areas in Central America are short, giving a strong comparative advantage to road transport over other modes. With the growth and improvement of the regional road network, the share of road transport between the Central American countries increased from 65 percent of total tonnage in 1964 to 94 percent in 1970, and total tonnage in the same period rose from 735,000 to 836,000. The development of the interregional highway system also stimulated the growth of internal markets and interregional trade by connecting the main production and consumption centers and by reducing transport costs between them. The interregional system also provided access to important rural areas along the way and in general facilitated the movement of information and persons throughout the region, a key element to an effective integration.

The interregional highway system defined by the Central American countries in 1963 comprises thirteen highways with a total length of about 5,300 km. Construction of these highways has received substantial support from CABEI and from external agencies, primarily IDB and the U.S. Government (the latter was heavily involved in the construction of the Inter-American Highway, which represents about half of the present interregional highway system). The system, which is now basically complete, lies primarily in the agricultural regions of the Pacific plain and in the central highlands where population densities are generally over 50 km^2. The highway system in the more inhospitable regions of the Atlantic plains is largely undeveloped and lies outside the regional network. It is proposed, however, to add to the interregional system a number of new highways in the Atlantic region, and pre-feasibility studies have been or are being undertaken for most of these highways to determine their economic justification.

Although domestic traffic in most of the countries is rapidly growing, the original regional system was designed for long-term traffic demand and should not require substantial improvements or expansions, except for some sections near large urban areas, which are generally very congested and account for about one-fourth of all vehicle-km. travelled in the region.

Deficient maintenance of the present interregional system is a point of concern. A program for the maintenance and conservation of this highway system was agreed upon in 1971 by the Highway Department of the Central American countries, but its implementation should be accelerated.

Slow and inefficient border crossing procedures at present add substantially to transport costs. The excessive delays, lengthy administrative procedures and inconvenient hours of operation at crossing points result in high transport costs. A relatively small proportion of total vehicular traffic approaching border points actually cross them. The elimination of these problems by an effective Customs Union between the countries in the region could result in a substantial increase in Central American trade, particularly of certain low-value, high-bulk commodities such as cement and grains.

(4) Ports

Because of their geographical location and their agriculturally-based economies, the Central American countries have traditionally been very dependent upon ocean shipping. In 1960, only about seven percent of their trade was intraregional and was carried mostly by truck; the rest was trade with other countries outside the region, almost all by sea.

There are about 30 ports distributed along 4,100 km of Atlantic and Pacific coastlines, handling an estimated total of 12 million tons of cargo in 1973. Six of them (Puerto Cortes, Corinto, Acajutla, Santo Tomas, Limon and Puerto Barrios) are relatively important and handle more than half the traffic. However, they are small by international standards. The number of ports appear to exceed economic efficiency when the region as a whole is considered. Many have been built to serve the interests of private companies, and in most cases their hinterland has been limited to national boundaries. The above-mentioned buildup of the regional highway network means that, with the increased economic integration of the Central American countries, a desirable concentration of port activities should be possible. The Central American Transport Study done in 1964-1965 did recommend a port investment program for the five countries, but the recommendations were not based on a careful study of the interdependence between the ports. In 1967, the Permanent Secretariat for Economic Integration of the Central American Countries (SIECA), in its analysis of the port situation and prospects, recommended a regional approach to port planning in Central America, but did not attempt to derive specific programs.

The first attempt to investigate this issue in a systematic way was the Central American Ports Study, done by the World Bank in 1969-1970. Although the purpose of the study was more to establish and test a methodology than to derive a firm development plan for Central American ports, its conclusions are nevertheless interesting. It was found that the economies of scale expected in the region in the foreseeable future were not such as to make it worthwhile to concentrate development efforts exclusively on a few ports. However, it was also recognized in the study that a change in shipping technology away from traditional break-bulk handling and towards high speed bulk handling and containerization could alter that conclusion. The ports of Corinto in Nicaragua and Puerto Cortes in Honduras currently handle a limited number of containers. It appears the demand for containers will increase, which should result in a few ports handling most of this traffic.

Total port traffic is continuing to grow as a result of the increasing external trade of the Central American countries. Although interregional trade has been growing at a good pace and now accounts for over 20 percent (in dollar terms) of total trade as opposed to only 5-10 percent in the early sixties, the movement of goods by sea between the five Central American countries is following a decreasing trend. The increase in extraregional traffic, which moves mostly by sea and accounts for over 90 percent of the port traffic, has generally been matched, albeit with delays, by limited expansion of the more important ports. Port congestion, often a problem in the past, has been alleviated though not altogether eliminated.

More expansion work is now underway or is being planned for the five years ahead. On the Pacific side, at Corinto in Nicaragua, the second stage of expansion is under way with Bank assistance; the construction of a new port is about to start at Henecan in Honduras, also with Bank assistance; both Guatemala and Costa Rica have plans to build new Pacific ports as an alternative to expanding other existing facilities at San Jose/Champerico and at Puntarenas, which are now operating at capacity. On the Atlantic side, Honduras has recently completed a second expansion of Puerto Cortes with Bank assistance (Loan 767-HO) and is planning to build a new port at Puerto Castilla to serve the development of wood-paper industry in the Olancho region. Nicaragua is also embarking on a port scheme in the Leguna de Perlas area to facilitate ship access along the Escondido River. Costa Rica has begun expanding the port facilities at Limon and is considering a new port at Cieneguita. While all these projects are considered in each country to be consistant with national objectives (and those financed by the Bank have all had a clear rational priority), it is not clear at this stage whether all the existing and planned ports best serve the objectives of overall Central American Integration.

The ongoing US$1.7 million Central American Transport Study should try to answer this question and, possibly, help adjust these plans to better meet the regional integration objectives. (This study is being jointly financed by UNDP, IDB, CABEI and the Central American countries, and the Bank has been following it closely, providing advise at various stages in its preparation and execution.) However, even if the study formulates unambiguous recommendations in this respect, it is not at all certain that regional economic considerations, such as the economies of scale derived from increasingly large port operations, the development of containerization and the minimization of land transport costs, will prevail over national interests.

Annex A

SELECTED CENTRAL AMERICAN ORGANIZATIONS

The following list indicates some of the key organizations in Central American integration. They are listed alphabetically by acronymn or title, depending on common usage. The date of establishment and location of principal office, where available, are listed in parentheses.

CABEI--Central American Bank for Economic Integration (1960--Honduras)

At the outset, CABEI concentrated on infrastructure projects designed to contribute to trade and industrial development. Subsequently it has focused more on industrial projects. It recently announced its intention to finance more agricultural activity.

CAN--High Level Committee (1971--n.a.)1/

This Comité de Alto Nivel, composed of Economic Ministers from the five countries, has filled the basic role of the Economic Council and is working towards restructuring and revitalization of the CACM.

Central American Clearing House (1961--Honduras)

Handles clearance of payments for intra-regional trade in local currencies. Has been very successful, handling around 90 percent of CACM trade payments.

Central American Monetary Stabilization Fund (1969)

Created to coordinate monetary policies of the Central American countries and to help with short-term balance of payments problems, using long-term funds from the United States, West Germany, Venezuela and Mexico.

ECLA--Economic Commission for Latin America (1947--Chile/Mexico)

A United Nations organization which has played an active role in economic integration efforts in Latin America. Known in Spanish as CEPAL (Comisión Económica para América Latina).

Economic Council (1960--n.a.)

Composed of the Ministers of Economic Affairs from each country. This council is the final regional authority on questions of integration policy. Usually meets no more than four times per year; meetings presently suspended due to the Honduras/El Salvador conflict.

1/ n.a. indicates not applicable--the group or organization floats among locations and has no permanent secretariat.

<u>Executive Council</u> (1960--n.a.)

This council, composed of the Deputy Ministers of Economic Affairs from each country, does the preliminary work for the meetings of the Economic Council and, until the recent CACM problems, met frequently.

<u>FECAICA--Central American Federation of Chambers and Association of Industry</u>

Coordinates and serves as a forum for the Chambers of Industry in each country.

<u>FECAMO--Central American Federation of Chambers of Commerce</u>

Coordinates and serves as a forum for the Chambers of Commerce in each country.

<u>ICAP--Central American Institute of Public Administration</u> (1957--Costa Rica)

Provides training to government officials in public administration. Formerly known as ESAPAC (Advanced School of Public Administration).

<u>ICAITI--Central American Institute for Industrial Research and Technology</u> (1955--Guatemala)

Established with UN assistance to undertake scientific research and assistance for Central American industries. In the past ICAITI was more oriented to research than to applied technical assistance to local industry. Recently it has assisted SIECA in the preparation of industrial investment proposals for the region.

<u>INCAE--Central American Institute of Business Administration</u> (1963--Nicaragua)

This institute, established with assistance from Harvard University, runs two-year courses at the graduate level in business administration.

<u>INCAP--Institute of Nutrition for Central America and Panama</u> (1949--Panama)

This institute is perhaps one of the best known outside the Central American region, having gained an international reputation for the quality of its work. Part of its budgetary resources currently come from work done on contract for non-CACM countries.

<u>ODECA--Organization of Central American States</u> (1951--El Salvador)

Established to foster political unity among the Central American nations. Forum for Ministers of Foreign Affairs.

SIECA--Permanent Secretariat of the General Treaty for Central American Economic Integration (1960--Guatemala)

Acts as the secretariat to the CACM. Prepares a wide variety of studies, formerly for the Economic and Executive Councils, and now for the High Level Committee. Prepares statistical volumes and publishes various documents on Central American integration.

2

EL SALVADOR

(a) Development Performance: The most severe problems of the Salvadorean economy are its modest growth rate, its high unemployment (and underemployment) in urban as well as rural areas and its low nutrition levels. Even if the country increases its domestic public savings effort substantially, its financial resources to solve these problems are limited and foreign assistance could play an important role. Few projects are available to deal with the major economic problems of the country for a number of interrelated reasons: The Government has shown little interest in the past in trying to solve the problems of the lower income groups; it has been reluctant to raise additional fiscal resources or increase foreign debt; and it has not been successful in devising projects for solving the country's development problems.

You may wish to approach the issue by inquiring what El Salvador considers to be its most urgent development problems, what measures it intends to take to remedy these problems, what progress it has made in formulating projects, and what role it envisages for the international lending agencies.

(b) Ahuachapan Geothermal Plant: The Bank-financed geothermal plant at Ahuachapan has begun partial operation; however, a canal to carry geothermal effluent to the Pacific is seriously behind schedule. Consequently, the toxic effluent is now being discharged into the Paz River, which has generated some conflicts with Guatemala. CEL, the power company, understands the importance of expeditious completion of the canal and was at one point considering retaining a new contractor to complete construction of the canal in about one year. Recent analysis indicates, however, that the additional cost of accelerating construction might be as much as or greater than that of using thermal power during the interim period; CEL has therefore decided to delay accelerated construction until other alternatives can be fully considered. The main immediate problem is to obtain an agreement from El Salvador, which is also acceptable to Guatemala, on the maximum interim level of pollution in the Paz River from the geothermal plant. Because different opinions exist between CEL and the Bank as to what constitutes a tolerable level of pollution in the river, and in view of Guatemala's concern, the Bank some months ago invited the Pan American Health Organization (PAHO) to determine the actual level of pollution and to recommend safe levels of arsenic and boron content in the river. Both Guatemala and El Salvador have cooperated with PAHO in its consideration of the problem and the PAHO report is now being reviewed. By the time you meet with the Delegations, the Bank's position and those of the countries may be defined. You may wish to request Salvadorean (and Guatemalan) cooperation in reaching a rapid solution to the problem. You might also wish to inform the Salvadorean Delegation that a satisfactory resolution of the pollution problem would be necessary to enable us to go forward with Power VII, proposed as a stand-by project for the current fiscal year.

GUATEMALA

Agriculture and Rural Development Program: The Government is now showing increased attention to rural problems. A key element in its strategy is to provide support for the rural cooperative movement. At the Annual Meeting the Bank was advised that a plan for aiding cooperativesand also presently unorganized elements of the rural poor was in preparation, and Bank assistance would be requested for financing projects emerging from this exercise. FAO/CP assistance has been arranged to review the plan when it is ready (expected to be this November). Of particular importance to the feasibility of a substantial effort in the area of rural development is the improvement of project preparation and execution capacity and improved fiscal effort. You might wish to review the steps Guatemala is taking in these areas, as well as discuss the Guatemalan rural development strategy.

HONDURAS

(a) Agrarian Reform - Honduras is about to embark on a very ambitious agrarian reform program whose goal is to redistribute land to 100,000 families over the next five years. They have already made a substantial beginning towards changing the land tenure structure through distribution of land to about 20,000 families in the past three years. The Government has had difficulties, however, providing any substantial assistance to these families to help increase their productivity because of the lack of trained technicians, inefficient public sector administration, poor coordination between public sector institutions administering assistance programs, and lack of local resources. If the agrarian reform program now beginning is to have any chance of success, these difficulties must be overcome. In addition, care must be taken in the implementation of the agrarian reform not to discourage investment in private commercial agriculture, which is Honduras' principal source of foreign exchange.

You may wish to inquire how they intend to deal with such problems as providing effective technical assistance, credit and other support for land reform settlements, and government policy in regard to the organization of those settlements, which is just now being defined. The Honduran representatives may also be very interested in soliciting your views on these methods and on assistance which the Bank might provide for the agrarian reform effort. (Your Nairobi speech is well known in Honduras - a Spanish translation was distributed throughout the country in 1973 by the agrarian reform agency.) We have included integrated rural development projects in the Lending Program, which would involve assistance for agrarian reform settlements. The projects have not yet been forthcoming, however, because of the country's limited project preparation capability. A Third Livestock agricultural credit project (IDA) is now being appraised which would make longer term investment credit available to agrarian reform settlements.

(b) Public Investment Program - Honduras has adopted a relatively large and ambitious public investment program, and is now in the process of negotiating foreign assistance for its support. The program gives priority to rural development and agrarian reform, the completion of basic infrastructure, and the development of new export products. There is little doubt that these are the correct priorities; the issue is simply the time-frame within which Honduras can afford to implement such a program. Unfortunately, there seems to be little leeway on the question of timing. Two of the largest projects, the El Cajon hydroelectric project and the Pulp and Paper project (which will account for over US$500.0 million of public investment in the next seven years), should be undertaken without delay. El Cajon is the most economic power project available to meet Honduras needs in the 1980s, and the Pulp and Paper project offers the best prospect for rehabilitating Honduras exports in the next decade. You may wish to inquire as to Honduran proposals for financing the local share of the public investment program and as to their views of the impact on the economy of undertaking such a program.

(c) Program Loan - Immediately after the 1974 hurricane, the Bank considered, and discussed with the Government, the possibility of a program loan to help fill the balance of payments and fiscal gap expected as a result of the widespread destruction of bananas, reconstruction investment and the serious deterioration in Honduran terms of trade which became evident in 1974. After initial discussions with the Government, it was learned that Venezuela was prepared to make quick disbursing assistance available to all the Central American countries under an oil facility. This assistance, along with potential IMF support and other extraordinary assistance committed to Honduras, appeared at the time to provide sufficient funds in 1975 and 1976 to enable Honduras to go forward with both hurricane reconstruction and the major elements of its normal development program. The Government was therefore advised that extraordinary financing from the Bank Group seemed unnecessary.

It is likely that the Delegation may raise the possibility of a program loan. As justification they may be expected to refer to their very difficult balance of payments situation. An economic mission has just returned from Honduras, and we are not yet in a position to determine whether a program loan is justified. If, however, this issue is raised, you may wish to repeat what we told the delegation to this year's Annual Meeting, i.e. although Bank lending in Honduras will be relatively low in FY76 (a US$3.0 million supplementary loan for ports and a proposed US$9.0 million third livestock project), a number of large loans are planned for FY77, so on a per capita basis, Bank assistance to Honduras over the next few years will be quite high. Given the current shortage of Bank funds, rationing might be necessary even for the poorer countries, and there is no assurance that the Bank would be able to provide any additional support for Honduras beyond what is already contemplated.

NICARAGUA

(a) External Debt: A matter of growing concern to the Bank, the IMF and other international lending institutions has been the deterioration in the last few years of the terms of Nicaragua's external public debt. Traditionally, Nicaragua has maintained a reasonable and fairly constant level of external debt service (about 10 percent of exports). Recently, especially following the earthquake, recourse to commercial credits has increased sharply. As a result, the share of private bank credits in total external public debt outstanding has gone up from 32 percent in 1970 to over 50 percent at the end of 1973. A further US$120.0 million were borrowed from private banks during 1974. While the debt service ratio was still only 9 percent in 1974, it is expected to be on the order of 14 percent this year. Clearly, the Government will have to curb such borrowing lest the debt servicing burden becomes intolerable. By the mid-1980's the debt service ratio would exceed 40 percent if the share of external financing at commercial terms is maintained. Conversely, the economy could continue to grow at a satisfactory rate if such borrowing were reduced to US$20-$30 million a year, and the debt service ratio could then be maintained below 25 percent by the end of the decade.

We would suggest your raising with the Delegation the need to cut down external borrowing on commercial terms. Even if the debt service ratio were held to 20-25 percent by 1980, this would be very high for Nicaragua. We suggest that you reiterate our concern (mostly recently expressed to the Nicaraguan delegation to the Annual Meeting) and outline the implications such borrowing would be likely to have on the country's creditworthiness and balance of payments prospects.

The Nicaraguans may reply that high levels of commercial borrowing are necessary because of inadequate support by the international lending agencies. You may wish to say that we are considering new operations in education and power for 1976 and hope to develop in 1977 projects for agricultural credit, domestic airports, and water supply. The probability, however, that these projects will materialize will depend very much on adequate project preparation by the Nicaraguan agencies involved. (Project preparations continue to be weak in most of the public sector in spite of substantial technical assistance from a variety of sources.) You may wish to add that it will be important to our consideration of these projects that they be designed in a way that would contribute to a wider distribution of the benefits of economic growth.

(b) Rural Development: The Government is proceeding with the reorganization of the agricultural public sector with AID financial and technical assistance. This program includes the creation of a new institution (INVIERNO) which will supply credit and technical assistance to about 20,000 small producers (about 120,000 persons will be affected) in two selected regions and which will also coordinate public activities in education, health and infrastructure addressed to the same target groups. You may wish to inquire as to the overall progress in this endeavor.

PANAMA

(a) Rural Development: General Torrijos is keenly interested in the problems of developing the rural sector and of the welfare of medium and small farmers, and is aware of the importance given by the Bank to the subject. The Revolutionary Government has sought to drastically change the rural scene in Panama, which up to 1968 was largely composed of large farms owned by urban dwellers and devoted to extensive livestock breeding, slash and burn farming practiced by squatters on land which was not permanently settled, and some farming for cash crops. In bringing about change the new Government was faced with two problems: how to alleviate rural poverty on the one hand and how to maximize the productivity of Panama's scarce land resource on the other. The Government has sought to solve both problems simultaneously by: (a) settling groups of poor farmers on land acquired through expropriation of large estates; (b) organizing small farmers for joint political and economic action and providing such groups with support from public resources; (c) establishing publicly-owned agro-industrial complexes with the intention of eventually turning them over to "campesino" control; (d) giving high priority to social services and infrastructure in rural areas and (e) bringing new land into production, mainly by expanding into the jungle region to the east of Panama city.

From 1969 to 1972 a total of 350,000 hectares of land were expropriated (as against 4,000 hectares from 1962 to 1968) or about 16.5 percent of all land in farms. During the same period 197 "asentamientos" and "juntas", including some 7,600 families, were established with Government assistance. The benefitted families represent about 15 percent of the rural poor. Since 1972 the process of land expropriation and resettlement has slowed down and the Government has concentrated its efforts on solving some of the problems encountered during the early years of operation of farmer organizations. These were that (a) too much emphasis was given to producing traditional crops and not enought to new products (e.g. sorghum, vegetables, chicken, etc); (b) management has not always been good and the best production alternative for each settlement was frequently not chosen and (c) production methods tended to be capital rather than labor intensive, perhaps because abundant credit was made available. The net result, however, has been that land under cultivation has been extended considerably and that the output of staple crops (rice, beans and corn) has been increased. Social services in rural areas have also been extended and improved. The expansion of the education system has been noteworthy and the extension of integrated rural health programs (which include nutrition, potable water and family planning) have shown good results. Panama's rural health services now compare favorably with those of many Latin American nations.

For the future the strategy is to rely on the "frontier" being opened up to the east of Panama City, by the Panamerican highway extension, as the focus of new settlement and increased agricultural production. The Bayano region has already been opened and the Government has ambitious projects for an area of about 225,000 ha., of which 42,000 ha belong to the State and 183,000 ha to private farmers. The Government has asked the Bank to help finance investments in both the state farms, which will be used to expand production of rice, sugar cane and milk and help provide services (water, power, feeder roads, training, etc.) to over 3,000 individual farmers and nine organized groups (including 700 families) in the region. FAO/CP is assisting in the preparation of this project. A small mission to help define the project will visit Panama in November and a larger one would follow in February to help prepare it. The main issue to be explored is the relative importance which would be given to the State farm and privately owned farm components. The Bank's view is that State farms should not only be regarded as a means of increasing production in the short run, but as models for private farmers and as sources of extension services to them, since privately owned farms are likely to be the most efficient producers in the long run.

Extension of the Panamerican highway eastwards towards the Colombian border will continue to open up new areas for settlement in the thickly vegetated, high rainfall Darien region. The cost of constructing this road and maintaining it has proved higher than anticipated, largely because of high rainfall and difficult working conditions. (The United States pays 2/3 of the cost of the road up to asphalt surface standards, but this finish has not proved to be very durable). The OAS is helping prepare a regional development plan for the Darien which will include a resources study. The plan should be ready by mid-1976.

The role of the Private Sector

1 The Revolutionary Government has committed itself to both rapid economic development and a redistribution of income, and since 1972 has taken decided, though sometimes perhaps too hastily conceived, action in pursuit of both goals. In its impatience to "get things going" the Government has undertaken ambitious investment projects in cement and sugar production and is considering others in large scale farming and mining (see the Government's Investment Program, D-d). At the same time it has enacted a Labor Code and introduced rent controls, both of which are considered by the private sector to be ill conceived. It is claimed that the Code reduces discipline and hence productivity by making it almost impossible for an employer to fire an employee. Rent control legislation limits returns on investment (a guideline of 15% is used to set rents) and also gives the Government the right to use unrented and empty properties for social purposes, presumably to house the poor. Though this last provision has never been properly interpreted or applied, it has raised doubts in the private sector about the Government's attitude towards the right of property. As a result of the responsibilities assumed by the State in implementing new projects and of the reaction to the above mentioned legislation, the private sector has been alienated from the development process and remains an anxious onlooker at the sidelines. This is to be regretted as the private sector, with suitable encouragement, might make an important contribution to the financing of new investment, thus relieving the Government's debt service obligations in the future (See Economic Situation D-c). More importantly, because Panama's comparative advantage is likely to continue to lie in its internationally oriented service sector and this is inherently dependent on private initiative, the Government should strive to maintain an atmosphere of confidence for such initiative.

You may wish to find the opportunity to discuss how the private sector might be induced to make a positive contribution towards the development process. The Government could do much to restore investment confidence if it modified its Labor Code to provide income security to employees through an unemployment insurance scheme, instead of through job permanence guarantees as at present. Such a scheme has been proposed to the Government. The investment climate might also be improved if the Government indicated more clearly how it intends to apply the rent control legislation. Finally, you may wish to suggest that the private sector be encouraged to invest in the equity capital of some of the enterprises being created by the Government and that, in the interests of prudent management, the Government should confine its contribution to such enterprises to equity capital, letting them obtain credit on the merits of their business prospects, rather than with Government guarantees.

Topics which may be raised by General Torrijos:

Volume and Terms of Bank Lending

A Management Review of the Lending Program is scheduled for November on the basis of a recent economic mission's findings. In the meantime, Mr. Knapp indicated that pending the forthcoming management review we should assume that annual lending to Panama in the years following FY1976 should not exceed $20 million (in current prices). On this basis it was decided to drop from the Operations Program a $35 million loan for Stage I of the Panama-Colon Highway in FY1977 and a $30 million follow-up loan in FY1979. The Panamanians were informed of these decisions. They have also been told that Bank repayment terms may in future be limited to 15 years since Panama has surpassed the $850 per capita guideline established in the December 11, 1974 "Review of IBRD/IDA Program and Financial Policies."

If queried, you may wish to point out the need to ration scarce long-term resources among member countries to attend to the need of countries with comparatively low per capita incomes. Bank lending in the past has been higher than to other countries in Central America. For 1972-74 Bank lending averaged $12.90 per capita as compared to $11.90 for Costa Rica which, in turn, received the highest level of lending in the CACM. The Bank has expressed its willingness to help Panama obtain complementary resources from banks and suppliers for those projects with which it is associated. With regard to the Panama-Colon Highway, General Torrijos wrote to you on October 21, 1975 (copy attached), requesting that the decision to take the proposed loan off the lending program be reconsidered since his Government gives high priority to the improvement of this vital road which connects the country's two major cities located respectively on the Caribbean and Pacific terminals of the Panama Canal. Given the Panama-Colon Highway's high priority, and the extensive Bank participation in its preparation (the Bank also was executing agency for the recently completed National Transport Survey), we intend to recommend to Management that the project be reinstated in the lending program. You may wish to indicate to General Torrijos that the Bank is considering his request in the context of a review of our overall lending to Panama. Regarding repayment terms, we propose to request Management's approval of terms appropriate to each project, which in certain cases may exceed the 15 year guideline, in view of the urgent need to improve the term structure of Panama's public debt.

Public Utility Rates

General Torrijos may wish to discuss Bank policies on public utility rates. Under terms of the Loan Agreement for the Second and Third Power projects, the Government power company IRHE is obliged to obtain an 8.75% per annum rate of return on its net assets in operation. We have recently agreed to the Government's request that this requirement be waived for 1975 and 1976, since increased fuel costs have forced IRHE to raise effective tariffs sharply in recent months. General Torrijos has nevertheless expressed the view that power rates should not be set on "commercial" considerations and that consumers should be spared sharp increases in power costs. (See

Mr. Fernandes' memo of September 5, 1975 on General Torrijos' meeting of August 17, 1975 with Mr. Lerdau and Mr. Fernandes; G-g).

In response, you may wish to point out that in financing public utilities the Bank's objective is not only to increase supply but also to help build institutions which are financially sound and can therefore serve the public adequately over the long run. Satisfactory returns on investment are required to enable public utilities to undertake investment programs designed to expand services as demand grows and, as in the case of IRHE, to substitute hydroelectric power for thermal as relative costs change. You may wish to add that in the Bank's experience frequent but small rate changes do not cause consumer resistance, while large but delayed increases result in consumer discontent and have a damaging effect on the financial condition of utilities and therefore on the quality of service provided to the public. We expect the issue of tariffs to come up again in the context of a proposed loan for water supply (See E-c Notes on Prospective Operations). Moreover, by enabling public utilities to be largely self-sufficient financially, the need of transfers from Government resources, which are already insufficient to meet investment needs in other areas, would be reduced. Alternatively, Panama would have to borrow even larger amounts abroad, thus adding to its fiscal problems in servicing the public debt.

COSTA RICA

(a) Balance of Payments: As discussed in the draft CPP (item F.2a of the Briefing Book), the major economic problem area in Costa Rica is, and is likely to continue to be, the balance of payments. Following a severe deterioration in the balance of payments during 1974, the authorities took a number of measures designed to restrict import growth and promote exports and resolved to limit commercial foreign borrowing (short- and medium-term) which had become excessive during 1974. The Bank agreed with the Government to conduct a mid-1975 balance of payments review in order to reach a decision whether to go forward with a planned highway loan. The review was conducted and the findings were that the Government has had considerable success in alleviating the immediate balance of payments crisis. You may wish to express our appreciation of the Government's actions so far to resolve the short-term financial problems. At the same time balance of payments stability over the medium and long-term will require continued restraint in import growth and in short and medium-term foreign borrowing as well as successful export promotion and diversification. You may wish to inquire how the authorities intend to strengthen the medium- and long-term balance of payments situation. In particular you may wish to discuss the Government's export promotion and diversification programs and policies.

(b) Level of Bank Lending: The authorities may ask for a higher over-all level of Bank lending to Costa Rica. Specifically, the Costa Ricans may inquire on availability of Bank financing in the following project areas which have not been included in the lending program proposal in the draft CPP.

(i) Line of Credit for Tourism. The Government is determined to expand investment in tourism, thus helping to boost the country's foreign exchange earnings, and the Government asked about the possibility of Bank involvement in tourism at this year's Annual Meeting. While private foreign and local investment in this sector is considerable, the Government feels that more could be done with additional resources and may decide to bring the matter up.

(ii) Project for Improvement of San Jose Slum Area: Aware of the rapidly growing concentration of poor and unemployed in the metropolitan area of San Jose, President Oduber has ordered his assistants to seek foreign aid (primarily from AID) and develop a program of improvements (primarily in infrastructure, such as sanitation, health care, etc.) for the main slum areas of the city. In August of this year one of President Oduber's assistants (Mr. G. Bonilla) contacted the Bank to advise us generally of what the Government was planning and to sound out the possibility of eventual Bank assistance.

With regard to tourism, we are planning a sector survey in March 1976 for Costa Rica as part of a tourism survey of the five Central American countries. With regard to slum improvement, we suggested that Mr. Bonilla contact us again once a project outline is ready. In your reply, you may wish to mention the high per capita lending level to Costa Rica. In February 1974, Management approved a US$125.0 million lending program for FY75-79, or about US$13.0 per capita per annum. We intend to propose a lending program for FY77-81 of US$135.0 million or US$14.2 per capita (not including an enclave aluminum project which is discussed in the draft CPP, and which if included would add up to another US$10 to the per capita lending figure). Under the circumstances, we stated to the delegation to the Annual Meeting that it was unlikely that we would be in a position to add significantly to the lending under consideration for Costa Rica for the next few years. We suggested therefore that a first question that the Government would need to consider was whether it was prepared to give priority to the proposed new activities over other projects in various stages of discussion with the Bank.

(c) During the past year a Bank Agricultural Credit Project was dropped from consideration because of an unresolved issue of the on-lending rate of sub-loans to commercial farmers. In Costa Rica both the level and the structure of interest rates are in many ways unorthodox. Thus, for instance, most interest rates are currently below the rate of inflation which makes credit demand difficult to control. It is possible that the Government may raise the issue of sub-loan interest rates with you, but we have seen no indication that they are prepared to alter their policy of providing subsidized interest rates to commercial agriculture. When the discussions on the credit project broke down, the Central Bank indicated that it might present to us a project for small farmer credit, where we were never far apart on the interest rate issue. You might wish to indicate that we continue to be prepared to look at such a project if presented to us (it has been included in the lending program in the draft CPP).

(d) Whereas Costa Rica's income distribution is one of the most equitable in Latin America, and has improved considerably during the last two decades, the share of income received by the poorest groups has changed little over time, even though their absolute income level substantially exceeds that in other Central American countries. In order to further reduce income inequalities and increase the living standards of the poorest rural families representing about one fourth of the population, a Family Assistance Program was initiated in 1975. The program notably includes rural health, sanitation, housing and education projects, as well as nutrition programs for school-age children. Costa Rica's past efforts and programs to reduce income inequalities have been exemplary and you may wish to discuss the nature of this program with the authorities.

Costa Rica

I Progress in the history of:
A. Improving the lot of the common man - particularly in the rural areas
B. Family distribution of diet - nutri, health, soc. services

F. 2a COSTA RICA

(i) Country Program Paper

Attached is the draft Country Program Paper as prepared for the RVP review which took place on October 22, 1975. The review with Mr. McNamara is scheduled for November 12, 1975. Subsequent to the preparation of the attached draft, it was learned that the Costa Rican Government has begun considering a possible reshaping of the aluminum project (discussed in Paragraphs 22-23 and 41-45 of the attached CPP). They intend to assess the feasibility of a hydroelectric complex with about 200 MW of firm capacity which would serve a much smaller aluminum smelter than previously contemplated. The total cost of the hydroelectric-aluminum complex on this basis would be reduced from US$1.5 billion to roughly US$600.0 million. If the smaller project proves feasible, we would propose a reduction in the amount of Bank lending from the US$100.0 million recommended in the attached CPP.

II What is outlook for pop growth - status, organ. & approach of fam. plng prog.

III Outlook for BOP

IV Possibilities of expanding use of underutilized resource base:
cultivatable land
underutilized forests
mineral resources
Tourism
indus. exports to CA & world

CONFIDENTIAL
RVP Draft
October 14, 1975

COUNTRY PROGRAM PAPER

COSTA RICA

1973 Population: 1.9 million
1973 GNP per capita: $710 1/
Current Population Growth Rate: 2.6 percent per annum

Current Exchange Rate: US$1 = Colones 8.60

IBRD Lending Program 2/, 3/ (in current US$ millions)

	FY69-73	FY74-78	FY77-81
IBRD	75.6	100.0	135.0
No.	8	7	8

IBRD Operations Program 3/

$Total	135.0
No. of Operations	8
No./million pop.	4.2

IBRD Aluminum Enclave Program (FY78-81)

$Total	100.0
No. of Operations	2

Average Annual Per Capita Lending 4/

	FY69-73	FY74-78	FY77-81
IBRD w/o aluminum enclave program	7.9(7.9)	14.1(9.6)	14.2(8.0)
IBRD w/aluminum enclave program	7.9(7.9)	21.9(14.3)	24.7(14.1)

1/ Calculated according to World Bank Atlas methodology.
2/ The FY75-79 lending program compares with the program for the same period approved in February 1974 (excluding the aluminum enclave program) as follows:

	FY75-79 Lending Program Approved	Proposed	Percentage Change (Proposed/Approved)
No. of Loans	7	7	-
Current $ millions	125	170	+36.0%
Constant FY74 $ millions	80.7	107.4	+33.3%
Per capita p.a. (Const. FY74$)	8.5	11.3	+32.9%

3/ These figures exclude the aluminum enclave program.
4/ Numbers in parentheses indicate constant 1974 values using the commitment deflator (see Attachment I).

Introduction

1. The last full CPP review of Costa Rica was held in February 1973, when it was concluded that the prospects for resolving the short-term financial problems which Costa Rica was then experiencing were reasonably good and were not expected, therefore, to interfere with the economy's long-term growth. On this basis, the FY74-78 lending program was increased to $100.0 million (as compared to the $75.6 million program in FY69-73).

2. An Updated Lending Program Memorandum was submitted in February 1974 in lieu of a regular CPP--partly because it was then too early to estimate the impact of the oil crisis and partly because a new administration was to take office in May 1974. In view of improvements noted in fiscal and balance of payments management during 1973 and based on the financial requirements of the 1974-78 National Development Plan, the Region proposed and Management approved a $125.0 million lending program for FY75-79 (excluding the enclave aluminum program), subject to continued satisfactory economic performance by the Government.1/

A. COUNTRY OBJECTIVES

Background

3. Costa Rica's long-term development performance has been impressive, achieving a sound balance between high income growth and social development. Between 1965 and 1974 real output grew at an average of 6.3 percent per year. An official family planning program and rising income and educational levels contributed to a gradual decline in the population growth rate from about 4 percent per year in the 1950's to 2.6 percent at present.2/ Consequently, per capita income grew in real terms by 3.4 percent per year during 1965-74 and reached US$710 in 1973.3/ At the same time, the already fairly even distribution of income improved further, so that currently the profile of income distribution in Costa Rica is among the most equitable in Latin America and does not differ much from that of many developed countries. The absence of a standing army permitted substantial public sector resources to be devoted to improving the physical and human infrastructure of the country, e.g. the electric power system is the most developed in Central America; the adult literacy rate is 90 percent and the national mortality rate is one of the lowest in the Hemisphere. The considerable welfare gains, combined with a culturally and ethnically homogeneous population, help explain the country's history of democracy and political stability.

4. This satisfactory long-term development record, however, has been accompanied by recurring financial difficulties. The economy remains heavily dependent on the export of a few agricultural commodities, mainly, coffee and bananas. Therefore, fluctuations in (1) world markets and (2) weather conditions could be expected to influence the level of domestic activity strongly. Yet,

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1/ In March 1975 it was decided by Management that the FY75-77 lending program should be held to the US$80 million shown for that period in the Updated Lending Program Memorandum of February 1974.

2/ See Table 1.

3/ World Bank Atlas.

Table 1

MACRO-ECONOMIC INDICATORS - 1970-73 and 1980

	Unit	1970	1971	1972	1973	Bank Projection 1980 Absolute	Bank Projection 1980 Growth Rate 1/ (%)
At 1973 Prices and Exchange Rates							
GNP	$ mn	1,085	1,153	1,237	1,390.	2,032.0	5.6
Population	000	1,729	1,623	1,708	1,872.	2,240.0	2.6
GNP per capita	$	627	710	724	743.	907.0	2.9
Gross investment	$ mn	283	362	364	339.	461.0	4.5
Gross domestic savings	$ mn	..	224	216	257.	411.0	6.9
Exports of goods and n.f.s.	$ mn	310	330	381	422.	697.0	7.4
Imports of goods and n.f.s.	$ mn	398	427	446	504.	716.0	5.1
At Current Prices							
Net official capital inflow	$ mn	2	21	28	45.	133.0	16.7
Debt service ratio	Percent	9.7	10.1	10.1	10.2	14.0	-
Exports of goods and n.f.s.	$ mn	285	284	339	422	1,346.0	18.0
Imports of goods and n.f.s.	$ mn	350	389	415	504	1,447.0	16.3

1/ Average annual growth rate 1973-80.

economic growth has been sustained: during periods of cyclical downswings in exports, expansionary fiscal and monetary policies have largely offset deflationary effects on output, consumption and employment, but have led import growth to exceed that of the country's import capacity, thus resulting in serious balance of payments difficulties. Domestic price increases, have, at least until recently, generally been moderate, because in this small open economy demand pressures have mainly been reflected in import growth.

5. During the late sixties, rapid export growth, especially of bananas and coffee, allowed the country to achieve both high output growth and balance of payments equilibrium. By contrast in 1971, export shortfalls led to a severe deterioration in the economic situation. In order to stimulate the economy, credit to both the public and private sectors was increased dramatically resulting in a serious balance of payments crisis: the resource gap rose to 10.4 percent of GDP. At the same time, public savings had fallen to 2.4 percent of GDP and the public sector deficit was close to 4 percent of GDP. Subsequently, a recovery of exports in 1972-73 and a major tax reform approved in 1972 brought about a substantial improvement in Costa Rica's external and internal finances.

6. Whereas the public financial situation continued to improve during 1974, an unprecedented deterioration in the balance of payments occurred. As a result of continued improvements in tax administration and of the introduction of additional tax measures together with current expenditure control, public savings increased to 4.8 percent of GDP in 1974. Public investment remained at about 7 percent of GDP,1/ and the public deficit was reduced to about 2 percent of GDP. Exports expanded by 26 percent, both through volume and price increases, while imports grew about twice as fast. The major factors underlying the rapid import growth included a sharp rise in import prices, an expansionary credit policy and an inventory build-up. Import prices, led by oil, are estimated to have risen by 30 percent during 1974 versus an estimated 15 percent growth in export prices. The attempt to maintain a rising level of aggregate demand in spite of the loss of income from adverse terms of trade was possible only through substantial foreign borrowing, a large part of it on commercial terms, and through reserve losses. In 1974, the resource gap reached 14 percent of GDP and the current account deficit reached US$270 million or 16 percent of GDP. By December 31, 1974, net international reserves were estimated at about US$15.0 million (not including a US$22.7 million drawing from the IMF oil facility) or less than ten days imports. At the same time, domestic inflation rose from 4 percent per year (1965-72 average) to 17 percent in 1973 and 30 percent in 1974.

7. In response to these pressures, during late 1974 and early 1975, a number of measures were taken by the authorities designed to stem the growth of imports and encourage exports. Restrictions on installment credit for consumer durables were introduced, and consumption and sales taxes were increased. Higher support prices for basic grains were established to encourage import substitution.

1/ Tables 2 and 3.

Table 2: PUBLIC CAPITAL EXPENDITURE BY SECTOR, 1971-80

(In millions of current colones)

	Actual				Projections					
	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
Agriculture	11	12	10	12	13	15	17	19	22	25
Power	82	109	117	182	230	511	643	644	650	650
Transportation	127	202	195	306	340	400	416	426	406	450
Communications	42	54	41	100	251	279	194	230	238	295
Water	15	25	32	47	86	67	116	132	170	210
Education	25	26	40	55	95	40	80	84	109	132
Health	40	49	70	60	60	60	95	100	110	145
Housing	46	36	36	61	65	65	75	111	155	200
Other 1/	114	85	179	165	150	150	180	195	205	235
Total Capital Expenditure	502	598	720	988	1,290	1,587	1,816	1,941	2,065	2,342
Total as a percent of GDP	7.0	7.3	7.2	7.3	7.5	8.0	8.0	7.5	7.0	7.0

1/ Includes extra-budgetary, expenditures not identified by sector, and transfers to the private sector.

Source: 1971-74: Ministry of Finance.
1975-80: Planning Office and Bank projections.

Table 3: FINANCING OF PUBLIC INVESTMENT

(In millions of US$)

	Actual				Projected					
	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
Public Capital Expenditure	72	85	103	124	150	185	211	226	240	272
Public Savings	24	33	45	80	60	58	92	105	120	136
Capital Revenues	7	8	5	7	7	7	8	8	8	9
External Financing, net	31	36	39	46	83	102	90	93	100	100
(Disbursements)	(46)	(55)	(63)	(70)	(118)	(141)	(143)	(155)	(172)	(184)
(Amortization)	(15)	(19)	(24)	(24)	(35)	(39)	(53)	(62)	(72)	(84)
Internal Financing	10	8	14	-9 a/	-	18	21	20	12	27
Memorandum Items										
Public Capital Expenditure in mn. of colones	502	598	720	988	1,290	1,587	1,816	1,941	2,065	2,342
Exchange Rate Conversion	7.0	7.0	7.0	8.0	8.6	8.6	8.6	8.6	8.6	8.6

Source: 1971-74 Ministry of Finance and Bank estimates for external financing.
1975-80 Bank projections.

a/ The net repayment of debt to private sector was largely due to more favorable interest rates abroad. This flow was reversed by increased interest rates in mid-1974 on public securities.

Export taxes were restructured because of price changes in world markets. Also, since January 15, 1975, the Central Bank has required the registration of all import orders exceeding US$300 in order to anticipate developments in the trade balance so as to be in a better position to take additional corrective measures, if necessary.

8. The growth of imports slowed down noticeably during the first few months of 1975, and there are several reasons to expect a continuation of this trend. First, imports during January-February 1975 -- before the full impact of the restrictive measures was felt -- were 37 percent ahead of the corresponding two months in 1974; during March-May 1975, imports were only about 10 percent larger than during the same period a year ago. Second, a recent survey of manufacturing industries' inventories of imported goods showed that inventories remained high during the first half of 1975. Third, import orders as of July 15, 1975, indicate a further decline in import growth. And finally, the basic grains program initiated early this year is expected to be quite successful so that imports of corn and beans should be much reduced and a substantial export surplus of rice is likely to develop. If present trends continue, imports during the whole of 1975 should be about equal to the 1974 level in current terms and decline in real terms. Although reduction in consumption and import growth has slowed tax receipts, the Government has already indicated its willingness to take further tax measures (e.g. imposition of additional taxes on coffee exports) if needed to maintain adequate public revenues.

9. Largely because of low coffee prices, export earnings were only about 5 percent larger during the first five months of 1975 than in the same period a year ago. The recent increase in coffee prices is not expected to help Costa Rica's earnings significantly during 1975 as all of this year's crop has already been sold, except for about 10-20 percent which was part of a retention scheme to be financed by Venezuela. On the basis of the above trends, Costa Rica's trade deficit (merchandise only) during 1975 may be reduced to US$223.0 million from US$277.0 million in 1974; similarly, the current account deficit may be reduced from US$270.0 million to US$210.0 million.

10. The reduction in imports is not expected to have a substantial effect on output growth during 1975 because of the existence of large inventories: real output is expected to grow at about 6 percent. The rate of inflation, though less than in 1974, remains above 20 percent and is a source of concern to the authorities. The high rate of domestic credit expansion during the first few months of 1975, which occurred largely because credit for export and basic grains production is not subject to the ceilings set in the monetary program, also has come under their review.

Medium- and Long-Term Prospects

11. Whereas Costa Rica's foreign exchange earnings will be boosted during 1976-77 because of higher coffee prices, over the medium and long-term the balance of payments is likely to continue to be the main problem area. The world market outlook for the traditional export commodities is modest. On the other hand, the country has a substantial resource base which can help reduce the dependence on a few primary exports. Much of the potentially cultivable land could be more fully exploited; there are vast undeveloped forests, though these will require substantial efforts to develop; exploration of mineral deposits is underway; foreign exchange earnings from tourism can be increased substantially; and industrial products exports to both the Central American

Common Market and the rest of the world can be increased. The development of new export lines is a gradual process, however, and even assuming successful export promotion policies, Costa Rica's total export earnings are not expected to grow as fast, at least during 1975-80, as they had during the past few years. Real output growth is expected to average 6 percent per year during 1976-80, or slightly less than in the recent past. The maintenance of balance of payments equilibrium during the next few years will probably require that 1975 imports not exceed those of 1974 in current terms and that, thereafter, import growth in real terms does not exceed GDP growth. This implies a restraint in consumtion and imports, especially of luxury consumer goods, and selective import substitution. Under these assumptions, the public debt service ratio, presently at 10 percent, would rise to 14 percent, a high but temporarily tolerable burden.1/2/

12. The solution of the country's structural balance of payments problem is a major element of the Government's development objectives as outlined in the 1974-78 Development Plan and restated by the First Vice President in January 1975. These objectives include: (1) expansion and diversification of production, with emphasis on exports; (2) further improvements in the distribution of income; (3) opening up of new regions; and (4) greater efficiency of the public sector both in terms of resource mobilization and policy-making.

13. The realization of these objectives will require substantial assistance from the international lending agencies, both to support a continued high level of public investment and in the form of credit lines for productive activities. The Government will have to maintain its public savings effort and follow more cautious credit policies than in the past. Public investment will continue to be dominated by physical and social infrastructure projects. During 1971-74, about 55 percent of public capital expenditures was for the transport, power and telecommunications sectors, while another 25 percent went into the education, housing, health and water supply sectors. Total public investment for the next few years is expected to remain at about 7.5 percent of GDP, with power, transport and communications expected to absorb about two-thirds of the total. Investments in power and telecommuni-

1/ If the current account deficit during 1975 exceeds our present estimate by, e.g., US$30.0 million and if this deficit were to be financed through commercial bank borrowing, all other conditions remaining the same, the estimated public debt service ratio in 1980 would increase from 14 to 15.6 percent.

2/ All of our projections exclude the impact of the possible aluminum enclave project, as both the timing of the project and the nature of the project arrangements have still not been defined fully. (See paras. 22-23 and 41-45). The project has been under study for a number of years and about US$2.0 million has been spent so far on technical and economic feasibility studies. Under the most optimistic assumptions, construction of the hydroelectric plant could begin in 1978, construction of the smelter in 1980, and production for exports could start in 1982. The main effects during the construction phase (which would fall in our projection period) would be to raise the level of GDP and gross domestic investment above our projections, while the net balance of payments effect is likely to be positive because the project would be largely foreign-financed, from private as as well as public sources.

cations, in addition to meeting the growing demands of industry and commerce in the more developed areas of the country, are expected to provide greater access to these services in rural areas and integrate them more fully into the rest of the economy. The main emphasis of the transport program will be on completing the basic network of trunk highways and on the construction of feeder roads which will contribute to spatial integration of the economy and open up new areas for production. The remainder of the public investment program is composed largely of further investments in housing, water and sewerage, health and education.

14. Public support for the development of agriculture, industry and tourism is expected to be mainly in the form of credit lines. Emphasis will be placed on projects or activities which earn or save foreign exchange. A major drive towards export promotion has been initiated. Exports on non-traditional products to non-CACM countries are being promoted through a tax rebate scheme equivalent to 15 percent of the f.o.b. value; marketing outlets are being established in several countries in the Caribbean; an export development fund is to be created in the near future and preferential interest rates are granted to production for export; also, a substantial expansion of hotel facilities is taking place to promote the tourism industry. The Government plans to continue its efforts to reduce consumption and the importation of luxury consumer goods through tax policies. Finally, in order to further reduce income inequalities and improve the welfare levels of the poorest rural families, a Family Assistance program was initiated in 1975. The program notably includes rural health, sanitation, housing and education projects, as well as nutrition programs for school-age children. It is being financed through a 3 percentage point increase in the sales tax rate and a 2 percent payroll tax which is to be increased by 1 percentage point per year up to a rate of 5 percent.

B. EXTERNAL ASSISTANCE

15. In order to sustain a 6 percent real growth rate in the 1976-80 period while at the same time increasing its net international reserves to more manageable levels, Costa Rica will require a net official capital inflow of some US$650.0 million. In addition to disbursements under current loans from official lending agencies, this assumes new commitments of approximately US$800.0 million from those agencies and bilateral sources plus about US$450.0 million in private funds (mostly from suppliers' credits and commercial banks). Power and transport sectors will require the largest amounts of external resources -- up to US$250.0 million and US$150.0 million, respectively.1/

1/ These figures exclude the aluminum enclave project. If the project is undertaken, substantial additional funds will be required by the power sector for hydroelectric generation to supply the smelter (paragraph 41).

16. Among the major lenders other than IBRD, IDB is contemplating new loans in agriculture (credit, irrigation, animal health); industrial credit; electric power (generation and rural electrification); education (university and vocational); water supply and sewerage; and rural health. CABEI is considering projects for highways, power, telecommunications, industry, tourism and housing. USAID, which is planning gradually to phase out of Costa Rica, is considering continued assistance in food and nutrition, population planning and health. The new Venezuelan oil facility would provide Costa Rica with about US$65.0 million, on 25-year terms, during the next six years for local cost financing of on-going and future projects supported by the major lenders. The Governments of Costa Rica and Venezuela recently reached an agreement regarding the principal uses of the oil facility funds. (These will include local cost financing of the Bank-financed Fifth Power Project and the proposed Fourth Highway project.) Previous commitments by the major lenders are summarized in the following table:

Table 4: Summary of Lending by Major Agencies (in US$ million)

	IBRD	IDA	AID	IDB	CABEI 1/
TOTAL 1950-1974	149.0	4.5	82.5	143.6	138.6
Lending 1950-1965	47.7	4.5	33.8	34.6	4.5
Lending 1966-1974	101.3		48.7	109.0	134.1
Transport	17.1		7.1	23.5	62.0
Power and Telecommunications	66.0		--	54.3	11.0
Education	6.2		--	8.2	3.6
Health	--		1.6	--	--
Housing	--		--	--	28.0
Agriculture	12.0		29.3	8.9	5.7
Industry	--		5.0	5.5	13.9
Others	--		5.7	8.6	9.9

1/ As of June 30, 1974.

17. The external public debt repayable in foreign currency (excluding undisbursed commitments) amounted to US$324.9 million at the end of 1974. The terms of Costa Rica's external public and publicly guaranteed debt have been slowly hardening in the last few years due to increasing public borrowing from private sources, which now represents 38 percent of external public debt (excluding undisbursed) as opposed to 28 percent at the end of 1970. Thus the average rate on new commitments increased from 5.5 percent in 1970 to 8.7 percent in 1974, while the average maturity decreased from 27.1 years to 14 years during the same period. The IBRD share of external public debt outstanding and disbursed was 27 percent at the end of 1970 and 23.1 percent at the end of 1974. The corresponding shares of IBRD in external public debt service were 14.9 percent and 14.8 percent. Although IDB has made loans totalling the equivalent of US$144.0 million, most of this amount is repayable in local currency so that IDB's share of the public debt outstanding and disbursed and repayable in foreign currency was 1.5 percent at the end of 1974; CABEI accounts for 6.9 percent of the total, and the U.S. Government for 20.1 percent.

C. BANK STRATEGY

18. Consistent with Government public investment priorities, the thrust of the Bank's past lending has been to help develop basic infrastructure, such as power, telecommunications and highways, which so far have received about 85 percent of total Bank lending. We have also supported efforts to increase and diversify exports through lending for agricultural credit and have helped make educational programs more consistent with manpower objectives through a loan for secondary and vocational education.

19. We plan to continue to support the main thrust of the Government's public investment program. While this means that our lending from FY76 through FY81 will be heavily weighted towards the traditional sectors (power and transport) there are a number of reasons why we believe it inadvisable to propose any substantial restructuring of the sectoral composition of our lending. In the first place, Costa Rica's impressive longer-term development performance, characterized by a rare combination of fast growth and a steadily improving pattern of income distribution, suggests that we should go slow in questioning the Government's investment priorities. Secondly, we have been able to play a constructive role in the Government's formulation of macro-economic policies, particularly in recent months when ceilings developed with the Bank on import growth and external commercial borrowing for 1975 have become key elements of Government policy; to continue an effective dialogue at the macro-economic level, we need to support the Government's basic investment priorities. Third, our long-standing substantial involvement in the traditional sectors give us a special ability to foster institutional development in these sectors. Fourth, IDB and CABEI are expected to continue substantial lending programs in Costa Rica, and particularly IDB is expected to support important sectors, e.g., agriculture and rural development, in which Bank participation would be limited; moreover, some of the Government's most important social development programs (e.g., the Family Assistance Program) will be largely financed internally. Finally, per capita lending limitations will in any event restrict our flexibility to move into new sectors.

20. The lending program proposed for FY77-FY81 is US$135.0 million (excluding the aluminum enclave project discussed in paragraph 22 below) as compared to US$125.0 million approved for FY75-FY79. For the FY75-FY77 period, the proposed program would represent a US$10.0 million increase over the US$80.0 million approved in March 1975. The lending of US$135.0 million for FY77-FY81 would result in real lending (expressed in constant FY74 dollars) of US$76.1 million, which would not even maintain the real level of lending of US$80.7 million which was approved for FY75-FY79. It is expected that with the proposed Bank lending, IBRD's FY77-FY78 share of new commitments by the major lenders will be about 20 percent while IDB's will reach 30 percent and CABEI's 25 percent. Annual lending per capita for FY77-81 would be US$14.2 in nominal and US$8.0 in real 1974 terms (excluding the enclave aluminum project). If the proposed lending program is approved, in 1981 the IBRD share of public debt will be 18 percent, compared to 27 percent in 1974, and its share of debt service will fall to 13 percent compared to 15 percent in 1974.

21. The proposed lending program would be subject to satisfactory economic management, particularly of the balance of payments. As discussed in paragraphs 8 and 9 above, the Government has had considerable success this year in restricting import growth, and the prospects are good that the Government will meet the targets established in the Aide Memoire prepared by the Bank last April, i.e., that in 1975 the deficit on merchandise account (trade balance) will not exceed US$250.0 million, and short- and medium-term foreign borrowing (loans of seven years or less) by the public sector will not exceed US$80.0 million. On this basis we intend to propose that we go ahead now with the loan for Highways IV (Memorandum to Loan Committee requesting authority to invite negotiations is in preparation). The next loans are not likely to go forward until the second half of FY77, and we will have full opportunity to further review the economic situation prior to that time. The next economic mission is scheduled for May 1976.

21a. With an expected low rate of project slippage, we have eliminated two projects which had been in the FY75-79 program: a Rural Water Supply project (FSO funds are likely to be requested from IDB for this purpose) and Education II (bilateral and FSO funds may be available). New projects are proposed for Industrial Credit (in FY78 and again in FY81),for regional development in Limon Province, and for feeder roads. The Industrial Credit Project, however, represents a shift in the lending channel rather than our entry into a new sector. Because of our inability so far to solve the problem of member country guarantees, we have been unable to go forward with the planned lending to the Central American Bank for industry in Central America and have begun exploring possibilities of lending to financial institutions in individual Central American countries.

22. We propose to continue treating the aluminum enclave project separately from our regular lending program for Costa Rica because we plan to obtain special security arrangements adequate to assure that the Bank, in making loans for the project, would not need to rely to any significant extent on the creditworthiness of Costa Rica. (These security arrangements are described in paragraphs 44-45 below.) The project consists principally of an aluminum smelter capable of producing 300,000 tons of aluminum annually and a large (800 MW) hydroelectric plant to supply the required power. The major purposes of our involvement in the project would be (i) to help assure that Costa Rica obtains an adequate share of the benefits of the project and (ii) to help mobilize the external financing required for the project. Given current costs estimates, we are proposing an increase in Bank lending for the project from the US$60.0 million proposed in the 1974 Updated Lending Program Memorandum to US$100.0 million.

This latter figure would represent roughly 7 percent of total project costs, which we consider the minimum necessary to achieve the above objectives. If, for purposes of determining per capita lending, the aluminum project were added to our regular lending program, the total for FY77-81 would represent US$24.7 per capita per annum (US$14.1 in real terms).

23. The Bank has been associated with this project since 1972 when former President Figueres requested Bank assistance in its preparation and financing. Since then we have provided advice to the Costa Rican parties on various aspects and at various stages of the development of the project. The most notable result probably has been the Costa Ricans' hiring a consulting firm to study the technical and economic feasibility of the over-all power-aluminum complex. The Bank assisted in its selection and in preparation of its terms of reference. There has been, however, a noticeable cooling in the attitude of ALCOA, the foreign sponsor, in the project in the past few months (para. 42). Consequently, our projection that a Bank loan would be needed for the hydroelectric component in FY78 may be optimistic. We nevertheless believe that we should maintain the proposed lending for the project in our lending program. The aluminum project potentially will provide Costa Rica with a major new source of foreign exchange earnings. At the same time the project is of such magnitude for an economy the size of Costa Rica that special care needs to be exercised by the Costa Ricans in the preparation of benefit and cost estimates and in the negotiation of the project. All of these factors, when coupled with the receptivity so far shown by the Costa Ricans to Bank advice, warrant our continued close association with this Project, and our ability to play an effective advisory role undoubtedly would be greatly diminished if we withdrew the prospect of Bank financial support.

Status of On-going Operations

24. As of June 30, 1975, a total of US$83.6 million remained to be disbursed on eight loans. The largest portion of undisbursed funds consists of a US$41.0 million loan for power (signed in June 1975) which has not yet become effective. About US$0.3 million remains to be disbursed on a 1972 power loan which is almost complete, with negligible cost overruns. About US$23.0 million represents the undisbursed portion of a US$23.5 million loan for telecommunications approved in June 1974. The project is progressing satisfactorily, with about US$10.0 million of the loan already committed, although disbursements are lagging somewhat behind schedule. An earlier telecommunications project, approved in 1972, is proceeding satisfactorily, with less than 20 percent of the total US$17.5 million remaining undisbursed. A 1970 highways project has been practically completed, and only about 20 percent of the US$15.7 million loan remains undisbursed. Likewise, a US$1.4 million project for highway studies, approved in 1973, has been largely completed; however, the disbursements are behind schedule. In 1972 the Bank made a US$9.0 million loan for a Second Agricultural Credit project. The sub-loan commitments have been proceeding on schedule but disbursements have been lagging (36 percent behind schedule). Efforts are being made to have full disbursement of the proceeds by the original closing date. Lending for livestock and agro-industries has surpassed appraisal estimates while lending for crops and fruits and vegetables failed to meet expectations. The only on-going project which has suffered serious delays is the US$6.2

million education project approved in 1973. This project is about 18 months behind schedule, and practically no funds have been disbursed. The delays are attributable mainly to late appointment of the project director and slow formation of the project unit, problems which primarily because of a change in the Minister of Education which followed the change in Government in 1974. The project is receiving intensive supervision by the Projects Department, and this is reflected in slightly improved Project Unit performance. However, the rate of project implementation is likely to remain slow for some time to come.

International Finance Corporation

25. IFC has made one investment in Costa Rica (US$0.6 million in 1966 to Productos de Concreto, S.A.) which has been fully repaid. At present, IFC is actively exploring a number of new investment possibilities in Costa Rica.

D. ECONOMIC SECTORS AND SECTORAL DISTRIBUTION OF BANK OPERATIONS

Electric Power

26. The most important sector, in terms of lending amount, would be electric power. The US$50.0 million we are proposing for Power VI would represent over 35 percent of the lending total for FY77-81.

27. Since 1961 the Bank has provided major financial assistance to Costa Rican power development through five loans to the Instituto Costarricense de Electricidad (ICE) totalling US$80.8 million. The Bank loans have helped provide about 200 MW of the country's total installed capacity of 360 MW. As a result of ICE's development program, the percentage of the total population served by the electric power system rose from about 50 percent in 1960 to 60 percent in 1970 and 70 percent in 1975, so that now about 95 percent of the urban and 55 percent of the rural population have access to electricity. Partially as a result of encouragement by the Bank, ICE has recently completed Costa Rica's first national rural electrification plan which is designed to increase the portion of the rural population with access to electricity to about 65 percent by 1980. (It expects to request IDB FSO financing for implementation of the plan.)

28. Through its lending, the Bank has also stimulated improvements in sector regulation and in ICE's management. Also, as a part of the Bank-financed Power V project, an effort was made to promote interconnection of the Costa Rican and Nicaragua power systems by allowing for a possible substitution of a thermal plant (which would serve as the ICE system's reserve capacity) for an interconnection line with Nicaragua. However, the progress in negotiations has been insufficient for interconnection to materialize in time to avoid the necessity of going ahead with the thermal plant. We would continue exploring the possibilities for regional interconnection during preparation of the

Power VI project. Probably the most significant of the improvements fostered by the Bank in its power lending has been the strengthening of the financial position of ICE. Prior to negotiations of the US$41.0 million Fifth Power Loan, the Government authorized a series of increases in electric power tariffs (over 80 percent between April 1974 and May 1975); subsequently, it also agreed to annual revaluation of ICE's assets. These improvements were necessary to enable ICE to embark upon its ambitious 1975-78 expansion program, currently estimated to cost about US$220.0 million, and for which, in addition to the Bank loan, IDB has made a loan of US$50.5 million, CABEI is expected to lend US$13.0 million, and the Government will contribute US$24.0 million from counterpart resources generated under the Venezuelan oil facility; ICE would finance the balance from its own funds.

29. The largest item in the 1975-78 expansion program is the 135 MW Arenal hydro development, which, when completed, will enable the system to cover demand until the early 1980's. It will also eliminate the need for thermal generation (except for peak loads), thus helping to save up to US$5.0 million per annum in imported fuel. The next step after Arenal would be the first stage (156 MW) of the Santa Rosa hydro development, downstream from Arenal, which is to be put into service in the early 1980's, and the cost of which is presently estimated at roughly US$150.0 million. The Santa Rosa project would comprise the major component of the proposed Power VI loan. The main sectoral objectives of our proposed continuation of substantial involvement in the power sector are further to support the strengthening of the management and finances of ICE, to help the Government and ICE to mobilize the substantial external resources required for ICE's expansion program and to continue efforts begun under the Power V loan to foster interconnection between the electric power systems of Costa Rica and Nicaragua.

Transport

30. Development of an adequate transport system has been one of the Government's highest priorities during the past decade and has absorbed about 25 percent of total public direct investment in this period. Highways have been the dominant mode (the length of the all-weather highway system has doubled between 1963 and 1973), absorbing most of the investment, including three Bank loans and an IDA credit totalling US$28.1 million. In addition to financing highway reconstruction, Bank lending has been directed towards providing the capital city of San Jose, the country's economic center, with an all-weather link to Limon, the country's principal port. The first part of the link, from Siquirres to Limon, has been practically completed. The second part, a US$65.0 million road from San Jose to Siquirres, for which the Bank financed feasibility and engineering studies, would be financed by a proposed US$39.0 million loan which is planned for Board presentation this year. This road, which would complete the link to Limon, while opening

new areas of considerable agricultural potential, would be the largest item in the 1975-79 national highway expansion program. The latter includes about 1,300 km. of roads to be constructed or improved, at an estimated total expenditure of up to US$250.0 million equivalent. We are proposing also, for the end of the program period (FY81), a project for feeder road construction to help complement the substantial investment being made by the Bank and other external agencies (particularly CABEI) in main highway construction.

31. The Bank has long been concerned about the lack of overall transport sector planning and intermodal coordination, particularly as regards ports and railways. In 1970-71 an effort was made to develop a project for the port of Limon and, at the same time, through creation of a National Port Authority, to help upgrade port and railways planning and their coordination with other modes. However, the Government, which at that time had relatively limited control over the autonomous Pacific and Atlantic port and railways authorities (which, influenced by local interests, were also fiercely competitive with one another), was unable to provide assurances that a proposed National Port Authority would be established and negotiations were discontinued in 1971. In view of the fact that financing from other sources has been obtained for the main Costa Rican ports, we do not envisage any Bank involvement in the port sub-sector at this time.

32. The issue of overall sector planning was brought up again in 1974-75 in connection with the proposed highways project. This time, the Government succeeded in taking a major step toward improving overall sector planning and coordination by establishing within the Ministry of Transport a Transport Sector Planning Office (TSPO) which would be responsible for all transport modes and would also serve as a link between the transport sector and the National Planning Office. (Technical assistance for TSPO would be provided as a part of the forthcoming Bank loan.)

33. Transport in the metropolitan area of San Jose has been a cause of serious concern to the Government. The rapid growth of automotive traffic is already causing congestion in the city of San Jose, and the projections for the future indicate further deterioration. To deal with the problem, the Government obtained a UNDP grant for a study of urban transport, and the Bank has been serving as the executing agency. The study, which is now almost completed, indicates that better traffic control and regulation (including re-routing of the transit traffic) as well as regulation and special provisions for public transportation (e.g., bus-priority lanes) are the priorities which require immediate attention. We are therefore proposing an urban transport project for FY77. (Further studies as well as detailed planning and engineering required for this project would be provided as a part of the proposed Highways IV project.)

Agriculture and Rural Development

34. Agriculture is the most important sector of the Costa Rican economy, accounting for some 40 percent of employment, 75 percent of export earnings and 20 percent of GDP. On average, physical output grew over 7 percent per annum during the last decade. Growth of production and exports of bananas, sugar and livestock has been especially buoyant; more recently agro-industries have also become important. In order to help diversify and increase agricultural production and exports, the Bank has so far made two loans for agricultural credit.

35. The main elements of the Government's current agricultural strategy include: (i) growth and diversification of production and exports along with an increase of employment opportunities in the rural sector; (ii) self-sufficiency in basic grains (which Costa Rica increasingly has been importing); (iii) economic advancement of the small farmer; (iv) promotion of co-operatives and expansion of colonization schemes; (v) integration of different regions into one general development plan; and (vi) integration of Costa Rican agriculture into the Central American Common Market. The Government, which must still determine an appropriate balance among these sometimes conflicting objectives, is pursuing them primarily by providing low interest credit, regulating some of the prices (such as basic grains and fertilizers) and by providing technical assistance. In addition, it has in recent years increased its support to the National Institute for Cooperatives (INFOCOOP) and, in particular, to the Land and Settlement Institute (ITCO), which has been increasingly successful in the promotion of colonization schemes. Finally, the Government has actively sought to obtain external resources, both official and private, for investment in agriculture.

36. In 1974, we were requested to lend for a third agricultural credit project, designed to help increase and diversify exports, assist the Government's program to increase production of basic grains and, for the first time, to make investment credit available to the small farmer. However, because the Bank's position on interest rates to be charged on sub-loans to commercial operators could not be reconciled with that of the Government, the latter requested that further consideration of this project be postponed. We are expecting the Government to submit a revised request that will include only small farmers (where we were never far apart on the sub-loan interest rate), and a US$5.0 million loan for this purpose is proposed for FY78. Given the importance of export growth, however, we would continue to explore the prospects for resolving the interest rate issue with a view to making another loan for agricultural credit in FY80. Our planned activity in the

sector would be coordinated with that of the other external agencies active in the field (mainly IDB and AID) and would be shaped to take into account the recommendations, due before the end of the year, of the tripartite IBRD/IDB/AID sector survey mission which visited Costa Rica in May 1975.

Regional Development

37. The Government has become increasingly concerned over the lagging economic development of some of the provinces. Presently its attention is focused on Limon Province (stretching along the Atlantic coast of Costa Rica), which is the most underdeveloped part of the country. To deal with the problem on a systematic basis, and with the help of an AID loan, the Government first undertook an inventory of the Province's natural resources. The inventory, completed by a Cornell University team, shows that the area has good potential for agricultural, forestry and, possibly, fisheries development. Project identification work is now being organized by the Government and is likely to be oriented towards integrated rural development with some agro-industrial elements to relieve the high unemployment in the area. In view of the time considered necessary for project preparation, we are proposing for FY79 a regional development project, with emphasis on both export promotion and income distribution.

Industrial Finance

38. Like all of Central America, Costa Rica's economic progress has traditionally depended on the fortunes of a few export crops on the world market. The development of the Central American Common Market (CACM) provided a substantial impetus to the growth of non-traditional exports, but these are still comparatively small and limited mostly to CACM itself. Export diversification remains of key importance. The limited size of the Common Market means that Costa Rica will have to rely increasingly on markets outside Central America for the growth of non-traditional exports. As a part of our effort to find an alternative to lending through CABEI for industry and tourism development, we are proposing a DFC operation for Costa Rica in FY78 (to be processed as a standby for FY77), through which we would hope to make a contribution to export growth and diversification. The possible channels for the DFC operation as well as the policy framework within which the operation should be developed, are being explored in conjunction with an industrial sector survey, which is scheduled to be completed by end 1975. Given the apparently substantial levels of protection on industrial production at present, it will of course be particularly important that the normal DFC tests of economic performance be applied to sub-loans. One industry that may well show good economic rates of return and foreign exchange earnings is tourism, which could be financed through DFC channels.

Telecommunications

39. In the early 1960's the Government decided that a telecommunications network should be developed as one of the key elements in the integration of the national economy. Since 1963, ICE has received four Bank loans for telecommunications development, totalling US$57.0 million. The last loan ($23.5 million) was approved in June 1974, to support the first half (1974-77) of ICE's program for expansion of the National Telecommunications System through 1980. The entire 1974-77 program is currently estimated to cost in excess of US$60.0 million; in addition to the Bank funds, CABEI and suppliers' financing will be used for its implementation. At the end of 1973 Costa Rica had a density of 2.16 telephones per 100 population, the highest in Central America, but the demand for service considerably exceeds ICE's present capability to provide it. By 1980 the telephone density would be double the present level.

40. One notable feature of the last two Bank operations was the provision of funds for the development of a rural telephone/telegraph system, through which over 600 locations isolated until now will be included in the National Telecommunications System by 1977. In view of substantial improvements so far in the technical standards of operation and the strong financial position of ICE's telecommunications section, our view, which coincides with that of the Government, is that lower priority should be given to further lending for telecommunications than to proposed activities in other sectors. We are, therefore, proposing as a reserve project fo FY78 a telecommunications operation which would be directed primarily at further sector consolidation and extension of service to isolated areas of the country.

Aluminum Enclave Program

41. As part of our efforts to assist the expansion and diversification of Costa Rican exports, we are proposing loans for the (800 MW) electric power and (300,000 tons per annum) smelter components of a large scale aluminum project. According to mid-1975 cost estimates (in current dollars, including contingencies), the entire complex is estimated to cost in excess of US$1,500 million.[1/]

42. Our proposed lending for this project was included in the 1973 CPP and the 1974 Updated Lending Program Memorandum. Since the 1974 review, a number of important developments have taken place. The technical feasibility of the power component (the Boruca hydro project) has been established. The National Aluminum Commission (CNA) has been established to provide policy guidance in project preparation. CNA, on the basis of terms of reference prepared in consultation with the Bank, hired a consulting firm to study the technical and

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	US$ Millions
Boruca hydro-electric project	$600
Aluminum smelter	870
Infrastructure (port and highway)	60
	$1,530

economic feasibility of the entire power - aluminum complex. The study was completed in May 1975 and later submitted to the Bank for review. While full review of the study has not yet been completed, some preliminary analysis done by the staff appears to support the consultant's conclusion that the project would yield a satisfactory rate of return. By June 1975, the Aluminum Company of America (ALCOA) was supposed to have made an offer to CNA on the basis of which negotiations could start. However, by that time ALCOA stated that it was unable to make an offer or to accept a deadline to do so, stating its inability to raise sufficient capital for a project of this magnitude as a reason for delay and indicating further that, because of the relatively low quality of the Costa Rican bauxite, the project should be based on imported aluminum oxide. (The main advantage of the Costa Rican location for the smelter is not the bauxite but the hydroelectric resource, with additional advantages being proximity to the U.S. market and a favorable investment climate in Costa Rica.) At the same time, ALCOA requested, and CNA granted, permission to seek partners that could participate in financing of the smelter. It is not at this time clear that ALCOA is interested in participating in this project in the near future, and the CNA may soon begin looking for other investors. While the project thus may be delayed substantially, for the reasons discussed in paragraph 23 above, we believe we should continue to stand ready to consider participation in the financing of the project.

43. With regard to the smelter component, IFC has had various discussions with the Costa Rican parties and has explained its potential role, not only in facilitating eventual participation by Costa Rican investors in the equity of the smelter enterprise, but also in mobilizing loan funds for the project. We agree with IFC's view that the smelter component should first be considered by IFC and only in the event that IFC were unable to provide the necessary financing should it be considered by IBRD. Nevertheless, the capital structure and financing requirements of the aluminum enterprise have yet to be defined, and before that is done, it will not be possible to reach definitive conclusions as to the scope of the potential role for IFC or the need for Bank financing. In the meantime, we believe that we should leave open the possibility of our participating in the financing of the aluminum plant. The aluminum plant is expected to represent over one half of the cost of the project, and is the key to the success of the entire operation. The viability of the power plant and the earnings which Costa Rica will receive from the project as a whole will be dependent on the sale of the metal produced in the aluminum plant. The Costa Ricans will need to negotiate the terms and conditions for financing both the power and the aluminum plants essentially as a single package. If IFC were unable to participate, we would be in a much stronger position to accomplish our major objective of helping Costa Rica obtain an adequate share of the benefits of the project if we stood ready to participate in the financing of both the power and aluminum plants. We are therefore requesting approval to program loans of US$75.0 million in FY78 for the power component and US$25.0 million in FY81 for the smelter component.

44. As in previous years, the power and smelter loans are treated as part of an "enclave" program, and, therefore, not as part of the regular lending program for Costa Rica because of the following security arrangements which we would propose in order to assure that the Bank, in making loans for the project, would not need to rely to any significant extent on the creditworthiness of Costa Rica: While there may be changes in the project structure, it has been assumed so far that the hydroelectric project would be developed and operated by ICE, which would sell power to a smelting enterprise owned largely by ALCOA (or other foreign investors or groups of investors). On this basis, and as previously discussed (February 1974) with Industrial and Legal Departments, the Bank would require: (1) arrangements, guaranteed by the foreign investors, between the smelting enterprise and ICE assuring the minimum payments to ICE necessary to service all loans obtained for construction of the hydroelectric complex, whether or not the smelting enterprise uses power; (ii)a guarantee from the foreign investors for all loans for the construction of the smelting plant or other arrangements between the foreign investors and the smelting enterprise or the lenders to assure the availability of funds to service all loans obtained for the construction of an aluminum smelting plant, irrespective of the amount of aluminum produced or sold; and (iii) a commitment of the foreign investors to assume responsibility for all necessary cost overrun financing for the hydroelectric project and the aluminum smelting plant.

45. Ideally, the above guarantees would be unqualified, but they are not likely to be negotiable without some provision for them to lapse on the occurrence of so-called "political risks." In common with arrangements on other similar projects which have been accepted by the Bank, these events of force majeure would include (1) the physical impossibility of constructing or operating the aluminum smelter because of war, revolution or insurrection in Costa Rica or because of deliberate acts of the Government and (2) expropriation of the foreign investors' interest in the smelter. Counterpart assurances would be obtained from the Government that it would not take any action which would relieve the foreign investors of their obligations under the arrangements securing the loans. The above security arrangements are those considered necessary to assure repayment of any Bank loans for the project. They do not deal with those additional arrangements that might be necessary to assure that Costa Rica receives an adequate share of the benefits from the project. This latter issue would be assessed after the feasibility study for the entire project is reviewed and after a more definite timetable for negotiations between CNA and ALCOA or other investors is established.

E. CONCLUSIONS AND RECOMMENDATIONS

46. Costa Rica in recent years has achieved high per capita income growth while avoiding concnetration of development benefits in the upper income groups. Fiscal performance has improved substantially in the last

two years, through a combination of major new revenue measures and improvements in tax administration; and project preparation capability in general continues to be better than in any of the other Central American countries. The major area bearing closest watching is, and is likely to continue to be, the balance of payments, which deteriorated sharply in 1974 in large measure because of the recent rise in import prices but partly also because of monetary expansion. With the aid of new measures taken early this year, the Government has had considerable success in restricting import growth in recent months and the prospects are good that the Government will meet the targets established in the Aide Memoire of April 11, 1975, i.e., that in 1975 the shortfall on merchandise account will not exceed US$250.0 million and short- and medium-term foreign borrowing (loans of seven years or less) will not exceed US$80.0 million. These developments represent an encouraging indication that the Costa Ricans will be able to overcome the immediate balance of payments difficulties; they will be aided in this effort by the prospect of a substantial increase in export earnings in 1976 because of higher coffee prices. Over the longer term, the expansion and diversification of exports will be the key to economic growth and balance of payments stability.

47. Given the Government's progressive and equitable development program and the need for substantial external assistance on terms similar to those offered by the Bank, we propose a lending program (excluding the enclave aluminum project) of US$135.0 million (8 projects) for FY77-81. This would represent a US$10.0 million increase over the five-year lending total approved last year (Updated Lending Program Memorandum of February 1974). For the FY75-77 period, it would represent a US$10.0 million increase over the US$80.0 million approved by Mr. Knapp in response to Mr. Krieger's memorandum of March 3, 1975. Real lending for FY77-81 would be US$76.3 million in prices of 1974, which would be less than the real lending level of US$80.0 million approved for FY75-79. Annual lending per capita (excluding the enclave aluminum project) would be US$14.2 in nominal terms and US$8.0 in real terms. The proposed lending program, however, would be subject to satisfactory balance of payments management. We intend to propose that we go ahead now with the loan for Highways IV (Memorandum to Loan Committee requesting authority to invite negotiations is in preparation). The next loans are not likely to go forward until the second half of FY77, and we will have full opportunity to further review the economic situation prior to that time. (The next economic mission is scheduled for May 1976).

48. As far as the sectoral composition of our lending is concerned, we are proposing to continue supporting the main thrust of the Government's public investment program. While this means a Bank lending program heavily weighted towards power and transport, the Bank will need to be prepared to support the Government's investment priorities if we are to be able to maintain an effective dialogue at the macroeconomic level. Moreover, (i) our long-standing institutional involvement in the traditional sectors gives us a special ability to foster institutional development in these areas; (ii) IDB and CABEI are expected to continue substantial lending programs in Costa Rica, and particularly IDB is expected to support important sectors, e.g., agriculture and rural development, where Bank participation would be relatively limited; (iii) some of the Government's most important social development programs will be largely internally financed; and (iv) per capita lending limitations will in any event

limit our flexibility to move into new sectors. While our contribution in terms of lending amounts will be relatively modest in most of the less traditional sectors, we plan to continue lending for agriculture with a view to supporting improvements in institutional capacity to reach small farmers (Small Farm Credit) and to assisting in the development of an integrated approach to regional development (Limon Regional Development). We would also support expansion of exports by lending for commercial agriculture (Agricultural Credit IV). As part of our effort to find an alternative to lending through CABEI, we are proposing two DFC operations which would hopefully have as principal objectives assistance in export growth and diversification.

49. We propose to continue treating the aluminum enclave project separately from our regular lending program for Costa Rica because we plan to obtain special security arrangements adequate to assure that the Bank, in making loans for the project, would not need to rely to any significant extent on the creditworthiness of Costa Rica. The major purposes of our involvement in the project would be (i) to help assure that Costa Rica obtains an adequate share of the benefits of the project and (ii) to help mobilize the external financing required for the project. Given current costs estimates, we are proposing an increase in Bank lending for the project from the US$60.0 million proposed in the 1974 Updated Lending Program Memorandum to US$100.0 million. This latter figure would represent roughly 7 percent of total project costs, which we consider the minimum necessary to achieve the above objectives. If, for purposes of determining per capita lending, the aluminum project were added to our regular lending program, the total for FY77-81 would represent US$24.7 per capita per annum (US$14.1 in real terms). While there has been a noticeable cooling in the attitude of ALCOA, the foreign sponsor, in the project in the past few months, we believe that we should maintain the proposed lending for the project in our lending program. The aluminum project potentially will provide Costa Rica with a major new source of foreign exchange earnings. At the same time the project is of such magnitude for an economy the size of Costa Rica that special care needs to be exercised by the Costa Ricans in the preparation of benefit and cost estimates and in the negotiation of the project. All of these factors, when coupled with the receptivity so far shown by the Costa Ricans to Bank advice, warrant our continued close association with this project, and our ability to play an effective advisory role undoubtedly would be greatly diminished if we withdrew the prospect of Bank financial support.

SELECTED ECONOMIC DEVELOPMENT DATA

	Actual				Projections			Growth Rates			Percent of GDY		
	1971	1972	1973	1974	1975	1976	1980	1971-73	1973-74	1974-80	Av. 71-73	1974	Av. 78-80
National Accounts (1973 Prices US$ Mln.)													
GDP	1,235	1,344	1,427	1,491	1,584	1,678	2,120	7.5	4.5	6.0	101.0	103.5	101.5
Gains from Terms of Trade	-20	-20	-	-50	-44	-39	-31	-	-	-	-1.0	-3.5	-1.5
GDY	1,215	1,324	1,427	1,441	1,540	1,639	2,089	8.4	1.0	6.4	100.0	100.0	100.0
Imports (incl. n.f.s.)	411	453	504	593	546	571	715	10.7	17.7	3.2	34.5	41.2	34.3
Exports (imp. capacity)	321	378	422	411	435	471	665	14.7	-2.6	8.3	28.3	28.5	31.3
Consumption	991	1,108	1,170	1,258	1,305	1,381	1,678	8.7	7.5	4.9	82.4	87.3	81.0
Investment	314	291	339	365	346	358	461	3.9	7.7	4.0	23.8	25.3	22.0
Domestic Savings	224	216	257	183	235	258	411	7.1	-28.8	14.4	17.6	12.7	19.0
National Savings	216	186	227	154	197	211	330	2.5	-32.2	13.5	15.9	10.7	15.3
Price Indices													
Domestic Price Index	80	85	100	131	157	171	229	11.8	31.0	9.8			
Export Price Index	85	89	100	116	129	141	193	8.5	16.0	8.9			
Import Price Index	90	94	100	130	142	153	202	5.4	30.0	7.6			
Terms of Trade Index	94	95	100	89	91	92	96	3.1	-11.0	1.2			
Public Finance (Current Prices, US$ Mln.)													
Current Receipts	243	291	395	485	560	657	1,148	28.0	22.8	15.4			
Current Expenditures	219	258	350	405	500	599	1,012	26.0	15.7	16.5			
Public Savings	24	33	45	80	60	58	136	37.0	77.8	9.2			
Public Sector Investments	72	85	103	124	150	185	272	19.6	20.4	14.0			

September 1975

ATTACHMENT S 1

COSTA RICA: BALANCE OF PAYMENTS, EXTERNAL ASSISTANCE AND DEBT PROJECTIONS
(amounts in millions of U.S. dollars at current prices)

	Actual		Projected					
	1973	1974	1975	1976	1977	1978	1979	1980
SUMMARY BALANCE OF PAYMENTS								
Exports (incl. NFS)	422.3	533.0	615.7	721.9	873.5	1015.2	1166.4	1346.0
Imports (incl. NFS)	504.0	770.1	772.2	875.0	996.7	1130.5	1280.3	1447.4
Resource Balance	-81.7	-237.1	-156.5	-153.1	-123.2	-115.3	-113.9	-101.4
Interest (net)	-21.8	-20.1	-32.0	-42.3	-56.1	-68.1	-80.5	-94.4
Direct Investment Income (net)	-15.4	-21.7	-28.2	-35.5	-44.1	-53.9	-65.1	-78.2
Current Transfers (net)	7.0	7.6	8.4	9.2	10.1	11.1	12.2	13.5
Balance on Current Account	-111.9	-271.3	-208.3	-221.7	-213.3	-226.2	-247.3	-260.5
Private Direct Investment	37.6	43.0	49.5	56.9	65.4	75.2	86.5	99.5
Official Capital Grants	5.2	6.4	4.9	2.7	1.6	1.3	0.5	0.0
Public M & LT Loans								
Disbursements	70.8	108.6	185.6	189.1	191.2	206.1	229.8	246.2
-Repayments	-30.9	-32.1	-46.9	-51.4	-70.7	-82.7	-96.5	-113.0
Net Disbursements	39.9	76.5	138.7	137.7	120.5	123.4	133.3	133.2
Other Long Term (net)	12.1	13.5	15.0	15.0	15.0	15.0	15.0	15.0
Short Term (net)	-12.2	55.0	0.6	26.6	31.1	33.7	37.0	40.7
Other (incl. errors and omissions)	46.6	54.3	-	-	-	-	-	-
Change in Reserves (-increase)	-17.3	22.6	-0.4	-17.2	-20.3	-22.4	-25.0	-27.9
GRANT AND LOAN COMMITMENTS								
Official Grants & Grant-like	-	-	-	-	-	-	-	-
Public M & LT								
IBRD 1/	6.2	23.5	41.0	39.0	20.0	40.0	35.0	22.5
IDA	-	-	-	-	-	-	-	-
Other Multilateral	7.6	37.9	90.1	68.5	75.4	82.9	91.2	100.3
Bilateral	5.4	17.5	43.4	42.3	41.5	40.7	40.2	40.0
IMF Oil Facility	-	22.7	28.0	-	-	-	-	-
Other Public	54.3	70.7	64.7	98.2	93.3	73.8	90.0	114.1
Total Public M & LT Loans	73.5	172.3	267.2	248.0	230.2	237.4	255.4	276.9
DEBT AND DEBT SERVICE								
Public Debt Out. & Disbursed	248.4	324.9	463.6	601.3	721.8	845.2	978.5	1111.7
Interest on Public Debt	12.8	18.0	23.2	33.5	45.6	55.6	65.8	77.1
Repayments on Public Debt	30.9	32.1	46.9	51.4	70.7	82.7	96.5	113.0
Total Public Debt Service	43.7	50.1	70.1	84.9	116.3	138.3	162.3	190.1
Burden on Export Earnings (percent)								
Total Public Debt Service	10.3	9.4	11.4	11.8	13.3	13.6	13.9	14.1
TPDS & Direct Invest. Inc.	14.0	13.5	16.0	16.7	18.4	18.9	19.5	19.9
Average Terms of Public Debt								
Int. as Percent Prior Year DO & D	6.2	7.2	7.1	7.2	7.6	7.7	7.8	7.9
Amt. as Percent Prior Year DO & D	14.9	12.9	14.4	11.1	11.8	11.5	11.4	11.5
IBRD Debt Out & Disbursed	63.7	75.2	83.1	95.2	114.9	138.3	162.4	186.4
IBRD as Percent Public Debt O & D	25.6	23.1	17.9	15.8	15.9	16.4	16.6	16.8
IBRD as Percent Public Debt Service	15.3	14.8	11.7	11.2	9.2	9.3	10.4	10.8
IDA Debt Out & Disbursed	5.4	5.3	5.2	5.1	5.0	4.9	4.8	4.7
IDA as Percent Public Debt O & D	2.2	1.6	1.1	0.8	0.7	0.6	0.5	0.4
IDA as Percent Public Debt Service	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1

ACTUAL AND PROJECTED EXTERNAL DEBT	Actual Debt Outstanding on Dec. 31, 1974				Projected Debt Outstanding on Dec. 31, 1980		1974-80 Growth Rate
	Disb. Only	Percent	Total	Percent	Disb. Only	Percent	Disb. Only
IBRD	75.2	23.1	123.4	25.9	186.4	16.8	16.3
IDA	5.3	1.6	5.3	1.1	4.7	0.4	-2.0
Other Multilateral	28.3	8.7	77.4	16.2	346.1	31.1	50.0
Bilateral	69.0	21.3	98.7	20.7	238.1	21.4	23.0
IMF Oil Facility	22.7	7.0	22.7	4.8	13.4	1.2	-8.5
Other Public	124.4	38.3	148.9	31.3	323.0	29.1	17.2
Total Public M & LT	324.9	100.0	476.4	100.0	1111.7	100.0	23.0

1/ Starting in 1977, CY data have been derived by continuing FY data from the lending program (Attachment I).

COSTA RICA: BALANCE OF PAYMENTS: IMPORT DETAIL

(In millions of US$)

	1973	1974	1975	1976	1977	1978	1979	1980
I. Imports								
A. Constant (1973) prices								
Food	45.0	59.3	47.1	48.7	49.7	51.2	52.6	54.0
Other consumer goods	70.4	67.3	53.3	55.9	57.5	59.9	62.2	64.4
Petroleum	28.4	25.3	26.9	28.6	30.4	32.3	34.3	36.5
Intermediate goods	167.5	215.1	195.0	206.0	218.6	232.1	246.8	262.5
Capital goods	144.8	182.9	185.0	191.7	205.0	218.2	232.2	247.1
Total goods cif	456.1	549.9	507.3	530.8	561.2	593.7	628.1	664.6
Other non-factor services	47.9	43.3	38.0	40.3	42.7	45.3	48.0	50.9
Total goods and n.f.s.	504.0	593.2	545.3	571.1	603.9	639.0	676.1	715.5
B. Price indices (1973=100)								
Food	100.0	143.1	127.5	124.6	129.8	134.4	138.9	148.7
Other consumer goods	100.0	121.7	134.9	146.9	158.7	170.6	183.4	196.3
Petroleum	100.0	362.0	387.0	421.0	456.0	490.0	526.0	563.0
Intermediate goods	100.0	119.0	131.3	142.5	153.2	164.3	175.9	187.5
Capital goods	100.0	111.0	123.7	135.2	146.0	157.2	168.3	179.2
Total goods	100.0	130.5	142.1	153.7	165.5	177.4	189.8	202.7
Non-factor services	100.0	121.7	134.9	146.9	158.7	170.6	183.4	196.3
Total goods and n.f.s.	100.0	129.8	141.6	153.2	165.0	176.9	189.4	202.3
C. Current prices								
Food	45.0	84.9	60.0	60.7	64.6	68.8	73.1	80.3
Other consumer goods	70.4	81.9	71.9	82.0	91.3	102.2	114.0	126.5
Petroleum	28.4	91.6	104.1	120.4	138.6	157.8	180.4	205.5
Intermediate goods	167.5	256.0	256.0	293.5	335.0	381.3	434.0	492.2
Capital goods	144.8	203.0	228.9	259.2	299.4	343.1	390.8	442.9
Total goods	456.1	717.4	720.9	815.8	928.9	1,053.2	1,192.2	1,347.4
Non-factor services	47.9	52.7	51.3	59.2	67.8	77.3	88.1	99.9
Total goods and n.f.s.	504.0	770.1	772.2	875.0	996.7	1,130.5	1,280.3	1,447.4

COSTA RICA: BALANCE OF P[illegible]ENTS: EXPORT DETAIL

(in millions of US$)

	1973	1974	1975	1976	1977	1978	1979	1980
Exports								
A. Constant (1973) prices								
Coffee	94.0	115.4	90.0	90.0	103.0	104.0	107.0	110.0
Bananas	90.7	81.5	88.7	90.5	92.3	94.1	96.0	97.9
Sugar	21.5	13.3	15.7	18.1	20.8	23.9	26.8	29.2
Cocoa	4.4	4.0	5.3	5.5	5.8	6.1	6.4	6.7
Beef	31.6	43.0	45.0	49.4	54.4	60.4	67.6	76.4
Other goods	102.3	127.2	146.4	161.1	177.1	194.9	214.4	235.8
Total goods	344.5	384.4	391.1	414.6	453.4	483.4	518.2	556.1
Non-factor services	77.8	75.9	87.3	96.0	105.7	116.2	127.8	140.6
Total goods and nfs	422.3	460.3	478.4	510.6	559.1	599.6	646.0	696.7
B. Price indices (1973=100)								
Coffee	100.0	109.1	93.0	144.0	181.0	205.0	210.0	214.0
Bananas	100.0	117.8	140.0	111.8	119.8	125.9	133.8	142.6
Sugar	100.0	182.5	270.0	253.0	195.0	197.0	210.0	225.0
Cocoa	100.0	149.3	115.0	123.0	131.0	129.0	128.0	126.0
Beef	100.0	78.1	98.0	123.1	146.3	162.0	179.3	206.7
Other goods	100.0	121.7	134.9	146.9	158.7	170.6	183.4	196.3
Total goods	100.0	114.6	127.3	140.0	155.7	169.0	179.9	192.4
Non-factor services	100.0	121.7	134.9	146.9	158.7	170.6	183.4	196.3
Total goods and nfs	100.0	115.8	128.7	141.4	156.2	169.3	180.6	193.2
C. Current prices								
Coffee	94.0	125.9	83.7	129.6	186.4	213.2	224.7	235.4
Bananas	90.7	96.0	124.2	101.2	110.6	118.5	128.5	139.7
Sugar	21.5	24.3	42.5	45.8	40.6	47.1	56.3	65.7
Cocoa	4.4	5.9	6.1	6.8	7.6	7.9	8.2	8.5
Beef	31.6	33.5	44.0	60.9	79.6	97.8	121.2	157.9
Other goods	102.3	154.9	197.5	236.5	281.1	332.4	393.1	462.8
Total goods	344.5	440.6	498.0	580.8	705.9	816.9	932.0	1,070.0
Non-factor services	77.8	92.4	117.7	141.1	167.6	198.3	234.4	276.0
Total goods and nfs	422.3	533.0	615.7	721.9	873.5	1,015.2	1,166.4	1,346.0

COUNTRY DATA - COSTA RICA

AREA
50,900 km^2

POPULATION
1.82 million (mid-1972)

DENSITY
.. Per km2of arable land

SOCIAL INDICATORS

	Costa Rica 1960	Costa Rica 1970	Reference Countries: Mexico 1970	Panama 1970	Spain* 1970
GNP PER CAPITA US$ (ATLAS BASIS) /1	..	630 /a	750 /a	880 /a	1,210 /a
DEMOGRAPHIC					
Crude birth rate (per thousand)	48	32 /a	43 /a	36 /a	19 /b,c
Crude death rate (per thousand)	9	6 /a	9 /a	6 /a	9 /b,c
Infant mortality rate (per thousand live births)	74	57 /a,d	61 /a	38 /e	15 /b,c
Life expectancy at birth (years)	63 /f	69 /g	65 /a	64 /h	70
Gross reproduction rate /2	3.6	3.3 /g	3.0 /g	2.8 /h	1.4
Population growth rate /3	3.8	3.2 /i	3.5 /i	3.1 /i	1.1 /i
Population growth rate - urban	4.2 /j	4.7 /j	5 /i,k	5 /l	2 /m
Age structure (percent)					
0-14	48 /n	44 /b	46 /b	43 /a	28
15-64	49 /n	52 /b	50 /b	53 /a	63
65 and over	3 /n	4 /b	4 /b	4 /a	9
Age dependency ratio /4	1.0 /n	0.9 /b	1.0 /b	0.9 /a	0.6
Economic dependency ratio /4	1.9 /n	1.7 /b	1.6	1.5	1.1
Urban population as percent of total	34 /j,n	46 /j,o	60 /a,k	48 /e,l	49 /m,p
Family planning: No. of acceptors cumulative (thous.)	..	..	..	..	..
No. of users (% of married women)	..	..	..	..	..
EMPLOYMENT					
Total labor force (thousands)	400 /n	600 /b	13,000	470	12,700 /a
Percentage employed in agriculture	49 /n	37 /b	39	39	28 /e
Percentage unemployed	7 /n	4 /q	4	7	1 /e
INCOME DISTRIBUTION					
Percent of national income received by highest 5%	35 /r,s	23 /e,s	36 /o,s	33 /o,t	..
Percent of national income received by highest 20%	60 /r,s	51 /e,s	64 /o,s	59 /o,t	..
Percent of national income received by lowest 20%	6 /r,s	5 /e,s	4 /o,s	3 /o,t	..
Percent of national income received by lowest 40%	14 /r,s	15 /e,s	11 /o,s	9 /o,t	..
DISTRIBUTION OF LAND OWNERSHIP					
% owned by top 10% of owners	..	..	..	45	..
% owned by smallest 10% of owners	..	..	..	1	..
HEALTH AND NUTRITION					
Population per physician	2,200	1,630	1,440	1,550	750 /u
Population per nursing person	1,210 /v	1,690	1,570	1,210	1,430 /w
Population per hospital bed	..	250	930	320	220 /w
Per capita calorie supply as % of requirements /5	98 /r	110	110	109	107
Per capita protein supply, total (grams per day) /6	55 /r	63	65	61	81
Of which, animal and pulse	30 /r	35	28	31	40
Death rate 1-4 years /7	7.5 /n	6.4	11	7	0.9
EDUCATION					
Adjusted /8 primary school enrollment ratio	100 /x	112 /x	104 /x	110 /x	83
Adjusted /8 secondary school enrollment ratio	21	29	23	42	49
Years of schooling provided, first and second level	11	11	12	12	13
Vocational enrollment as % of sec. school enrollment	19 /y	10 /y	24 /o	32	20
Adult literacy rate %	..	89 /e,z,aa	76 /z,aa	82 /aa,ab	94 /w,z
HOUSING					
Average No. of persons per room (urban)	1.3 /n,p	1.1 /o	2.5 /ac,ad	2.5 /p	..
Percent of occupied units without piped water	41 /n,ae,af	..	61 /ad,af	74 /af	..
Access to electricity (as % of total population)	55 /n,ae	..	59 /ad	52	..
Percent of rural population connected to electricity	32 /n,ae	..	..	16	..
CONSUMPTION					
Radio receivers per 1000 population	66	73 /a	301 /a	164 /a	210 /a
Passenger cars per 1000 population	14	26 /a	28 /a	34 /a	95 /a
Electric power consumption (kwh p.c.)	385 /n	687 /a	662 /a	640 /a	1,946 /a
Newsprint consumption p.c. kg per year	3.1	5.7 /a	1.8 /a	3.9 /a	6.0 /a

Notes: Figures refer either to the latest periods or to the latest years. Latest periods refer in principle to the years 1956-60 or 1966-70; the latest years in principle to 1960 and 1970.

/1 The Per Capita GNP estimate is at market prices for years other than 1960, calculated by the same conversion technique as the 1972 World Bank Atlas.

/2 Average number of daughters per woman of reproductive age.

/3 Population growth rates are for the decades ending in 1960 and 1970.

/4 Ratio of population under 15 and 65 and over to population of ages 15-64 for age dependancy ratio and to labor force of ages 15-64 for economic dependency ratio.

/5 FAO reference standards represent physiological requirements for normal activity and health, taking account of environmental temperature, body weights, and distribution by age and sex of national populations.

/6 Protein standards (requirements) for all countries as established by USDA Economic Research Service provide for a minimum allowance of 60 grams of total protein per day, and 20 grams of animal and pulse protein, of which 10 grams should be animal protein. These standards are somewhat lower than those of 75 grams of total protein and 23 grams of animal protein as an average for the world, proposed by FAO in the Third World Food Survey.

/7 Some studies have suggested that crude death rates of children ages 1 through 4 may be used as a first approximation index of malnutrition.

/8 Percentage enrolled of corresponding population of school age as defined for each country.

/a 1972; /b 1973; /c Excluding Centa and Melilla; /d Rate computed on live-births tabulated by registration; /e 1971; /f 1962-64; /g 1970-75; /h 1965-70 UN estimate; /i 1960-72; /j "Metropolitan area" of San Jose City (excluding rural sector of district of Las Pavas), Cartago City, and administrative centers of all cantons except San Pablo, Nandayure and Buenos Aires; /k Localities of 2,500 or more inhabitants; /l Localities of 1,500 or more inhabitants having essentially urban characteristics; /m Localities of 10,000 or more inhabitants; /n 1963; /o 1969; /p Estimate; /q 1967; /r 1961; /s Households; /t Economically active population; /u Number on the register, not all working in the country; /v 1964; /w 1968; /x Including overage students; /y Not including teacher-training; /z 15 years and over; /aa Definition not available; /ab Ten years and over; /ac Urban and rural; /ad Data refer to housing units; /ae Data refer to living quarters; /af Piped water inside.

* Spain has been selected as an objective country because it has the same cultural tradition, it is also an open economy with strong trade relations with neighboring countries and has a high standard of living. Yet, because of a dynamic growth of exports of goods and services, Spain has achieved aq economic diversification and stability that would be desirable for Costa Rica.

COSTA RICA: CUMULATIVE ESTIMATED AND ACTUAL DISBURSEMENTS OF LOANS AND CREDITS

($ millions)

as of June 30, 1975

Project & No.	Amount: - Original - Cancelled - Net	Date: - Approved - Signed - Effective		Closing Date	Forecast Date	FY'74	FY'75 1	FY'75 2	FY'75 3	FY'75 4	FY'76 1	FY'76 2	FY'76 3	FY'76 4	FY'77	FY'78	FY'79	FY'80	FY'81	FY'82	FY'83
Siquirres-Limon	15.7	3/31/70	Orig:	12/31/75	9/30/70 (1st)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Highway	-	4/ 2/70	Rev:	-	12/27/74	-	-	12.1	13.2	14.2	15.2	15.7	-	-	-	-	-	-	-	-	-
IBRD 664	15.7	6/17/70	Act:	-	-	10.3	10.3	12.1	12.1	12.2											
Fourth	6.5	2/15/72	Orig:	6/30/76	1/19/72	4.6	4.9	5.2	5.5	5.8	6.0	6.2	6.4	6.5	-	-	-	-	-	-	-
Power	-	2/24/72	Rev:	-	1/ 6/75	-	-	-	-	6.3	6.3	6.4	6.4	6.5	-	-	-	-	-	-	-
IBRD 800	6.5	6/ 2/72	Act:	-	-	6.0	6.0	6.1	6.2	6.2											
Third	17.5	2/15/72	Orig:	6/30/77	1/19/72	10.2	10.5	12.3	13.0	14.0	15.0	16.0	16.8	17.0	17.5	-	-	-	-	-	-
Telecommunication	-	2/24/72	Rev:	-	6/10/75	-	-	-	-	12.5	13.5	14.5	15.0	15.5	17.5	-	-	-	-	-	-
IBRD 801	17.5	6/ 2/72	Act:	-	-	6.3	7.4	9.5	12.1	14.2											
Second	9.0	5/16/72	Orig:	12/31/76	4/12/72	3.5	4.0	4.7	5.4	6.1	6.8	7.3	7.8	8.3	9.0	-	-	-	-	-	-
Agricultural Credit	-	6/ 5/72	Rev:	-	12/31/74	-	-	-	-	5.5	6.3	7.0	7.7	8.3	9.0	-	-	-	-	-	-
* IBRD 827	9.0	1/25/73	Act:	-	-	3.0	3.3	3.6	3.6	3.8											
Highway	1.4	12/19/72	Orig:	12/31/74	12/ 6/72	1.4	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Studies	-	12/28/72	Rev:	12/31/75	12/28/74	-	-	.4	.9	1.4	-	-	-	-	-	-	-	-	-	-	-
IBRD 872	1.4	6/29/73	Act:	-	-	-	-	.4	.4	.4											
Education	6.2	6/19/73	Orig:	12/31/78	5/29/73	.2	.3	.4	1.0	1.6	2.2	3.2	4.0	4.8	6.0	6.2	-	-	-	-	-
Project	-	6/25/73	Rev:	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
IBRD 915	6.2	12/27/73	Act:	-	-	-	-	-	-	-											
Fourth	23.5	6/11/74	Orig:	12/31/78	5/21/74	-	-	3.2	5.1	6.8	8.0	10.5	11.5	13.0	19.0	23.5	-	-	-	-	-
Telecommunication	-	6/14/74	Rev:	-	6/10/75	-	-	-	-	3.0	4.8	6.5	8.8	11.0	18.5	23.5	-	-	-	-	-
IBRD 1006	23.5	11/19/74	Act:	-	-	-	-	-	.1	.4											
Fifth	41.0	6/ 9/75	Orig:	6/30/79	6/16/75	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Power	-	6/16/75	Rev:	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
IBRD 1126	41.0	N.E.	Act:	-	-	-	-	-	-	-											

* Balance indeterminate

Controller's
8/15/75

Attachment V

Economic Work Program

An economic mission leading to the preparation of an economic memorandum is presently scheduled for May 1976. It will review prospects and major constraints to the long-term development of Costa Rica.

At the sectoral level, the following activities are underway or planned: (i) an agricultural-rural sector survey report, based on the findings of a joint IBRD/IDB/AID mission earlier this year, is currently in preparation: it should provide an analysis of the major constraints to agricultural development in Costa Rica as well as identify project possibilities; (ii) an industrial sector survey mission is scheduled for October 1975 to study small and medium-scale industrial development possibilities and identify appropriate channels for DFC-type lending; (iii) a tourism sector survey mission will be sent in March 1976 to review prospects for increased foreign exchange earnings from this sector; (iv) transport sector knowledge will be updated in connection with project preparation and appraisal work for the proposed 1976 and 1977 transport loans; and (v) power sector information will be reviewed in connection with supervision of on-going projects and the proposed 1979 loan to this sector.

(ii) Political Situation

A progressive political party (which included some communists) held the Presidency of Costa Rica from 1940 to 1948. It was responsible for important social legislation -- a labor code and the establishment of a social security system -- but it began to lose popular support as it showed an increasing tendency towards repression against those who opposed its policies. Finally, when a Congress dominated by the Government party attempted to annul the election of the opposition candidates (Ulate) to the Presidency in 1948, revolution broke out. A group of young politicians and intellectuals, led by Jose Figueres Ferrer overthrew the regime and ruled as a junta until 1949. Upon adoption that year of a new Constitution which reflected strongly the view of Figueres and his followers, the junta withdrew and Ulate was inaugurated as President.

Since 1949 Costa Rican political life, in sharp contrast to that of its Central American neighbors, has been characterized by free elections and by the peaceful transfer of power from one president to the next every four years. The most important political party during this period has been the Partido de Liberacion Nacional (PLN), founded by Figueres in 1951. It has won four of the six elections since the 1949 Constitution was adopted (Figueres himself was elected President in 1953 and 1970). Figueres and his supporters, first through the 1949 Constitution and later when they controlled the Presidency, adopted a number of important reforms. The standing army was abolished; women were given the right to vote; free secondary education was established; the commercial banking and insurance sectors were nationalized; The Government gained control over the major public utilities (power, water, telecommunications); the minimum wage was introduced. The most recent initiative in the social welfare field, proposed first by Figueres and subsequently adopted during the Oduber administration, is the family assistance program, which is to be financed by an increase in the sales tax and a payroll tax. It would involve programs of food, nutrition, health, water supply and housing for over 1,000 rural communities.

Although PLN candidate Oduber won the 1974 election with less than a majority of the vote, and the PLN for the first time in its history does not have a majority in the Congress, the opposition is fragmented, and Oduber so far has not had difficulty obtaining passage of his legislative program. In the short run, there appear to be no major political issues threatening the Oduber administration or the PLN. The Government seems to be coping with the economic problems which developed in 1974, and has taken measures to protect the incomes of the working classes and to begin addressing the problems of the lowest income groups. The "Vesco case" seems to be fairly quiet, at least for the moment, as the opposition continues to be unable successfully to exploit the relationships between Vesco and prominent PLN figures. There is no question that some key PLN leaders (Mr. Oduber probably excluded) have had substantial financial ties with Vesco, the fugitive American financier. Figueres offered Vesco a haven in Costa Rica in 1972 in return for investing in the country. Vesco became a partner with Figueres in an otherwise bankrupt business (Vesco's estimated "stake" - $2 - 3 million). Mr. Figueres' son-in-law, Danilo Jimenez Veiga, ex-Minister of Labor and now Executive President of INA (National Vocational Training Institute), reportedly also established a partnership with Vesco in a timber-processing firm. Foreign Minister Gonzalo Facio's law firm represents Vesco in the local courts. Furthermore, Vesco is believed to have made campaign contributions to a number of Congressmen. In an essentially wide open economy such as Costa Rica's it is easy to disguise investments, and no one knows the extent of Vesco's holdings, but what is known about them and his connections with public officials, together with a US$20.0 million equivalent purchase of Government bonds (after he was granted resident status), have been interpreted by many Costa Ricans as "Vesco buying a republic". In the heat of the Presidential election campaign of 1973 and early 1974, the opposition requested expulsion of Vesco and resignation of Figueres. Figueres refused and just before he left office the PLN-dominated Congress passed a law (the so-called Vesco law) which made the extradition of Vesco practically impossible. The opposition this year made an attempt to repeal the Vesco law, but after this was unsuccessful and President Oduber made it clear he was not going to take action to expel Vesco, the issue again subsided.

(iii) Economic Situation

See discussion in F.2(a) of the Country Program Paper.

(iv) Foreign Assistance and Debt

See discussion in F.2.a Country Program Paper.

Guatemala

F.2.c Guatemala

(i) Political Situation

There was increasing unrest in Guatemala in the years following the assassination of the dictator Castillo Armas in 1957. Terrorism by the left and right-wing guerrilla groups was first concentrated in the rural areas but by 1968 these groups were most active in the urban centers, especially in Guatemala City. In July 1970, Colonel Arana Osorio came to power after promising to restore law and order. Arana Osorio succeeded in reducing the level of violence and terrorism substantially, while at the same time stressing the importance of development and social justice and promised to implement the progressive Development Plan 1971-75, which had been prepared by the Planning Office of the previous administration. Despite the severe domestic political pressures, the administration did adopt a series of economic and organizational measures which had been recommended by the Plan.

In July 1974, General Kjell Laugerud García was sworn in as President after a heated dispute over the presidential election results. While retaining most of the cabinet officers of the previous administration, he has replaced two of the most powerful Ministers (Economy, and Communications and Public Works). These Ministers were also those who most strongly opposed the Bank's position on the proposed third power project which resulted in a temporary cooling of relations between the Bank and Guatemala.1/ The new Ministers, together with the Minister of Finance, have been instrumental in rebuilding a normal working relationship with the Bank which has resulted in the development of a substantial lending program for Guatemala.

The political coalition of three traditionally rightist parties that took General Laugerud to the presidency in last year's election broke up early this year with the withdrawal of the National Liberation Movement (MLN). The MLN is dissatisfied with what it considers to be a shift to the left in the government economic and social policies, its specific complaint being the Government's support of the rural cooperative movement. The MLN alleges that communism has infiltrated Guatemala again and has denounced the existence of "Peruanismo" within the ranks of the

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1/ In July 1973, the Bank had refused to approve a proposed contract award for the major project components on the ground that the contractor involved had not presented the lowest evaluated bid.

armed forces. The President went to great lengths in a speech delivered to Congress on the July 1 anniversary of his inauguration to justify the Government's support for small farmers and rural cooperatives while vigorously rejecting any notion that this had anything to do with communism. He concluded by calling on the powerful economic groups in the country to join forces with the Government's program.

(ii) Economic Situation

Guatemala is a country with considerable economic potential. The northernmost of the five countries forming the Central American Common Market (CACM), it has not only the largest population -- over 5 million -- but it is also the best endowed in terms of natural resources. Its rich, mainly volcanic soils located in a wide range of altitudes allow the cultivation of almost any type of agricultural product. There are some mineral resources, and construction of a large nickel enterprise will start soon. The economics of the exploitation of oil resources available near the Mexican border is under study. In addition, Guatemala, because of climate, physical environment and archeological assets has substantial tourism potential. Thus far, however, the country has taken much less than full advantage of its development potential and the bulk of its native population, which constitutes close to half of the total, lives on the margin of the monetary economy.1/

During the 1950's and 1960's real GDP increased at an average rate of about 5 percent per year; in the 1970's the rate has accelerated to over 6 percent. The economy is highly dualistic with an efficient export agricultural sector existing side by side with subsistence farming, which is largely concentrated in the Indian highlands. Given the inadequate income and employment base of the smallest farmers, most of them are forced to supplement their incomes through seasonal work on large plantations. It is estimated that over 400,000 workers a year are involved in seasonal migration. Although the accomplishments of the National Institute of Agrarian Reform in inducing resettlement of "minifundistas" or landless rural workers have been limited, considerable spontaneous migration towards the underpopulated northern section of the country has taken place and continues at present. This migration process may have alleviated population pressure in the cities and reduced problems of urban unemployment. (In the past ten years urban population grew only slightly faster than rural population.)

1/ According to an FAO study prepared for SIECA, published in 1974, Guatemala has the most uneven income distribution of the five Central American countries.

The lack of social and economic infrastructure, especially in rural areas, is a serious constraint on Guatemala's development process. Because of the traditionally limited role of the public sector in the economy, education and health facilities, electricity, water supply, and road connections are either non-existent or deficient in most of the rural areas. In the case of education, the problem is compounded by the lack of Spanish among many groups of the Indian population, and in the case of road connections, Guatemala's mountainous and broken relief has made their development rather costly.

Although the participation of the public sector in the economy has increased somewhat in the past decade, owing to the creation of new public entities and rapid development of some public utilities already in existence, it remains at a very low level. Central Government current revenues since the mid-1960's have fluctuated around 8.5 percent of GDP, and current expenditures around 7.5 percent of GDP -- the lowest ratios in Central America. Fiscal policy traditionally consists in adjusting expenditures to available revenues. Given the extension of poverty in the country, and particularly in rural areas, the low level of current expenditure has been inadequate to meet the needs of the population. An expansion of current expenditures in health and education is urgently needed. Moreover, the higher levels of government investment since 1972 (which are projected to continue during the 1975-79 plan period), and which have grown most rapidly in the social areas, will necessitate substantial increases in the government's current expenditures. The 1975-79 Development Plan contemplates higher rates of current revenues and expenditures than in the past to provide for an expansion in public services, but does not make allowances for the upgrading of the services already being provided. A major obstacle to the growth of investment has traditionally been the limited capacity in project preparation. The Planning Office expects to receive technical assistance from the Interamerican Development Bank for the establishment of a project evaluation, coordination and control unit within the Planning Office and project preparation units in the various specialized public agencies.

The Plan contemplates substantial changes in investment priorities. The share of health and education is expected to increase from about 15 percent of total public investment to over 20 percent; the share of transport is expected to decrease from about one-third to about 17 percent, with major emphasis on feeder roads as opposed to highways. The share of power is planned to increase mainly through the development of hydroelectric generating capacity, which would reduce the current heavy dependence on thermoelectricity and thus on imported oil. Moreover, a considerable expansion of the present generating capacity is urgently required if a serious bottleneck to industrial development is to be avoided. Increased emphasis is also planned for the rural sector. The Government in its recent public statements has been stressing the importance of a stepped-up public sector effort to help the rural poor. It is focusing on the development of credit programs for rural cooperatives, which have grown in number in the past few years and now serve an estimated 50,000 small (mostly Indian) farmers. To finance the proposed increased levels of public investment will require a substantially stepped-up fiscal effort and substantial assistance from external financing agencies.

The traditional vulnerability of Guatemala's balance of payments has been reduced substantially in recent years as a result of a gradual diversification of the export structure. During the early 1960's coffee accounted for 70 percent of export earnings and bananas for another 15 percent. By the mid-1960's, cotton had replaced bananas as second major export commodity and industrial products accounted for about one-fourth of merchandise exports. In the latter part of the 1960's and early 1970's exports of meat and sugar as well as exports of manufactures to the CACM, such as textiles, clothing and chemicals continued to grow, and industrial products exports have now surpassed coffee in importance. Also, in recent years tourism has become a leading source of foreign currency for the country.

Imports growth, which was very high in the first half of the 1960's, decelerated considerably thereafter and until 1972, owing to the rapid process of import substitution of non-durable consumer goods. In 1973 and 1974 imports grew at unprecedented rates, mainly as a result of a rapid increase in import prices, but also because of accumulation of inventories. The process of industrialization has resulted in substantive changes in the structure of imports, with consumer goods reducing their share in total imports from 34 percent in 1960 to only 27 percent in 1973, while raw materials increased their share by almost 10 percentage points in the same period.

The prospects for continued growth of the Guatemalan economy at about 6-7 percent per year are fairly good. Favorable market conditions are foreseen for the country's principal exports. A continued expansion of tourism is expected. The low public debt service ratio and relatively high level of foreign exchange reserves will permit an expansion of foreign borrowing to help finance a considerably higher level of investment.

(iii) Foreign Assistance and Debt

During the period 1970-74, Guatemala has borrowed about US$220.0 million from external sources, of which about 80 percent is repayable in foreign currency. The Bank has provided US$20.0 million. The Inter-American Development Bank (IDB) has provided a similar amount repayable in foreign currency and over US$40.0 million repayable in domestic currency, with a major share of these loans for health, transport and agriculture. The Central American Bank for Economic Integration (CABEI) has provided about US$40.0 million, mainly for transport, industry, agriculture and telecommunications. AID has lent about US$46.0 million with major emphasis in agriculture. In addition, the Guatemalan public sector has borrowed about US$54.0 million from suppliers and private financial institutions during the period. As of end-1974, total public debt outstanding repayable in foreign currencies including undisbursed amounted to US$207.0 million, of which only about 8 percent had been contracted with external private sources. This debt structure represents a significant improvement from 1965, when the debt outstanding from private sources accounted for 42 percent of the total. and will help maintain Guatemala's public debt service ratio at levels similar to or lower than those attained in the past two years (about four percent of exports).

Under the December 1974 Venezuelan oil facility agreement, Guatemala will be able to borrow up to an estimated US$25.0 million in 1975, and decreasing amounts in subsequent years.

Honduras

F.2.d. - HONDURAS

(i) Political Situation

Honduras has been ruled by military governments since December 1972, at which time General Oswaldo Lopez Arellano, Chief of the Armed Forces, became Chief of State in a bloodless coup. General Lopez continued to hold these two positions until April 1975 when he was removed as Chief of the Armed Forces by the Supreme Council of the Armed Forces, after a group of young lieutenant colonels who apparently favored more rapid action on social reform measures ousted most of the older officers who previously controlled the military. Shortly thereafter, the United Brands bribe attempt was disclosed with the accusation that high government officials were to be paid US$2.5 million by United Brands to lower or eliminate the recently imposed banana export tax. Although no firm proof has been presented directly linking General Lopez with the bribe, he was ousted as Chief of State when he refused to provide information on his foreign bank accounts to a government commission investigating the bribe. General Lopez was replaced by Colonel Juan Melgar Castro, a close associate.

Although the Army has controlled the Government for the last three years, all major Cabinet positions have been filled by civilians and there has been continuity of economic policies between the Lopez and Melgar Governments. Although these two governments might be characterized as oriented toward the Peruvian model, no formal ideology has been adopted and basic liberties, e.g., of speech, press, etc., have not been restricted. These governments have been far more active in their efforts to promote Honduran development than has been the traditional pattern. Upon taking office in 1972, General Lopez' Government promulgated emergency land reform legislation which provided for the compulsory leasing of under-utilized land for the resettlement of landless farmers. Under this measure, approximately 20,000 families have been given land. In addition, timber rights in the Olancho Forest Reserve (the country's major natural resource) were nationalized, and a National Forest Corporation (COHDEFOR) was created with the responsibility for managing conservation programs, exporting lumber and developing forest industry projects. The Lopez Government also created a National Industrial Development Corporation (CONADI) to stimulate the establishment of new industries. An ambitious public investment program has been drawn up and substantial foreign assistance is being negotiated for the financing of this program.

These actions represent a significant departure from previous policies and were undertaken in response to the Army's growing concern that social and economic problems were not being confronted effectively.

Rural unrest had reached the point where sporadic violence was common and the well organized peasant unions were threatening massive land invasions. (Honduras' three major peasant unions are officially estimated to have a total membership of 100,000, or roughly one-third of rural families.) The development of forest industries, particularly a pulp and paper industry, has been discussed for over ten years, but no action had been taken to lay the foundation for such projects. Public investment in infrastructure was taking place, but on an intermittent basis, and the country's basic infrastructure, particularly its transport and communications system, had not been completed. There was also a strong feeling that the private sector was not sufficiently dynamic or committed to Honduran development to provide the investment needed to undertake important agricultural and agro-industrial projects.

The policies of the Lopez Government have continued under Colonel Melgar. The agrarian reform law passed in January 1975 and which replaces the emergency legislation, provides for the expropriation of all underutilized rural land (including that previously leased under the interim program) in excess of fixed limits determined for each part of the country. This land would be transferred to landless peasants who are to be settled in groups of about 100 families to form "associative enterprises." The international organizations which have analyzed the law, generally agree that while it is moderate in nature, it should make available sufficient land to satisfy peasant union demands. The law will most seriously affect the traditional cattle ranchers who do not make productive use of their extensive holdings. However, it has also been opposed in principle by much of the rest of the private sector which views it as a step towards socialization. The Melgar Government hopes to convince the private sector that it will administer the agrarian reform in such a way as not to disrupt productive commercial agriculture, and recent Bank conversations indicate that there is some confidence in the private sector that their legitimate interests will be protected.

The Government moved slowly in its preparation of the agrarian reform law and regulations in order to resolve as many potential conflicts with the private sector as possible, but as a result it has come under intense pressure from the peasant unions, and another round of land invasions is expected within the next few months, since the Government will not be in a position to start distributing land before the upcoming planting season. It appears to be the Government's intention to quickly expropriate and redistribute sufficient land to satisfy peasant union groups in areas where the potential for violence is greatest in order to defuse this situation; however, it will probably take several years before the redistribution process is sufficiently advanced to significantly reduce the risk of violence in rural areas.

The private sector is also concerned with other government initiatives such as its taking control of forest development and wood exports, the creation of CONADI, and the proposed tax measures which will be necessary to finance the substantially increased public investment program. These are all held to be indicative of a growing tendency toward replacing private with state activity. In response to these military government initiatives, the private sector has recently been campaigning for a return to constitutional government. Thus far they have had little success, and the military still seem to be firmly in control. Within the military itself, the colonels who now control the Supreme Council are generally regarded as being more progressive than the Melgar Administration. For the present, however, this group appears to be somewhat divided and none of them has succeeded in establishing the power base or reputation necessary to challenge Colonel Melgar's control.

(ii) Economic Situation

With a per capita income of US$320 in 1973[1/], Honduras is the poorest country in Central America. Approximately two-thirds of the country's 2.7 million people live in rural areas, where a large majority obtains only a bare subsistence income. An official survey conducted in 1967-68 found that 60 percent of rural families received an annual income of less than $250 or an income per capita of about $40-$50; the comparable percentage in the two main cities was about 3 percent of families. The average national caloric and protein intake is well below minimum requirements; it has been estimated that 75 percent of pre-school children suffer from nutritional deficiencies and that the poorest 50 percent of the population has a daily intake of only 1,465 calories and 33 grams of protein. The need for social improvement is underscored by other indicators, such as the adult literacy rate, which is only about 50 percent. Progress in overcoming these deficiencies is difficult because of the rapid population growth rate, presently estimated at 3 percent per year, and the historically low rate of economic growth: GDP per capita, in real terms, grew at only 0.7 percent per year between 1950 and 1974.

The main determinants of the slow pace of economic growth in Honduras include a limited resource base, a lack of basic infrastructure and a continued dependence of the economy on the output and exports of bananas. The country's major agricultural asset is

1/ World Bank Atlas methodology.

the fertile coastal plain in the northwest of the country, where banana production for export has been developed by foreign companies since the late nineteenth century. Further to the east lie Honduras' large unexploited pine forests. With the exception of the northern coastal plain and the easternmost Mosquitia area, which consists of savannah and tropical forests and is virtually uninhabited, the country is made up of rugged hills and mountains, interspersed with valleys. At present the bulk of the population lives in the southern and western parts of the country, where the productivity of land and labor is very low and the rudimentary transport network has further limited the economic and social development and integration of the area. Significant road development in Honduras started only in the middle 1950's and the paving of the major highway connecting the northern industrial city of San Pedro Sula with the capital of Tegucigalpa was completed only about 5 years ago. As population pressure increases in the traditional areas, currently inaccessible fertile valleys in other parts of the country will have to be opened up but this will require large additional investments in physical infrastructure. Finally, the country has very limited known mineral resources; they include silver, lead and zinc, which are being exploited in small quantities, and low-grade iron ore.

The productive structure of the economy has changed little over time. It consists of a fairly efficient export agricultural sector, principally bananas, a stagnant non-export agricultural sector and the most undeveloped and least competitive industrial sector in Central America. Banana production has remained the major source of economic growth; banana exports still account for about 40-45 percent of total exports. To a large extent, Honduras' sluggish economic performance reflects the slow growth of the world banana market. Moreover, bad weather and plant disease have periodically brought economic instability. A recent illustration was the devastating effect of Hurricane Fifi in September 1974, which destroyed banana plantations as well as other crops, livestock and infrastructure. This natural disaster coupled with the effects of the depressed world economic situation, is expected to lead to a decline of 3-5 percent in Honduran national income during 1975. Other major export products aside from bananas include coffee, lumber and beef. Exports of industrial products are very limited. The creation of the Central American Common Market (CACM) in the early 1960's was a most promising attempt to expand and diversify the structure of production and exports; however, the short conflict with El Salvador in mid-1969 led to Honduras' withdrawal from the free trade arrangements of the market and progress towards their reestablishment has been limited.

Honduras' growth prospects during the remainder of the decade are limited. The world banana market outlook is for little growth and the supply of other major exports such as beef of lumber cannot be expanded rapidly. In view of the long-term relative stagnation of the Honduran economy, the extreme poverty of the rural population, the increasing rural unrest and the bleak growth prospects, the Honduran Government has mounted an ambitious public investment program, designed to alleviate the shortage of basic infrastructure, to diversify the structure of production and exports through the orderly but rapid development of the country's large forest resources and to improve the living standards of the rural population through agrarian reform. The public sector has so far limited its external borrowing to long-term official sources, with a resulting debt service ratio of only about 4 percent leaving ample margin for future borrowing. Given the vulnerable nature of the Honduran economy, however, a successful public investment program will be contingent upon generous international assistance on continued soft terms. At the same time, a substantial domestic tax effort will be required. In order to help speed up the agrarian reform process, international technical as well as financial assistance will be required. The Government's administrative and technical capabilities to carry out a successful agrarian reform are extremely limited; yet progress must be as rapid as possible, especially in view of the increasing rural unrest. In order to help strengthen the structure of the economy, it is also vital that improved economic relations with El Salvador be reestablished as soon as possible.

(iii) Foreign Assistance and Debt

At present the Bank is Honduras' largest creditor, holding 28 percent of the US$273.5 million external public debt outstanding as of December 31, 1974. This includes undisbursed debt repayable in foreign currency. IDA holds an additional 13 percent of the total. Although IDB has made loans totaling the equivalent of US$88.0 million, over 80 percent is repayable in local currency; consequently, IDB's share of the public debt repayable in foreign currency is only 6 percent. CABEI accounts for 22 percent of the total, the U.S. Government for 25 percent, Venezuela for 2 percent and privately held debt for 4 percent. Of the US$88.7 million outstanding debt repayable in local currency, the IDB accounts for 81 percent, CABEI for 14 percent and the USAID for 5 percent. The debt service ratio is currently 3.7 percent. It will increase as a reult of borrowing to finance the ambitious public investment program. As a result, even if Honduras is able to obtain generally concessionary terms, as has been the case in the past, the debt service ratio may rise significantly in the 1980's.

The Venezuelan Government has established a special oil facility for the countries of Central America and Panama. Under this arrangement, about US$40.0 million will be available to Honduras in 1975 and 1976. These funds can be used to finance the local costs of projects financed by the international lending agencies; however, Honduras and Venezuela have not yet reached agreement on which projects would receive such support. Honduras also received US$20 million from the IMF oil facility in 1974, but is not eligible in 1975.

Apart from the Bank Group, external assistance has been provided principally by USAID, the IDB, and the Central American Bank (CABEI). The lending of these agencies by sector is summarized below.

	IBRD	IDA	AID	IDB 1/	CABEI	Total
Total Gross Lending 1950-June 1975	127.4	33.2	94.4	100.7	134.8	490.5
Gross Lending 1950-1965	25.9	12.5	26.7	27.2	8.1	100.4
Gross Lening 1966- June 1975	101.5	21.7	67.7	73.5	126.7	391.1
Sectoral Lending 1966- June 1975						
Transport	38.2	--		11.6	51.5	101.3
Power	60.3	9.5		--	12.9	82.7
Telecommunications	--	--		--	5.6	5.6
Education	3.0	3.0	9.0	7.6	--	22.6
Health	--	--	6.7	15.1	10.2	32.0
Housing	--	--	4.0	12.5	14.1	30.6
Agriculture	--	9.2	40.0	24.5	1.2	74.9
Industry	--	--	1.5	2.2	28.8	32.5
Other	--	--	6.5	--	2.4	8.9

1/ Most IDB lending is repayable in local currency.

Nicaragua

F.2.e. NICARAGUA

(i) Political Situation

Nicaragua's political system has for many years been dominated by the executive branch, which has had the support of the National Guard, the country's only military force. The loyalty of the Guard has served as a deterrent to the possible use of force by opposition groups, and it has been successful in dealing with attempted coups, riots and sporadic guerrilla activity in the mountainous areas of the country.

The two political parties, the Liberals and the Conservatives, have been competing for power since the formation of the republic in the early part of the 19th century. Liberal control of the Government since 1937 has been due to the success of the Somoza family in maintaining itself and its party in power. Since 1937, the liberals have won elections by large margins, with support from rural areas and from the growing middle class. While irregularities have been alledged in the past, neutral observers seem to agree that there was little tampering with the results of the last (1974) election. The Liberal and Conservative Parties control their own newspapers and radio stations. La Prensa, the chief conservative opposition paper, vigorously attacks the Government of General Somoza, and has occasionally been closed for short periods of time.

In August 1971, President Somoza, after obtaining the agreement of the leadership of the opposition Conservative Party, dissolved Congress which was replaced by a popularly elected Constituent Assembly. The Assembly approved a new constitution in early 1974, which allowed President Somoza to be re-elected. In the interim period General Somoza maintained control of the Government through membership on a three-member Governing Council. This Council (which included a member of the opposition) exercised formal executive power. General Somoza was also appointed head of the National Committee of Economic Reconstruction which was created to coordinate the reconstruction efforts after the December 1972 earthquake. Through these positions he maintained firm personal control over the day-to-day public administration, with all the branches of the executive reporting directly to him.

In the elections of September 1974, General Somoza obtained 92 percent of the vote and his new Government was inaugurated in January 1975. Recently, an increase in guerrilla activities by the Sandinista National Liberation Front has been reported in the area of Matagalpa, and some successful raids have taken place in Managua itself -- most notably the kidnapping of prominent officials last December. (They were released after the Government yielded to the guerrillas' demands for a substantial cash payment and safe passage to Cuba.) As a result, there has been a noticeable increase in the security measures in the last year for the more important Government officials.

(ii) Economic Structure and Long-Term Past Trends

The December 1972 earthquake which destroyed Managua, the capital city, the oil crisis and the OECD recession have resulted in sharp deviations from the historical trends for a number of Nicaraguan economic parameters. Most but not all of these deviations may be considered of a temporary nature, and will be discussed in the context of recent developments and prospects.

Nicaragua's major natural resource is its arable land. A main feature of economic development over the last twenty years was the doubling of the farm area compared to an increase in population of around 80 percent. Most of the considerable net addition to Nicaragua's farmland has been for the development of livestock production. There have also been large increases in the area devoted to cotton, corn and coffee production. Much of the rich agricultural land in the Pacific area is still farmed on an extensive, low-technology basis and the production potential of the vast Atlantic region has hardly been touched.

Agriculture is the base of the economy. Although the share of agricultural production in total output declined from roughly one-third in 1950-52 to about one-quarter in 1970-72, agriculture continues to be the main source of employment and of export earnings and many industries and services support the agriculture sector. The structure of production is very dualistic, reflecting the highly concentrated pattern of landownership. The "traditional" sector of farms of up to 7 hectares supports about one-third of rural families, most of them without security of tenure or access to credit, extension and marketing services. The "modern", export-oriented sector of larger farms producing cotton, coffee, livestock, sugarcane and irrigated rice occupies most of the best land. Expansion of cotton and livestock activities, especially during the 1950's, often involved the displacement of small farmers producing basic grains.

Manufacturing industry, which has been the most dynamic sector of the economy, now accounts for around one-fifth of value added and is an important source of exports. The major impetus for growth of manufacturing from the demand side was the considerable growth of real incomes on the basis of expanded agricultural production. A good part of the stimulus also resulted from Nicaragua's successful promotion of beef and sugar exports to the U.S. and of industrial exports to the Central American Common Market (CACM). Food processing is by far the most important branch of industry. The growth of manufacturing production has been on the basis of relatively simple activities such as the mixing of chemicals and processing of agricultural products. The latter has been an important means of the developing internal linkages in the economy and in raising the value of exports, especially beef.

Nicaragua's post-war economic growth has been impressive but characterized by sharp cyclical changes. Real income grew at an average annual rate of 6.4 percent or 3.5 percent in per capita terms during the period 1946-1972. The strong upward trend in income resulted from the expansion of production for exports, primarily of cotton, coffee, beef and simple manufactured goods.

The distribution of income and wealth is significantly skewed. A few groups control most profitable industrial, financial and commercial ventures; the largest 2 percent of farms occupy almost one-half of the total farmland. The large income differentials between urban and rural areas have been the major propellant for urban migration, which has resulted in a rate of growth of urban population of almost five percent per year in the period 1963-71 as compared with a rate of growth of only one percent per year in the rural areas. In 1972 average income per family in Managua was 3.5 times that in the rural areas. Furthermore, average income of Managuan families in the lowest 50 percent income bracket was more than 5.5 times higher than that of the corresponding groups in the rural areas indicating a greater degree of unevenness in income distribution in rural areas as compared with Managua. The higher concentration of income in the hands of the richest in the rural sector is attributable not only to land concentration, but also to the credit and marketing facilities available to larger farmers engaged in production for export.

The socio-economic role of the General Government in the past has been limited by persistently low tax revenues and current expenditures relative to GDP. The slow growth of current expenditure -- and consequent shortage of important public services facilities such as education and health -- largely reflects budgetary stringency dictated by insufficient revenues. Public sector fixed investment has been mainly for transport and electric power. During the 1960's a good trunk road system in the Pacific area and its integration with neighboring countries was completed, and installed electric power capacity was increased five-fold. Outside the field of transport and electricity, the process of project identification and preparation in the past has been extremely limited, and overall planning practically non-existent. Some progress in all these fields can be detected after the 1972 earthquake and will be discussed below.

(iii) Recent Development and Prospects

The earthquake, which struck Managua on December 23, 1972, took a toll of about 10,000 lives, destroyed or rendered unusable practically all the central zone of the city, including most government offices, hospitals and schools, the financial and commercial buildings and perhaps 2,500 small shops engaged in small-scale manufacturing and retail trade. About 32,000 housing units, occupied by an estimated 193,000 people, were destroyed; this represented about 45 percent of the housing in the Managua area.

The cost of replacing physical assets destroyed by the earthquake was estimated in early 1973 at about $300 million. Subsequent price increases of imported as well as domestically produced construction materials and other goods have raised this amount to probably $400 million or over. Nicaragua has been successful in raising financial resources for reconstruction. External commitments (including reinsurance payments) totaling over $300 million have been obtained for this purpose; in addition, emergency taxes yielded the equivalent of about $40 million more. Except for some external financing on soft terms for the construction of streets and the municipal markets of Managua, no other external financing for reconstruction is foreseen in the near future. The resources already available together with the proceeds of new taxes which replaced emergency taxes and the normal resources of the specialized financial institutions should be sufficient to enable completion of the bulk of the reconstruction process before the end of the decade. Reconstruction of low income housing however, will probably take a longer period of time.

A recent OAS report on the progress of physical reconstruction indicates that in Managua by June 1975 education facilities, electricity (part of them provisional) and telephone connections, access roads and streets exceeded pre-earthquake levels. Water and sewerage were available to approximately the same share of the population as in 1972. Hospital facilities (which were totally wiped out by the earthquake) had attained a level of about 80 percent. In relation to commercial buildings, a number of new prefabricated shopping center complexes were already in operation. Most of these centers, however, are rather luxurious and cater to the high income minority of the population, while for the bulk of the Managuans the lack of shops at suitable locations continues to be a major problem. This problem is aggravated by the defficiency of urban transportation -- many new low income neighborhoods lack bus connections.

The impact of the earthquake on productive capacity was considerably lower than at first feared. Although some food industries and an important share of the textile and clothing industries suffered considerable damage the reconstruction process imparted strong dynamism to the construction industry to the point that its expansion nearly compensated for declines in other industries. In spite of the earthquake

GDP grew by over two percent in 1973 and it is estimated to have expanded by a further 11-12 percent in 1974. GNP per capita in 1974 is estimated to have attained a level of $630. Moreover, of the 170,000 persons displaced by the earthquake, by mid-1974 almost one half had returned to Managua. By the same time, the serious unemployment problem created by the seism, both in Managua and other main cities had been overcome and unemployment rates had fallen down to pre-earthquake levels.

Public finances were considerably strengthened after the earthquake. The emergency taxes -- 10 percent tax on exports and one month's salary of government employees -- increased the ratio of government revenues to GDP from about 10 percent in the early 1970's to 12 and 13 percent in 1973 and 1974, respectively. When the emergency taxes expired (end-1974), a new tax law was approved which, in addition to replacing revenues from the emergency taxes, is expected to add progressivity to the tax system. The tax changes, which are in full effect in mid-1975, affect the income, property, consumption and sales taxes, and represent a considerable fiscal effort for Nicaragua.

In addition to the efforts in the fiscal field some progress is noticeable in planning and project preparation in areas of particular interest to the major external lenders, i.e., rural and social development. A project for rural education has recently been prepared (and appraised by the Bank) and a project for rural water supply is being developed for Bank consideration in FY77 (see section on prospective Bank operations). In addition, the Government is proceeding with the reorganization of the agricultural public sector with AID financial and technical assistance, including the creation of a new institution (INVIERNO) which will supply credit and technical assistance to small producers in two selected regions and which will also coordinate public activities in education, health, housing and infrastructure addressed to the same target groups. The direct beneficiaries of this project are estimated at 20,000 rural poor families (6 persons per family). The recent improvements in fiscal performance, planning and project preparation are probably attributable to a combination of factors including (a) a willingness to exploit the opportunities that exist to assist the rural poor without impinging seriously on private sector interests, (b) signs of social unrest in some rural areas, and (c) a desire to attract increased resources from the external lending agencies.

During the 1970's the terms of Nicaragua's external public debt have steadily deteriorated. This is the result of increased borrowing from private financial institutions, the share of which increased from 32 percent of total debt outstanding in 1970 to over 50 percent in 1973. In 1974, it is estimated that about two-thirds of the new commitments were contracted with private sources. A considerable portion of these hard-term loans was contracted by public financial institutions, such as the Housing Bank (BAVINIC), the lending terms of which are considerably softer than commercial terms. The use of this type of foreign financing which has resulted in a negative spread, which besides placing a heavy burden on the debt servicing capacity of the country, endangers the financial institutions. Even under optimistic assumptions as to export growth and the terms of future foreign borrowing, the debt service ratio would rise from about 9 percent in 1974 to a peak of over 20 percent in 1981. While this matter is of considerable concern to the Bank, as we have made clear in recent months to General Somoza and other Government officials, an improvement in external debt management is noticeable this year. (The Government has contracted $30 million on commercial terms during 1975, as compared with about $125 million in 1974.)

In terms of economic growth, the prospects for Nicaragua will basically depend on the success of policies addressed to: a) promotion of resource-based exports: Nicaraguan wood products, fruits and vegetables and some basic grains have good prospects in external markets; b) substitution of imports which can be efficiently produced domestically e.g., corn and some processed food products; c) curbing of imports, which can be achieved in part through appropriate credit management; and d) further improvement in project preparation and external debt management to reduce reliance on commercial banks and attract more concessional funds.

(iii) Foreign Assistance and Debt

Since the Managua earthquake of December 1972, Nicaragua has borrowed a total of approximately US$400.8 million from external sources, of which US$387.6 million is repayable in foreign currency. The World Bank Group has lent US$44.5 million (of which US$20.0 was an IDA credit for reconstruction). The Inter-American Development Bank has provided US$33.1 million repayable in foreign currency and US$10.1 million repayable in local currency for reconstruction, agriculture and medical education. The Central American Bank for Economic Integration (CABEI) has lent US$19.1 million repayable in foreign currency and US$3.7 million repayable in local currency for road projects, industrial development and telecommunications. AID has lent a total of US$50.0 million for reconstruction, and other governments have lent US$5.0 million for similar activities. In addition, to meet the financing requirements of reconstruction and agricultural credit for export products, the Nicaraguan public sector has borrowed an additional US$232.6 million from commercial sources in the United States, Japan and Europe. The heavy recourse to commercial borrowing has considerably increased public debt service obligations for the remainder of the decade. We project that the debt service ratio will rise from 9 percent in 1974 to a peak of over 20 percent in 1981.

Under the December 1974 Venezuelan oil facility agreement, Nicaragua will be able to borrow up to an estimated maximum of US$17 million in 1975, and decreasing amounts in subsequent years.

Panama

POLITICAL BACKGROUND

1. Now beginning its eighth year in power, General Torrijos' Revolutionary Government is well entrenched and has the support of the middle and lower income groups and the National Guards (Panama has no army as such). His Government, which includes elements from a wide political spectrum as well as a number of able technicians, has provided a strong sense of national identity and purpose. The Revolutionary Government has largely based its appeal on rallying support for (a) a renegotiation of the 1903 Panama Canal Treaty with the United States, (b) a redistribution of political power from the Panama - Colon metropolitan axis to the hitherto neglected rural areas and (c) the cleansing of public administration to do away with alledged corrupt practices and provide a government which can show results.

2. In 1969 the old constitutional National Assembly was dissolved and political parties were banned. To provide a firmer legal base from which to renegotiate the Canal Treaty, the Revolutionary Government held a national election in 1972 for an Assembly of 505 Community Representatives. This Assembly approved a new constitution that same year, and gave General Torrijos special executive power to approve contracts and agreements for the State, conduct foreign affairs and appoint cabinet ministers. Though General Torrijos is a member of the Legislative Council which acts for the Assembly of Community Representatives when the latter is not in session (it only meets once a year) he is not President. The President is Mr. D. B. Lakas, a close friend, and the Vice President is Mr. Gerardo Gonzalez, who is left leaning.

3. Panama's main aspirations in renegotiating the Canal Treaty are to: (a) do away with the concept of perpetuity in its agreement with the United States, (b) terminate U. S. jurisdiction over Panamanian territory, (c) obtain larger income from the Canal and (d) obtain Panamanian participation in the administration and defense of the Canal and eventually have full responsibility for its operation. Negotiations have been conducted intermittently with the United States since 1968, but there are divided opinions within the U. S. Government, especially on the important issue of defense of the Canal Zone, and it does not appear likely that negotiations can be concluded in the near future. The State Department, conscious of the impact which the Canal sovereignty issue might have in the rest of Latin America, appears prepared to accomodate Panamanian aspirations, while opinions in Congress, which would have to ratify a new Treaty, are sharply divided.

4. General Torrijos, and some prominent members of his Government including Vice President Gonzalez, come from the rural areas in the west of Panama and his Government has followed a consistent policy of decentralizing political power from the metropolitan area. The Ministries of Agriculture and Public Works have been moved to provincial capitals in the west and the Government has undertaken projects to improve infrastructure as well as social services in rural areas. The regime has also taken measures that have tended to weaken the base of the wealthier metropolitan groups which controlled the government in the past. Some large land holdings were expropriated during

the early years of Revolutionary Government, and more recently a Labor Code and Rent Controls were enacted which are deemed to favor the interests of lower income groups at the expense of the business community. Relations between the Revolutionary Government and the Panamanian private sector have been cool and at times tense. The private sector has claimed that the "rules of the game" are not clear and there are insufficient assurances for investors. The Government is now seeking to reestablish the confidence of the private sector by holding frequent consultations with the business community, but it is not yet evident that the breach has been closed.

5. The Government's first term of elected office ends in 1978, and as this date approaches it may feel the need to show the results of its efforts. Failing a new agreement on the Panama Canal, the completion of large investment projects, such as the Bayano hydroelectric plant and the new Tocumen airport (both of which have been partly financed by the Bank) and the initiation of similarly large projects, could be the means by which the Revolutionary Government might seek to receive continued popular support.

THE ECONOMIC SITUATION

(Panama uses the US$ as its currency, but currency is referred to as the Balboa, (B/)).

1. Until 1973 the Panamanian economy grew rapidly --at an annual rate of over 7 percent -- relying increasingly on foreing banks credit. This growth was led by shrimp and banana exports, employment in the Panama Canal Zone, import-substituting manufacturing and, more recently, by an internationally-oriented services sector which was encouraged by Panama's use of the U. S. dollar as its currency, by liberal trade and banking regulations and by its strategic geographic location. More recently, however, growth slackened. GDP growth is estimated to have fallen to 3.5 percent in 1974 and to less than 2 percent in 1975. Causes of the decline have been both domestic and external. Major domestic causes were supply constraints affecting commodity exports (bananas and to a lesser extent shrimp) and a gradual exhaustion of the possibilities in industrial import substitution offered by the domestic market. Panama has also suffered the consequences of world recession. As traffic through the Panama Canal slackened, employment in the Canal Zone stagnated and exports of services slowed down. Higher import prices and interest rates in 1974 were fully transmitted to the open domestic economy, reducing the profitability of private investment. Private investment, especially in construction,was also affected by price control and labor benefit measures adopted by the Revolutionary Government in recent years.

2. The Government has been rapidly expanding public investment to offset the decline in private investment, create the basis for a renewal of economic growth and improve the living conditions of the rural and urban poor. It has also sought to integrate the heretofore neglected rural zones more closely to the rest of the economy. Total investment by the public sector rose from 4.6 percent of GDP in 1968 to an estimated 15.0 percent in 1975. The authorities are presently preparing a long-term public investment program which would continue these trends into the 1980's (See the Government Investment Program, D-d).

3. The growth of public savings has not kept pace with capital outlays. Although significant revenue efforts led to increases in the ratio of public sector current savings to GDP, from 1.7 percent in 1968 to over 3 percent in 1973, public investment has been almost three times as high as savings. This made it necessary to borrow heavily from official and private internal and external sources. Total Central Government debt outstanding rose from B/170 million at the end of 1968 to B/612 million at the end of 1974. Whereas 18 percent of this debt was placed with the Panamanian Social Security Institute and 12 percent was owed to the four major official lending agencies (IDB, IBRD, AID, EXIMBANK) with relatively long maturities, more than 40 percent was owed to private foreign creditors at comparatively short maturities. The large size of the Government's debt and its unfavorable term structure - over 52 percent of the Central Government's external debt will have to be repaid by 1980 -- have in turn led to mounting debt-service obligations. The ratio of Central Government debt service to current revenues reached 28.8 percent in 1972. A $15 million refinancing operation in 1973 reduced the immediate burden, but requirements will rise sharply after 1977.

4. The Government has recognized the need to increase the contribution of public savings to the financing of public investment. Accordingly, it has tightened tax administration and introduced a number of ad hoc tax measures that raised the ratio of government current revenues to GDP from 13.9 percent in 1968 to 15.4 percent in 1974. However, the Panamanian fiscal system, which is heavily dependent on specific taxes, lacks the necessary elasticity to allow revenues to expand in response to inflationary pressures and to keep pace with expenditures. The Government has also taken steps to increase rates for electricity and water supply, but further tariff and cost reduction measures will be needed to reduce the dependence of revenue-earning public agencies on Central Government capital transfers.

5. An economic mission returned from Panama on October 13, 1975. Its back-to-office report will discuss the Government's borrowing policies and the creditworthiness implications of the longterm investment program.

14. The principal sources of external financing to Panama in the past are summarized below:

Table 1: External Assistance to Panama, 1960-74
(Commitments in $ million)

	IBRD	IDB	AID
Commitments 1960-68	11.2 1/	37.2	72.2
Commitments 1969-74	100.1	85.0	140.0 2/
Power	76.0	-	-
Education and Health	-	12.4	17.0
Agriculture, Fisheries and Livestock	8.1	28.5	15.5
Industry	-	4.0	9.1
Water and Sewerage	-	21.3	36.0
Housing	-	16.6	35.2
Transport	27.2	34.5	72.5 2/
Other	-	4.9	26.9
Total	111.3	122.2	212.2

1/ Excluding $0.6 million which were cancelled.
2/ Including a $60 million grant from the U.S. Government for completion of the Darien Gap portion of the Pan-American Highway.

Both AID and IDB have lent heavily for agriculture and for social services. This pattern is likely to persist although IDB is expected to continue lending for the transportation sector and may also provide assistance for the power expansion program. To a large degree, AID and IDB concentration on agriculture and the social sectors reflects the Government's policy of directing borrowing on highly concessionary terms to those sectors while utilizing assistance received on harder terms for projects which are expected to result in more immediate economic benefits.

15. The Bank's share in Panama's publicly-guaranteed external debt outstanding and disbursed was 6.8 percent at the end of 1973 and the Bank's share of public external debt service was 3.4 percent. Its share in Panama's external debt is likely to rise to 12 percent by the end of the 1970's and its share of external public debt service would be no more than 10 percent.

3

F-3

OFFICE MEMORANDUM

TO: Mr. J. Burke Knapp DATE: December 26, 1974

FROM: A. Krieger, Acting Regional Vice-President, LAC

SUBJECT: Venezuela Agreement with Central America and Panama

1. We have obtained a copy of the agreement for economic cooperation signed December 14 between the Venezuelan Government and the Government of Costa Rica. We have been informed that virtually identical agreements were signed with the other four Central American countries and Panama. A synopsis of the Costa Rican agreement is as follows:

(a) At the end of each calendar quarter, beginning with the first quarter of 1975 and ending with the last quarter of 1980, the Venezuelan Investment Fund (VIF) will deposit in the Central Bank of Venezuela, to the order of the Central Bank of Costa Rica (CB), an amount of money determined in accordance with the terms of the agreement. The deposits will be denominated one-half in US dollars and one-half in Bolivares. They will be made against receipt of "certificates of deposit" in equal amount and currencies issued by CB in favor of VIF. The certificates of deposit will be for a term of six years, and will be at an interest "no higher" than the interest charged by the IDB on its ordinary capital resources (presently 8 percent).

(b) The deposits will be in amounts equal to the excess over six dollars of the average realization price of each barrel of oil exported in the preceding quarter to the recipient country for internal consumption. The total volume of exports, however, which can be included in the calculation in any one year cannot exceed the total volume of exports to Costa Rica for internal consumption in 1974, which "for purposes of this Agreement" is fixed at 7,300 barrels per day. 1/

(c) Beginning in 1976 (and ending in 1980), the maximum volume of exports to which the formula applies will be reduced each year by 16-2/3 percent. The VIF and CB, however, can agree to different annual reductions in the eligible volume of exports, provided that the reduction is not less than 10 percent per year.

(d) CB agrees to repay in advance to the VIF the deposits received to the extent necessary to permit the VIF to make loans and investments for "development projects and programs in Costa Rica". CB's prepayment obligation is subject to the approval of the Costa Rican Government for the proposed utilization of the deposits involved.

1/ The maximum barrels per day agreed with the other Central American countries and Panama are as follows: Guatemala, 14,800; Honduras, 11,600; El Salvador, 11,400; Nicaragua, 8,000; Panama, 13,600. It is difficult to relate these figures to actual trade data for 1974, which suggests that 1974 exports for internal consumption have been used more as a reference point for negotiations than as a precise measure of the maximum volume of eligible exports.

(e) The VIF is empowered to use the deposits received back from CB in the following manner:

i) to make loans for projects and development programs in Costa Rica;

ii) to make equity investments in companies located in Costa Rica for development projects 2/;

iii) to finance purchases in Costa Rica of goods and services required for projects and investment programs which the VIF is financing in other countries with which it has agreements similar to the present one;

iv) to pay for administrative costs of the VIF in the management of the operations covered by this agreement; and

v) for global loans in support of Costa Rican export credit programs 2/.

(f) The loans referred to in paragraph e(i) above are required to be used for projects and programs "which may receive or are receiving" other financing "particularly in foreign exchange" from IDB, including the resources of the proposed Venezuelan Trust Fund, from CABEI, from IBRD, and from such other financial institutions "of first rank" as the VIF and CB may agree. The loans "shall cover" the financing of local costs, including working capital, as well as Costa Rican participation in regional integration projects. The loans will be denominated and repayable in Bolivares. They will be for terms not exceeding 25 years with grace periods of up to six years, at an interest equal to the prevailing rate on IDB's ordinary capital loans.

2. As we interpret these agreements, the Central Bank of the recipient country will have the right to use the deposits of the "excess" oil payments for general balance of payments support until either (1) the funds are needed for the uses described in sub-paragraph (e) above or (2) the six-year term of the deposit expires. Apparently the Government can avoid the obligation of advance payment of the deposits by not agreeing to proposed uses of the funds by the VIF. One point that is not clear from the agreement is whether the loans to be made by the VIF from the proceeds of the deposits are to be used exclusively for local cost financing in cases where

2/. The agreement states that the conditions and criteria for equity investments and global loans for export credit programs will be the same as those applicable to similar operations in the Venezuelan Trust Fund established in the IDB. This Trust Fund, however, has not yet been established. The Trust Fund agreement is expected to be considered by the IDB Board in January. The provisions applicable to equity investments and export credit operations are to be included in a set of regulations being developed by IDB staff and expected to be completed by the end of January.

regional integration projects are not involved. The funds to be provided will be denominated in Bolivares, and it is likely that the language to the effect that the loans "shall cover" local costs is meant to make clear that local costs can be financed and not to preclude foreign cost financing.

3. Our preliminary estimate is that the Venezuelan agreements will provide the Central American countries and Panama with a total of approximately US$150 million in balance of payments support in 1975 and between US$500 and US$600 million for the six-year period covered by the agreements.

cc: Messrs. Cargill
Chenery
Alter (o/r)
Knox (o/r)
Escobar, Special Rep. for Inter-American Organizations
Holsen, Senior Economist, LAC I
Pfeffermann, Senior Economist, LAC I
Gonzales-Cofiño, Division Chief, LAC I
Fernandes, Division Chief, LAC I
Flood, Division Chief, LAC I

4

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: FILES

DATE: September 5, 1975

FROM: Roberto M. Fernandes, Division Chief, LAC I

SUBJECT: PANAMA: Meeting of Messrs. Lerdau and Fernandes with General Torrijos, Chief of Government

1. Messrs. Lerdau and Fernandes were received by General Torrijos on August 17, 1975 in the residence of Mr. Rodrigo Gonzalez, President of the Cerro Colorado Copper Commission. Also present were Mr. Barletta, Minister of Planning and Economic Policy; Mr. Fabrega, Director General of the State Power Company (IRHE), Mr. Villalaz, President of the Comision de Desarrollo del Bayano and Mr. Rodrigo Gonzalez.

2. After Mr. Barletta explained to General Torrijos the purpose of Mr. Lerdau's visit to Panama, Mr. Lerdau briefly mentioned the sectors for which the Bank has made loans in Panama as well as the projects which are currently under consideration by the Bank. Mr. Lerdau then said that the Bank would, in future, have to be increasingly selective in defining its lending programs given the massive demands of the poorer developing countries on limited Bank resources. He indicated that this constraint would lead the Bank to be particularly critical of its involvement in relatively high per capita income countries such as Panama. Bank lending for such countries will have to be justified on other than resource transfer grounds. The Bank would want to satisfy itself that it was achieving goals such as the establishment of sound institutions in the sectors for which it is lending.

3. General Torrijos and Mr. Barletta observed that it would be paradoxical if the Bank reduced its assistance to countries such as Panama which, after great efforts, were on the verge of achieving self-sustained economic growth. Continued Bank assistance throughout the 1970's would contribute to the Government's goal of making Panama progressively less dependent on official capital inflows in the 1980's.

4. Mr. Lerdau then mentioned the Bank's concern at the failure of IRHE to raise electricity rates so as to generate the revenues required for its expansion. General Torrijos reacted by saying that talk about increases in electricity bills was "subversive". He explained that it would be politically disastrous for the Government to authorize tariff increases prior to 1977 given the fact that recent sharp increases in the fuel costs of IRHE had been passed on to consumers. General Torrijos said that the best the Government could do at this point was to commit itself to the incorporation of the fuel savings resulting from the entry into operation of the Bayano hydroelectric project into the basic electricity rate. (Mr. Barletta subsequently assured Mr. Lerdau that the Government was committed to carrying out a 0.5% per month rate increase from January 1976 until the entry into operation of Bayano scheduled for July 1976.) Mr. Gonzalez strongly supported General Torrijos' views

and added that the increases in electricity costs over the last year had adversely affected industry, in particular dairy production. He concluded that a further increase of electricity costs would be most inoportune in the context of the economic recession which the country is experiencing.

5. Messrs. Lerdau and Fernandes said that unless electricity users were required to meet the cost of providing electricity to them, the burden would fall on the general public either through higher taxes or through deficiencies in other public services. Conversely, to the extent that public utilities such as IRHE become able to self-finance a substantial part of their investment programs, general government revenues will be released to finance non-revenue earning services such as health and education facilities for lower income groups.

6. Mr. Lerdau also observed that electricity costs normally represent a small part of industrial costs. (At a subsequent meeting with industrialists, we were told that electricity costs were on average no more than 2 to 3% of total cost of production.) As far as private consumers are concerned, Mr. Lerdau suggested that relatively high income urban consumers could well afford to pay for the real cost of producing electricity and that an appropriate tariff structure could provide for the subsidization of low income groups by wealthier consumers. Mr. Gonzalez said that he considered himself to be relatively affluent and, nevertheless, had been painfully affected by recent increases in his domestic electricity bills.

7. General Torrijos concluded the meeting on a positive note by mentioning his enthusiasm for the on-going Bank-financed livestock project. He considered that the livestock project was an example of a flexible approach that enabled assistance to be provided to small producers such as those organized in "asentamientos".

Cleared with and cc: Mr. Lerdau, Director, LAC I

cc: Messrs. Knapp
Krieger
Knox, Director, LAC Projects
Wessels, Division Chief, LAC Projects
Haasjes, Division Chief, LAC Projects

1

G. 1. b. COSTA RICA: Ongoing Projects

Costa Rica has received to date eighteen Bank loans and one IDA credit, totalling US$195.5 million, net of cancellations. The last operation, a loan for power amounting to US$41.0 million, was signed on June 16, 1975, and is expected to become effective shortly. About 85 percent of total Bank group lending to Costa Rica has been for power, telecommunications and highways, in that order.

Siquirres-Limon Highway Project

Ln 664 - April 2, 1970 -- US$15.7 million
Closing Date: December 31, 1975

The project provides the first all-weather connection between San Jose and the country's main port, Limon, which is on the Caribbean Coast, thus eliminating one of the main bottlenecks in Costa Rica's transport system. It has been now substantially completed under the direction of the Ministry of Public Works and Transport. Most of the project was completed on time, except for one bridge, which delayed the completion until October 1975 (nine months behind the original schedule). The final costs are expected to exceed the original estimate by about 20 percent. The Government has financed the additional costs out of its own resources.

Fourth Power Project

Ln 800 - February 24, 1972 -- US$6.5 million
Closing Date: June 30, 1976

The project, which is under the direction of the National Power and Telecommunication Authority (ICE), includes installation of two 15 MW gas turbines at San Antonio near San Jose, a 3 MW diesel power station, transmission facilities, and engineering studies of the power sector and ICE organization. The increased internal generating capacity was needed primarily to meet Costa Rica's power requirements during the dry season.

The project has been progressing satisfactorily. Installation of some transmission lines and substations--the only uncompleted project elements--will be delayed by up to twelve months because of changes in the borrower's program. The studies have been completed and have played an important role in finalizing ICE's expansion plans in the power sector for the rest of the decade. The expected cost of the project is substantially the same as the appraisal estimate.

Third Telecommunications Project

Ln 801 - February 24, 1972 -- US$17.5 million
Closing Date: June 30, 1977

This project, also part of the ICE program, includes expansion of the telephone network by 25,000 exchange lines, expansion of long distance and international service, and establishment of public-call offices in about 600 villages and small towns.

After some delays attributable to revisions of the project scope and late deliveries, the project is now progressing satisfactorily and is expected to be completed by December 1976, which is the original completion date. All procurement arrangements have been finalized. An estimated 18 percent overrun in the project total costs is expected, mainly due to increases in local cost elements.

Second Agricultural Credit Project

Ln 827 - June 5, 1972 -- US$9.0 million
Closing Date: December 31, 1976

Originally, most of the proceeds of this loan to the Banco Central de Costa Rica were to be made available through four commercial banks for livestock and crops, with only minor amounts for agroindustry, forestry and technical services. The latter project element was designed to strengthen the Project Implementation Unit within the Central Bank with a view to eventually also strengthening the project development and evaluation capacity of the participating commercial banks, which are actually dealing with the ultimate borrowers.

About 80 percent of the loan amount has now been committed as originally scheduled; however, the disbursements are lagging, and Bank supervision has been stepped up. As in the case of the preceding loan for agricultural credit, lending for livestock has surpassed appraisal estimates. So far about 67 percent of all funds committed have gone to livestock and about 5 percent to crops, compared with an expected distribution of 44 and 42% respectively. Loans for agroindustry have amounted to almost 30 percent of funds committed, compared with 6 percent estimated at appraisal.

In view of rapid commitments under this loan, the Central Bank made a request for a third agricultural credit. The project was appraised in May 1974. Unwilling to modify its policy of highly subsidized interest rates, the Central Bank subsequently requested that further consideration of this project by the Bank be postponed indefinitely.

Highway Studies Project

Ln 872 - December 26, 1972 -- US$1.4 million
Closing Date: December 31, 1975

This engineering creidt with the Ministry of Public Works and Transport involves detailed engineering studies for the proposed San Jose-Siquirres and Rio Sucio-Puerto Viejo highways. (A $39.0 million loan for this project to be negotiated shortly.) The studies have been completed (about five months behind the schedule) at a cost approximately the same as the appraisal estimate.

Education Project

In 915 - June 25, 1973 -- US$6.2 million
Total Cost -- US$9.4 million
Closing Date: December 31, 1978

This project with the Ministry of Public Works and Transport in cooperation with the Ministry of Education and the National Vocational Training Institute--INA--is designed to assist the Government in implementing the 1974-78 National Plan for Education Development, the objectives of which include (i) redressal of imbalance in educational opportunities throughout the country; (ii) more emphasis in secondary school curricula to science, industrial arts and home science (including family planning); and (iii) improvement and decentralization of vocational training, particularly in agriculture-related occupations. The project provides for construction and equipment of 6 rural lower secondary schools, workshop and laboratory facilities for 25 existing lower secondary schools, and five vocational training centers.

The project is about 20 months behind schedule--partly because of the delay in Congressional ratification of the Loan Agreement, and partly because of institutional/administrative problems. These include a project unit with inadequate authority, a weak project director, and an insufficient budget for counterpart funds at certain times. During the past six months, progress has been made on some aspects including: (a) preparation of a revised project implementation schedule and capital cost estimates; (b) drafting of master furniture and equipment lists, and (c) selection of two consultant design firms for specific project subcomponents.

The institutional/administrative difficulties concerning the project unit and its director continue to be the main problem affecting project implementation. Another increasing problem, however, is cost escalation of 50 percent. This will make necessary a reduction in project scope; discussions are currently underway concerning the most appropriate areas for making such cuts.

The project which was recently designated as a problem project for regional review, is under intensive supervision by the Projects Department.

Fourth Telecommunicationa Project

Ln 1006 - June 14, 1974 -- US$23.5 million
Total Cost -- US$50.8 million
Closing Date: December 31, 1978

This ICE project consists primarily of expanding: (i) the telephone network capacity by 56,300 exchange lines; (ii) the long-distance network capacity by 2,500 trunk circuits; (iii) the rural telephone system to serve 90 additional rural communities. Like the three previous telecommunication projects, it is designed to accomodate rapidly growing demand (over the past decade the number of connected subscribers was on average growing at about 18 percent p.a.) and to further expand the communications coverage of the rural areas. This and the preceding project will together provide a total of 700 isolated localities with a communication link with the rest of the country.

The project is progressing satisfactorily, and more than US$10.0 million has already been committed. No cost overruns or delays in implementation are envisaged at this time.

Fifth Power Project

In 1126 - June 16, 1975 -- US$41.0 million
Total Cost -- US$70.4 million
Closing Date: June 30, 1979

The project is a part of ICE's 1975-78 expansion program, currently estimated to cost $210-220 million. It is being financed jointly by IBRD ($41 million), IDB ($50.5 million), CABEI ($13.5 million) and Venezuela ($24 million--from the Venezuelan oil-facility). The Bank project would provide one 30 MW and one 32 MW additional hydro generating units for the existing plants, a 30 MW diesel generating plant and extensive transmission and distribution facilities.

The loan is expected to become effective shortly. The orders for the additional hydro generating units have already been placed. In addition, the works on the IDB-financed Arenal hydro project (135 MW), which is the major item in the 1975-78 expansion program, are progressing satisfactorily.

G. 1. d. COSTA RICA: Future Projects

FY76

Fourth Highway Project

Estimated Cost -- US$71.3 million
Proposed Loan -- US$39.0 million
Board Date -- December 16, 1975

The project would provide for construction under the Ministry of Public Works and Transport of a highway from San Jose to Siquirres, which would link up with the Bank-financed Siquirres-Limon highway (Ln. 664-CR). The existing road link between San Jose and Siquirres is already congested at some points and will be increasingly inadequate for handling the rapidly growing traffic between San Jose and Siquirres (which is half-way between San Jose and Limon, Costa Rica's main port). The future road to Sqiuirres will go by a completely new route, thus opening new land for more intensive exploitation. The project will also include a sizable technical assistance component with a view to (i) strengthening the overall transport sector planning and international coordination; and (ii) preparing detailed engineering studies for a proposed urban transport project. Some delay has been experienced in completing the processing of the project. Because of recent increases in the project cost estimate, the proposed Bank loan will fall US$10 million short of the estimated total foreign cost element. The Government has sought to fill the gap through borrowing from CABEI. The latter institution, however, has indicated that it will be difficult to consider this proposal for a number of months. We are currently completing an analysis of Costa Rica's balance of payments and fiscal situation which we believe will show that it would be reasonable to go forward with the project on the basis of the commitment we have received from the Government to provide the balance of the required funds from its own resources.

FY77

Urban Transport Project

Estimated Cost -- up to US$20.0 million
Proposed Loan -- US$10.0 million
Board Date -- End-FY77

The Bank served as the executing agency for a UNDP-financed transport study of the metropolitan area of San Jose. This was recently completed successfully and a number of priorities for traffic and transport planning, control and regulation have been developed. The Ministry of Public Works and Transport intends to hire expatriate experts (to be financed through the above-mentioned Fourth Highway Project) who would within the next two years work on detailed preparation of a projection table for Bank financing, whose main objectives would be (i) more efficient public transport facilities, (ii) better traffic management in the Metropolitan area, (iii) faster transti traffic, and (iv) reduction of environmental hazards in the central area of the city due to congested traffic.

FY78

Agricultural Credit (Small Farm)

Estimated Cost -- up to US$10.0 million
Proposed Loan -- US$5.0 million
Board Date -- FY78

This project would finance, through the Banco Central de Costa Rica and the nationalized commercial banks, modernization of small farms (up to 5-10 ha) engaged in dairying and cultivation of various cash crops, fruits and vegetables. The Central Bank is expected to present a request for this project in the course of 1976.

Development Finance Companies

Estimated Cost -- up to US$20-25 million
Proposed Loan -- US$15.0 million

An Industrial Sector Mission visited Costa Rica in October 1975 with a view to identifying suitable areas for Bank financing.

FY78/81

Aluminum Enclave Project

Estimated Cost -- US$1,500 million
Proposed Loan -- (Hydro-FY78) -- US$75.0 million
(Smelter-FY81) -- US$25.0 million

This project, which would be run by ICE (National Power Authority) in joint venture with a foreign metal processing company, would involve a hydro power complex at Boruca with up to 200 MW firm generating capacity catering to an aluminum smelter of up to 100,000 short tons capacity p.a.

Costa Rica has for the last five years actively sought to develop mining of bauxite and fabrication of aluminum for which it would also supply the necessary power. In 1970 ALCOA was granted concession for exploitation of local bauxite with a view to supplying an aluminum smelter at San Isidro del General to which, in turn, Costa Rica would supply power from the proposed hydro complex of Boruca. Engineering and economic analysis of the project was carried out over the course of five years at a cost of over $1 million, and the Bank was frequently consulted in the process. This study indicated that mining operations in Costa Rica would be uneconomical (low quality bauxite) and that a viable project would consist of a smelter operating on imported aluminum oxide (US$604 million) and a power plant (US$870 million) with the related infrastructure (US$58 million), a total capital cost of US$1,532 million. Faced with these capital requirements, and given the current rather unexciting market outlook for primary aluminum, ALCOA stated in September 1975 that it could not raise the necessary capital and agreed to return the mining concession. In this situation the National Aluminum Committion, which has been coordinating the project preparations and negotiating with ALCOA, decided to consider scaling down the hydro complex from 565 to about

200 MW firm capacity (estimated cost $250-300 million). Such a hydro complex would cater to a much smaller aluminum smelter, costing about US$250-300 million. Although no firm arrangements have been set for project implementation, ALCOA has shown an interest in pursuing discussions with Costa Ricans once the additional engineering and economic feasibility investigations now underway are completed.

As the $100 million of Bank lending now proposed was determined on the basis of minimum feasible Bank participation in a $1,500 million project, we would propose a lesser amount of Bank financing if the smaller project proves feasible.

2

THE STATUS OF BANK GROUP OPERATIONS IN EL SALVADOR

A. STATEMENT OF BANK LOANS AND IDA CREDITS
(as of September 30, 1974)

Loan or Credit Number	Year	Borrower	Purpose	Amount (less cancellations) Bank	IDA	Undisbursed
22	1949	Comisión del Río Lempa	Power	12.5	-	
104	1954	Government	Roads	11.1	-	
216	1959	Government	Roads	5.0	-	
221	1959	Comisión del Río Lempa	Power	2.7	-	
263	1960	Comisión del Río Lempa	Power	3.5	-	
31	1962	Government	Roads	-	8.0	
342	1963	Comisión del Río Lempa	Power	5.9	-	
358	1963	Administración Nacional de Telecomunicaciones (ANTEL)	Communi-cations	9.5	-	
521	1967	Government	Roads	2.8	-	
609	1969	Government	Education	4.9	-	2.1
227	1971	Government	Power	-	5.6	
811	1972	ANTEL	Communi-cations	9.5	-	8.7
889	1973	Comisión del Río Lempa	Power	27.3	-	21.7
1007	1974	Government	Education	17.0		17.0
			Total	111.7	13.6	49.5
		Total (less cancellations) of which has been repaid		35.7	.2	
		Total now outstanding		76.0	13.4	
		Amount sold 4.1 of which has been repaid 3.9		.2	-	
		Total now held by Bank and IDA[1]		75.8	13.4	
		Total undisbursed				49.5

B. STATEMENT OF IFC INVESTMENTS
(as of September 30, 1974)

Year	Obligor	Amount in $ million Loan	Equity	Total
1959	Industrias Textiles, S. A.	0.14	-	0.14
1969	Hoteles de Centro América, S. A.	0.60	0.23	0.83
	Total	0.74	0.23	0.97
	less sold or repaid	0.17		0.17
	Now held	0.57	0.23	0.80

1/ Prior to exchange adjustments.

INTERNATIONAL FINANCE CORPORATION
Summary of Investments held in
El Salvador - As of August 31, 1975
(millions of US$)

	Loan	Equity	Total
Commitments:			
Industrias Textiles, S.A.	$ .14	$ -	$ .14
Hoteles de Centro America, S.A.	.60	.33	.93
	.74	.33	1.07
Repayments Sales and cancellations	.25	.10	.35
Net Investment Held by IFC	.49	.23	.72
Undisbursed	-	-	-

G. 2. b. EL SALVADOR: Ongoing Projects

Telecommunications

Ln 811: April 7, 1972 -- US$9.5 million
Closing Date: December 31, 1976

This project provides for the installation of 18,000 lines of automatic telephone exchange equipment, 14,500 additional telephone exchange connections, 750 additional long distance circuits, and consulting services to help prepare the 1976-80 program. The project is proceeding satisfactorily, though the selection of consultants has been delayed. Consultants are expected to begin work in November 1975, and their final report is expected in August 1976. The preliminary report will outline the next telecommunications project.

Power VI

Ln 889: April 27, 1973 -- US$27.3 million
Closing Date: April 30, 1978

This project helped CEL, the national power company, construct a geothermal plant at Ahuachapan, including a 30 MW turbo-generator, a canal to the Pacific to discharge geothermal effluent, construction of the 67.5 MW Cerron Grande hydroelectric project (in which IDB is also participating), a telemetering center, and consulting services and training of staff.

With the exception of the canal to the Pacific, the project is substantially on or slightly ahead of schedule. However, the estimated two-year delay in completing the canal to the Pacific has increased the levels of arsenic and boron in the Rio Paz, which is already naturally contaminated. As the river is the boundary between El Salvador and Guatemala, the latter has protested to the Bank. The Bank requested PAHO to study the matter and make recommendations on a toxic level which could be tolerated safely. PAHO's report is being considered in the Bank prior to its transmittal to El Salvador and Guatemala.

Education II

Ln 1007: June 14, 1974 -- US$17 million
Closing Date: December 31, 1978

The project will provide basic education to rural areas, expand teacher training capacity, replace basic education schools, help introduce the General Basic Education Curriculum in urban and rural areas, and establish a non-formal rural training program. In all, the project affects over 330 schools, some 55,000 students, 249 workshops, and laboratories and staff housing in rural areas.

The project is about four months behind schedule, mainly because of delays in procurement and delays in decisions regarding staff housing. However, recent reports indicate that the Government is now going foward with staff housing construction. With adequate effort by the Government, the project could be brought back on schedule fairly soon. Requests for disbursements, however, have been extremely slow in coming to the Bank.

Sites and Services Project

Ln 1050 - November 14, 1974 -- US$2.5 million
Cr 517 - November 14, 1974 -- US$6.0 million
Closing Date: May 31, 1981

This project is being administered by a Salvadorean private foundation, to which the Government has made available the proceeds of the loan and credit. The project is designed to enable households to acquire developed lots and construct houses on them, and to provide infrastructure and core units for self-help housing, essential community facilities, and a pilot fund for small cooperative enterprises.

The project is substantially on schedule--there are some delays in making water available to service sites, but the Government has recently made funds available to the Water Authority for this and other project-related purposes. The private foundation is proving to be a highly competent project administrator, and their work is beginning to attract attention as a model not only for El Salvador but also for other parts of the world.

Population: 3.7 m (1973), 3.5% p.a.
Per Cap GNP: $340 (1974 Atlas), 1965-72, 1.2%
Area: 20,900 sq. Km.
Literacy: 58% adult population

EL SALVADOR - REVISED OPERATIONS AND LENDING PROGRAM
($ millions)

		FY75	FY76	FY77	FY78	FY79	FY80	FY76-80
Sites and Services	IBRD	2.5						
	IDA	6.0						
Sites & Services-II	IBRD				11.0			
Telecommunications III	IBRD			14.0				
Telecommunications IV	IBRD					14.0		
Education III	IBRD/IDA			20.0				
Education IV	IBRD						25.0*	
Nutrition - Population	IBRD				6.0			
Power VI	IBRD		40.0 1/					
Power VII	IBRD					22.0		
DFC I - INSAFI	IBRD						10.0*	
Operations Program	IBRD		40.0	34.0	17.0	36.0	35.0	156.0
	IDA		-	6.0	-	-	-	6.0
	Total		40.0	34.0	17.0	36.0	35.0	162.0
	Number		1	2	2	2	2	9
Lending Program	IBRD	2.5	40.0	14.0	11.0	14.0	10.0	89.0
	IDA	6.0	-	6.0	-	-	-	6.0
	Total	8.5	40.0	20.0	11.0	14.0	10.0	95.0
	Number	1	1	1	1	1	1	5
Commitment Deflator (FY74$)		141.9	150.4	158.4	166.4	174.7	183.5	
Real Lending		6.0	26.6	12.6	6.6	8.0	5.5	59.3

* New Project
1/ Transfered to FY77 Standby in 10/75 Lending Program review.

Division 1B- Latin America & the Caribbean
July 7, 1975

G. 2. d. EL SALVADOR: Future Projects

FY76

Power VII

Proposed Loan: US$40 million
Board Date: FY76

This was to have been the San Lorenzo hydroelectric project; however, the Electricity Authority (CEL) has decided to postpone this project and instead, to advance construction of a third geothermal unit at Ahuachapan, together with communication equipment and transmission facilities. Subject to agreement with CEL and the Government on the handling of geothermal effluent from Ahuachapan units 1 and 2, appraisal is scheduled for November. This project has been tentatively proposed for up to US$12 million of Third Window financing.

FY77

Telecommunications III

This project, which slipped from FY1976, is now being prepared by consultants. The composition of the project is not yet known.

Education III

This project is to be prepared by UNESCO in December. It will continue the expansion of rural education undertaken in the Second Education Project and will probably include a vocational training element.

FY78

Nutrition

A mission visited El Salvador early in October to discuss a possible nutrition/population project. The Government indicated that because of intensive involvement of other agencies in the population field they would like the Bank to concentrate exclusively on nutrition. The Agricultural and Rural Development Department is considering this request.

Sites and Services

This would be a second stage of the Sites and Services project being implemented with considerable success by a private foundation. It may also include a squatter upgrading element being studied under a recently signed UNDP urban development project.

FY79/80

Industrial Development

We hope to add to the program a DFC project for medium and small industry. The composition of the project is pending the results of an industrial survey mission just back from El Salvador.

3

G.3.a
p.1

GUATEMALA

Statement of Bank Loans
(As at August 31, 1975)
Net of Cancellations

Loan No.	Year	Borrower	Purpose	Amount (millions) Total	Undisbursed
Three loans fully disbursed				40.2	-
576	1968	Government	Education	6.3	0.1
722	1971	Government	Livestock	4.0	2.2
792	1971	GUATEL	Telecommunications	16.0	5.9
1104 *	1975	GUATEL	Telecommunications	26.0	26.0
Total				92.5	
of which has been repaid				20.8	
Total now outstanding				71.7	
Amount sold			3.5		
of which has been repaid			2.8	0.7	
				71.0	
Total undisbursed					34.2

*Not yet effective

G.3.a
p. 2

INTERNATIONAL FINANCE CORPORATION
Summary of Investments held in
Guatemala - As of August 31, 1975
(millions of US$)

	Loan	Equity	Total
Commitments:			
Industria Harinera Guatemalteca, S.A.	$ .20	$ -	$ .20
Exploraciones y Explotaciones Mineras Izabal, S.A.	15.00	-	15.00
	15.20	-	15.20
Repayments, Sales and Cancellations	.20	-	.20
Net Investment Held by IFC	15.00	-	15.00
Undisbursed	15.00	-	15.00

G. 3. b. GUATEMALA: Ongoing Projects

Education Project

Ln 576 - December 16, 1968 -- US$6.3 million
Closing Date: July 31, 1975

The project consists of constructing and furnishing a secondary teacher training school, expanding the existing Technical Institute of Agriculture, and constructing fifteen new secondary schools. The project had a two-and-a-half-year delay, but a project closing mission is now scheduled for December 7, 1975.

Livestock Project

Ln 722 - February 10, 1971 -- US$4 million
Closing Date: December 31, 1976

The project provides credit facilities and technical assistance for the improvement of pasture production and herd management methods to increase the number of slaughter stock available for sale. It is experiencing substantial delays due to lack of interest by the authorities, which is reflected in sub-loan processing delays, poor project management, and lack of incentive for private banks to participate.

Telecommunications Project

Ln 792 - January 5, 1972 -- US$16 million
Closing Date: December 31, 1976

The project consists of: (1) the expansion of local telephone exchanges, cable networks, and distribution facilities to provide approximately 35,000 additional direct exchange lines; and (2) the expansion of long-distance facilities by microwave, coaxial and UF cable, and VHF/UHF radio to provide about 560 trunk channels. There were initial delays, caused mainly by procurement problems, and some components of the project will be finished 21 months behind schedule. The project is now progressing satisfactorily.

Second Telecommunications Project

Ln 1104 - April 29, 1975 -- US$26 million
Closing Date: June 30, 1979

The project consists of the first phase of the Borrower's 1975-1981 Development Program for modernization and expansion of telecommunications services. The program includes: expansion of local telephone exchange switching equipment (82,900 exchange lines); construction of cable networks, distribution facilities and buildings, to provide at least 60,000 additional direct exchange lines;

expansion of long-distance facilities by microwave, VHF/UHF radio to provide about 722 trunk channels; expansion of capacity of the international telephone exchange; improvement and extension of the rural telephone system to about 86 locations; expansion of the telex network; and expansion of the borrower's training facilities.

G. 3. d. GUATEMALA: Future Projects

FY76

Second Education Project

Estimated Cost - US$21.6 million
Proposed Loan - US$14 million
Board Date: December 1975

The project has been appraised and is scheduled for Board presentation in December 1975. It will have the following components: (1) eleven new and three renovated lower secondary schools, (2) two new and one renovated combined upper and lower secondary schools, (3) two new common facilities centers, (4) a new agricultural training institute, (5) equipment, (6) extensive training programs for teaching and administrative staff, and (7) pre-investment studies to survey existing educational resources and to determine priority needs in education.

FY77

Agricultural Credit Project

Proposed Loan - US$10 million
Board Date: May 1977

The project will be a credit operation to provide financial assistance to the small farmers, especially those organized in agricultural cooperatives. The Government is currently preparing a document which will propose components for inclusion in this project. An FAO/CP Identification mission is scheduled for November 15, 1975 and an appraisal mission for September 1976.

Power III (Aguacapa) Project

Estimated Cost - US$65 million
Proposed Loan - US$35 million
Board Date: September 1976

Development of the electric power sector in Guatemala has not kept pace with the rapidly growing demand of industry, commerce and agriculture. This project, which is the first in a program designed to develop Guatemala's hydroelectric potential, will have a 90 MW generating capacity. An appraisal mission is scheduled for January 1976.

FY78

Power IV (Chixoy) Project

Estimated Cost - US$280 million
Proposed Loan - US$65 million
Board Date: FY78

The first stage of this project will have a generating capacity of about 230 MW. In addition to the Bank, IDB, CABEI, private banks and possibly the Venezuelan Development Fund, will be participating in its financing.

Roads II Project

Proposed Loan - US$15 million
Board Date: FY78

This project will consist of feeder and secondary roads. At present, a sector mission is in the field reviewing the Government's initial request and identifying roads which could be included.

Population:[1] 5.18 m; 2.1% p.a.
Per Cap. GNP: 520 (1973)[2]; 4.0% p.a. 1974-78
Area: 108,900 Km^2
Literacy: 46.5 adult pop. (1973)

Attachment I

GUATEMALA: ACTUAL AND PROPOSED LENDING THROUGH FY80

(US$ million)

		Through	Actual						Current	Program					Total	Total	Total	Total
		FY68	FY69	FY70	FY71	FY72	FY73	FY74	FY75	FY76	FY77	FY78	FY79	FY80	FY69-73	FY74-78	FY75-79	FY76-80
Livestock I	IBRD				4.0													
Agricultural Credit	IBRD										10.0							
Rural Development I (unidentified)	IBRD												10.0					
Communications I	IBRD					16.0												
Communications II	IBRD								26.0									
Communications III	IBRD											20.0						
Education I	IBRD		6.3															
Education II	IBRD									15.0*/								
Education III	IBRD												25.0*/					
Highways I	IBRD	18.2																
Roads II	IBRD											15.0						
Roads III	IBRD													20.0				
Pacific Port	IBRD													25.0				
Power I (Jutun-Mauala)	IBRD	15.0																
Power II (Escuintla)	IBRD	7.0																
Power III (Aguacapa)	IBRD										35.0							
Power IV (Chixoy)	IBRD											65.0						
Sites and Services	IBRD												15.0*/					
Operations Program	IBRD								26.0	15.0	45.0	100.0	50.0	45.0		30 m p a	236.0	255.0
	IDA																	
	TOTAL	—	—	—	—	—	—	—	26.0	15.0	45.0	100.0	50.0	45.0			236.0	255.0
	Number								1	1	2	3	3	2			10	11
Lending Program	IBRD	40.2	6.3		4.0	16.0			26.0	15.0	35.0	75.0	20.0	25.0	26.3	151.0	171.0	170.0
	IDA																	
	TOTAL	40.2	6.3	—	4.0	16.0	—	—	26.0	15.0	35.0	75.0	20.0	25.0	26.3	151.0	171.0	170.0
	Number	3	1		1	1			1	1	1	2	1	1	3	5	6	6
Commitment Deflator (FY74 $)			78.6	87.8	98.8	110.7	122.4	132.7	141.9	150.4	158.4	166.4	174.7	183.5				
Real Lending			8.0		4.0	14.5			18.3	10.0	22.1	45.1	11.4	13.6	26.5	95.5	106.9	102.2
(Commitments of Other Capital, CY)																		
Multilateral		n.a.	3.2	1.8	4.5	6.9	12.7	25.2	24.0	26.0	90.0	35.0	50.0	60.0	29.1	200.2	225.0	261.0
Bilateral		n.a.	0.6	25.1	11.5	--	4.7	--	10.0	10.0	13.0	13.0	15.0	15.0	41.9	46.0	61.0	66.0
Other sources		n.a.	13.2	22.9	10.0	18.3	2.7	--	--	--	--	--	--	--	67.1	--	--	--
IBRD o/s[3] incl. undisb.		26.7	31.2	29.3	32.2	49.7[4]	53.6[5]	51.7[6]	77.3	91.4	130.0	203.2	251.0	272.2				
excl. undisb.		7.5	10.4	12.0	15.7	21.1[4]	30.7[5]	33.9[6]	40.9	49.2	59.5	77.4	105.1	136.3				
IBRD Gross Disbursements		21.0	4.7	3.5	4.8	3.2	6.5	5.0	7.5	9.2	11.7	19.7	29.8	35.0	22.7	53.1	77.9	105.4
Less: Amortization		13.5	1.8	1.9	1.1	0.5	0.8	0.6	0.4	0.9	1.4	1.8	2.2	3.8	6.1	5.1	6.7	10.1
Equals: Net Disb.		7.5	2.9	1.6	3.7	2.7	5.7	4.4	7.1	8.3	10.3	17.9	27.6	31.2	16.6	48.0	77.3	112.9
Less: Interest & Charges		6.5	0.4	0.7	0.9	1.2	2.0	1.7	2.4	3.2	4.0	5.3	7.5	10.1	5.2	16.6	22.4	30.1
Equals: Net Transfers		1.0	2.5	0.9	2.8	1.5	3.7	2.7	4.7	5.1	6.3	12.6	20.1	21.1	11.4	31.4	48.8	65.2
Total Net Disbursements (Bank and Other, CY)[7]			0.1	16.4	2.1	-2.7	10.5	21.9	21.7	26.8	58.1	87.0	114.3	134.7	26.4	215.5	307.9	420.9

1/ Mid-1973.
2/ Market prices, World Atlas technique.
3/ As of end of fiscal year.
4/ The exchange adjustment of $2.7 million, as of June 1972, has been included in these figures.
5/ The exchange adjustment of $6.6 million, as of June 1973, has been included in these figures, with an increase of $3.9 million since FY1972.
6/ The exchange adjustment of $5.4 million, as of June 1974, has been included in these figures, with a decrease of $1.2 million since FY1973.
7/ Net of Amortization.

Note: All data in this table reflect o/s amounts and transactions of loans sold to third parties.

* New projects.

4

HONDURAS

Statement of Bank Loans and IDA Credits
(As at August 31, 1975)
Net of Cancellations

Loan/Credit No.	Year	Borrower	Purpose	Amount (millions) Bank	IDA	Undisbursed
Thirteen loans and credits fully disbursed				46.6	26.5	-
692	1970	Government	Power	5.5	-	0.1
767	1971	Emp. Nacional Portuaria	Ports	6.0	-	2.3
767**	1975	Emp. Nacional Portuaria	Ports	3.0	-	3.0
841	1972	ENEE	Power	12.3	-	3.9
896	1973	Government	Roads	18.8	-	14.4
434*	1973	Government	Livestock	-	6.6	5.1
452	1974	Government	Education	-	3.0	2.6
954	1974	Government	Education	3.0	-	3.0
1081	1975	ENEE	Power	35.0	-	34.8
Total				130.2	36.1	
of which has been repaid				17.0	0.4	
Total now outstanding				113.2	35.7	
Amount sold			2.6			
of which has been repaid			2.5	0.1	-	
Total held by Bank & IDA				113.1	35.7	
Total undisbursed						69.2

* Includes exchange adjustment

** Supplemental loan

INTERNATIONAL FINANCE CORPORATION
Summary of Investments held in
Honduras - As of August 31, 1975
(millions of US$)

	Loan	Equity	Total
Commitments:			
Empresa de Curtidos Centro Americana, S.A.	$ .30	$ .08	$ .38
Compania Pino Celulosa de Centro America, S.A.	-	.08	.08
	.30	.16	.46
Repayments, Sales and Cancellations	.30	.16	.46
Net Investment Held by IFC	-	-	-
Undisbursed	-	-	-

G. 4. b. HONDURAS: Ongoing Projects

Second Port Project

Ln. 676 - US$6.0 million -- June 25, 1971
Ln. 676 - US$3.0 million (supplement)-- July 30, 1975
Closing Date -- June 30, 1977
Original Estimated Cost --

The project consists of expanding Puerto Cortes on the North Coast of Honduras, and constructing the new port of Henecan in the South. This latter component was delayed almost three years as a result of Government reconsideration of the location of the South Coast port. Progress was good on the expansion of Puerto Cortes, and it was completed in March 1975. A supplemental loan of US$3.0 million was made to cover cost increases on the Henecan port; construction of this port has now begun and should be completed early in 1977.

Fifth Power Project

Ln. 841 - US$12.3 million -- June 28, 1972
Closing Date -- June 30, 1976
Original Estimated Cost --

The Honduras-Nicaragua interconnection line, a principal element of this project, should be completed shortly, but was delayed by about one year because of delays in negotiating a contract (signed in May 1973) with Empresa Nacional de Luz y Fuerza (ENALUF), the Nicaraguan utility. Other elements of this project, including extensions to the new areas, the 26 MW La Ceiba diesel plant, consulting services, and training, have either been completed or are proceeding on schedule.

Sixth Highway Project

Ln. 896 -- US$18.8 million -- May 30, 1973
Closing Date -- June 30, 1977
Original Estimated Cost --

The main component of this project, construction of the Tegucigalpa-Talanga highway, is now over 50 percent complete and should be finished by September 1976. Engineering studies of feeder roads to complement the highway are also underway.

Second Livestock Project

Cr. 434 -- US$6.6 million -- October 29, 1973
Closing Date -- June 30, 1979
Original Estimated Cost --

This project, which provides financing for livestock development, became effective January 18, 1974. About 45 percent of loan funds are now committed to sub-borrowers. Commitments and disbursements are somewhat behind schedule; however, the Central Bank is taking action to speed them up in preparation for a third livestock/agricultural development credit, which is now being appraised for FY-76.

First Education Project

Ln. 954 -- US$3.0 million -- January 9, 1974
Cr. 452 -- US$3.0 million -- January 9, 1974
Closing Date --June 30, 1978
Original Estimated Cost --

The loan and credit became effective on April 8, 1974. The project is proceeding normally. Plans for teacher training, vocational education and agricultural training facilities have been completed and construction is now beginning.

Sixth Power Project

Ln. 1081 -- US$35.0 million -- January 27, 1975
Closing Date -- December 31, 1979
Original Estimated Cost --

This loan became effective on May 5, 1975, and construction is now underway. It will finance the 40 MW third stage of the Lake Yojoa-Rio Lindo hydro development, the construction of distribution system improvements, and extension of electricity supply to rural areas.

Population 2.8 m (mid-73); 3.5% p.a.
Cap. Inc.: $304 (1973); 1.4% p.a. 1973-77
a: 115,200 sq. km.
Literacy: 50% adult population

HONDURAS - UPDATED OPERATIONS AND LENDING PROGRAM
($ millions)

		FY75	FY76	FY77	FY78	FY79	FY80	Total FY76-80	Reserve Projects 1/
Rural Development I	IDA				6.0				
Rural Development II	IBRD						8.0		
Agr. Credit III	IDA		9.0						
Agr. Credit IV	IBRD								10.0 (FY79)
Power VI (Rio Lindo)	IBRD	35.0							
Power VII (El Cajón)	IBRD			75.0					
Ports II (Supplement)	IBRD		3.0						
Ports III	IBRD				10.0(s)				
Ports IV	IBRD								15.0 (FY80)
Highway VII	IBRD/IDA			30.0					
Highway VIII (Feeder Roads)	IBRD					7.0			
Industry I (Olancho)	IBRD								30.0 (FY77)
Tourism I	IBRD				10.0				
Education II	IBRD					8.0(s)			
Education III	IBRD								10.0 (FY80)
LENDING PROGRAM	IDA	-	9.0	7.0	-	-	-	16.0	4
	IBRD	35.0	3.0	98.0	26.0	15.0	8.0	150.0	35 m pa
	Total	35.0	12.0	105.0	26.0	15.0	8.0	166.0	
	No.	1	1*	2	3	2	1	9	

1/ Projects in this category are not yet part of the approved Lending Program. Manpower for these projects is authorized for pre-appraisal purposes. These are projects which may be included in the approved Lending Program as a result of deferral or droppage of other projects or because of availability of additional resources.

(s) Projects annotated with an (s) are "advanced projects" the preparation schedules of which will be such as to permit Board presentation in the preceding fiscal year if desirable as a result of the slippage of other projects or the availability of additional funds.

* The Port Supplement loan has not been counted as an individual operation.

G. 4. d. HONDURAS: Future Projects

FY-76

Livestock III

Proposed Credit -- US$9.0 million

Continuation of financing for livestock development, and credit for commercial agricultural crops and agro-industry development.

FY-77

Highway VII (Talanga-Juticalpa)

Proposed Loan -- US$30.0 million

Reconstruction of the Talanga-Juticalpa road (120 Km) and the Juticalpa-Catacamas road (40 Km); the purchase of maintenance equipment, and the provision of consulting services for transport planning.

Ports III

Proposed Loan -- US$10.0 million

Construction of Puerto Castilla (the proposed port of exit for products from the pulp and paper project described below), and improvement of other ports.

Power VII (El Cajón Hydroelectric)

Proposed Loan -- US$75.0 million - Total Estimated Cost: $360.0 m.

Construction of an arch dam with a 450 MW generating capacity. Part of the power produced would be sold to Nicaragua in the 1980's. In addition to a Bank loan, it would be financed by the IDB, the Central American Bank, proceeds from the Venezuelan Oil Facility and suppliers' credits.

FY-78

Industry I (Pulp and Paper)

Proposed Loan - US$30.0 million
Total Estimated Cost: US$350.0 million

Development of an integrated pulp and paper sawmill operation, and two satellite sawmills to begin exploitation of Honduras' large pine forest reserves. It would be financed principally by private investors, the IDB and possibly Venezuela. This project has been included in the Lending Program as a "Reserve Project" and the Bank would participate only if another project were deleted from the FY76-80 Program.

Rural Development I

Proposed Loan - US$8.0 million

We are now beginning to explore, with assistance from the FAO/IBRD Cooperative Program, the feasibility of a rural development project in the southern (Choluteca) area of Honduras where substantial agrarian reform activity has taken place.

5

NICARAGUA

Statement of Bank Loans and IDA Credits
(As at August 31, 1975)
Net of Cancellations

Loan/Credit No.	Year	Borrower	Purpose		Amount (millions) Bank	IDA *	Undisbursed
Fifteen loans and credits fully disbursed					55.9	3.6	-
532	1968	Government	Education		4.0	-	1.0
808	1972	Emp. Aguadora de Managua	Water Supply		6.9	-	2.6
840	1972	Emp. Nacional de Luz & Fuerza	Power		24.0	-	14.5
943	1973	Banco Central	Agriculture		8.5	-	7.9
389	1973	Government	Earthquake Recon.		-	20.0	11.6
879	1973	Autoridad Portuaria de Corinto	Ports		11.0	-	9.1
879 **	1975	Autoridad Portuaria de Corinto	Ports		5.0	-	5.0
Total					115.3	23.6	
of which has been repaid					30.1	0.1	
Total now outstanding					85.2	23.5	
Amount sold				4.4			
of which has been repaid				4.1	0.3	-	
Total held by Bank & IDA					84.9	23.5	
Total undisbursed							51.7

* Includes exchange adjustment

** Supplemental loan

International Finance Corporation
Summary of Investments held in
Nicaragua - as of August 31,
1975

(Millions of US$)

	Loan	Equity	Total
Commitments:			
Textiles Fabricato de Nicaragua, S.A.	$ 1.00	$ 1.07	$ 2.07
	1.00	1.07	2.07
Repayments, Sales and Cancellations	.60	1.07	1.67
Net Investments held by IFC	.40	-	.40
Undisbursed	-	-	-

G. 5. b. NICARAGUA: Ongoing Projects

Earthquake Reconstruction Project

Cr 389 - June 6, 1973 -- US$20.0 million
Closing Date: June 30, 1976

The project is part of a program to reconstruct and rehabilitate the Nicaraguan economy after the earthquake which partially destroyed Managua on December 23, 1972. It comprises five components: (1) sites and services (US$8.0 million), which consists of 6,400 lots, community facilities for all project locations, and technical assistance; completion of construction for all sites is now estimated to be at least one year behind schedule; (2) industry (US$2.5 million), which applies to the secondary cities and consists of the procurement of fixed capital assets for medium-sized industries and of industrial sites and services (the Industrial Serviced Sites are delayed although the industrial lending sub-component is approaching completion.); (3) education (US$2.0 million), which consists of four temporary general secondary schools, two permanent multilateral secondary schools, and one permanent technical institute; it is 24 months behind schedule; (4) water supply (US$2.5 million), which consists of emergency repair and rehabilitation of existing installations, equipment and materials for rehabilitation work and some local cost financing of civil work under the previous Loan 808-NI (no significant delays are reported.); (5) power (US$5.0 million), which consists of emergency repair and rehabilitation of existing installations; extension of existing distribution network to provisional housing; expansion of substations, primary, and secondary distribution facilities; transmission systems and substations; the power component also includes office buildings, warehouses and workshops, vehicles, and equipment which were in the Power Company's (ENALUF) 1973-74 work program for repairs throughout the country. Three months delay is estimated for this component.

Education Project

Ln 532 - April 10, 1968 -- US$4.0 million
Closing Date: December 31, 1976

The project consists of the following: (1) Construction of eleven new schools and extensions to eight existing schools, including boarding facilities; (2) acquisition and installation of instructional equipment for 21 schools; and (3) acquisition and installation of furniture for 21 schools. Unsatisfactory project administration, frequent changes in project unit staff, difficulties with the civil works contractors after the earthquake due to changes in construction work standards, cost overruns and shortages of construction materials and local funds for the project have caused the delay in completion. We expect the project to be finished before December 1976.

Second Managua Water Supply Project

Ln 808 - March 17, 1972 - US$6.9 million
Closing Date: September 30, 1976

The project consists of the construction of water wells, pumping stations and storage tanks, extension and improvement of distribution network, installation of service connections and water meters, and repair of earthquake damage. No delays are expected.

Eighth Power Project

Ln 840 - June 28, 1972 -- US$24.0 million
Closing Date: March 31, 1977

This project is being jointly financed with the Central American Bank for Economic Integration, which is supplying US$6.1 million to ENALUF. The project consists of a 100 MW steam-electric station; 230 kV and 138 kV transmission lines and substations; a loan dispatch center; consultant's services; and a 230 kV interconnection line to Honduras. The project is expected to meet Nicaragua's requirements up to 1978 and to provide power also to Honduras, until completion of the large hydro-power project in that country. The project is experiencing large cost overruns and delays of more than one year.

Second Port of Corinto Project

Ln 879 - February 2, 1973 -- US$11.0 million
Closing Date: June 30, 1979

The project is designed to satisfy present and projected traffic demands up to about 1985, permit establishment of container-handling facilities, and protect road and rail access to the port. It comprises the construction of a new wharf, various buildings, storage areas, utilities, purchase of container-handling equipment, channel dredging, coastal defense works, consultants services and staff training. Substantial cost overruns and some delays have been incurred in the project.

Agricultural Credit Project

Ln 943 - November 16, 1973 -- US$8.5 million
Closing Date: December 31, 1978

The project is part of a program to increase and diversify agricultural output (excluding coffee, cotton and bananas), and beef and dairy production. The project consists of: (1) a credit program to some 550 farmers, (2) financing of storage and transport facilities and contract machinery, (3) technical services, (4) seed multiplication, marketing centers and artificial insemination, and (5) a beef marketing study. The project has experienced some initial delays; however, it is expected that it will be completed nine months in advance of the appraisal estimate.

Population: 2.2m; 3.2 p.a.
Cap. GNP: $436 (1971); 3.0% p.a. 1974-78
130,000 sq. kms.
acy: 57 percent

NICARAGUA: ACTUAL AND PROPOSED LENDING THROUGH FY80

		Through	Actual						Current	Program					Total	Total	Total	Total
		FY68	FY69	FY70	FY71	FY72	FY73	FY74	FY75	FY76	FY77	FY78	FY79	FY80	FY69-73	FY74-78	FY75-79	FY76-80
Agric. Credit I	IBRD	2.7																
Agric. Credit II	IBRD							8.5										
Agric. Credit III	IBRD										12.0							
Agriculture:																		
-Grain Silos I	IBRD	0.5																
-Irrigation I	IBRD	2.6																
-Irrigation II	IBRD												10.0					
Education I	IBRD	4.0																
Education II	IBRD									12.0								
Education III	IBRD												15.0					
Power I-VII	IBRD	42.4																
Power VIII	IBRD					24.0												
Power IX	IBRD										15.0							
Power X - Geothermal	IBRD											30.0						
Power XI Interconnection with Costa Rica	IBRD													35.0*				
Highways I-II	IBRD	7.0																
Domestic Airports	IBRD										8.0							
Feeder Roads	IBRD												10.0					
Port I (Corinto)	IBRD	3.2																
Port II (Corinto)	IBRD						11.0											
Port II Suppl. (Corinto)	IBRD									5.0*								
Water Supply I	IDA	3.0																
Water Supply II	IBRD					6.9												
Water Supply III	IBRD											10.0						
Sites and Services	IBRD													10.0				
Reconstruction I	IDA						20.0											
Small Industry Credit	IBRD										8.0							
Operations Program	IBRD							8.5										
	IDA																	
	Total							8.5										
	Number	1				2		1	0									
Lending Program	IBRD	62.4				30.9	11.0	8.5										
	IDA	3.0					20.0											
	Total	65.4				30.9	31.0	8.5	0									
	Number	15				2	2	1	0									
Commitment Deflator									141.9	150.4	158.4	166.4	174.7	183.5				
Real Lending									0	13.3	6.3	12.0	8.6	5.4				

*/ New Project.

September 1975

G. 5. d. NICARAGUA: Future Projects

FY76

Second Education Project (Integrated Rural Education)

Total Cost: US$19.8 million
Proposed Loan: US$11.0 million
Board Date: April 1976

The project, which has already been appraised, will include the construction of 18 Rural Community Learning Nuclei, 18 Lower Secondary Schools in semirural towns, 9 Agricultural Training Centers, and 4 Agricultural Secondary Schools. In addition, 84 houses for teachers and administrators will be built as well as boarding facilities for 590 students in the agricultural centers and schools. The project provides for technical assistance, teacher upgrading and project administration.

Third Water Supply Project (Rural Water and Sewage)

Proposed Loan: US$10 million
Board Date: March 1977

This is a national rural water supply sanitation program for small rural villages and possibly some of the smaller urban areas. The inclusion in this project of a nutrition component is being considered. An appraisal mission has been scheduled for June 1976.

Small Industry Credit

Total Cost: n.a.
Proposed Loan: US$8 million
Board Date: FY77

This will be a DFC follow-up to the industrial component of our Earthquake Reconstruction Project (Cr 389). Under this loan we intend to finance the procurement of fixed capital assets for medium-sized industries, and provide technical assistance to INFONAC (National Development Institute) to strengthen its administrative capacity. We are reviewing the application submitted to us, but have not decided yet on a mission schedule.

Ninth Power Project

Board Date: July 1976

The project consists of an expansion of the transmission and distribution lines. We are planning to send an appraisal mission in January 1976.

Third Agricultural Credit Project

Proposed Loan: US$12 million
Board Date: May 1977

This project will be a follow-up to our Loan 943-NI. It will give more emphasis to reaching the smaller farmers. We have scheduled an FAO/CP preparation mission for November 1975.

Feeder Airports Project

Proposed Loan: US$8 million
Board Date: February 1977

This project will upgrade domestic airports, designed mainly to provide an improved transport link between the least developed areas of the country, the Atlantic region and the rest of the country. We have scheduled an appraisal mission for June 1976.

FY78

Tenth Power Project

Proposed Loan: US$20 million
Board Date: FY78

This project will be designed to help Nicaragua begin to exploit its geothermal resources, which according to preliminary results of exploration now underway, may have a substantial potential for electric power generation. We expect to make this loan in FY78. A US$20.0 million loan is being considered

6

6.6.a

PANAMA - E-a

THE STATUS OF BANK GROUP OPERATIONS IN PANAMA

A. STATEMENT OF LOANS

(As of August 31, 1975)

Numbers	Year	Borrower	Purpose	US$ million: Amount less cancellations	Undis-bursed
5 loans	(1953-62) fully disbursed			18.0	-
661 PAN	1970	IRHE	Power	42.0	7.4
783 PAN	1971	Dirección de Aeronaútica	Airport	20.0	11.1
784 PAN	1971	Banco Nacional de Panama	Agriculture (Fisheries)	3.4	1.5
901 PAN	1973	Banco Nacional de Panama	Agriculture (Livestock)	4.7	3.7
948 PAN	1974	IRHE	Power	30.0	23.3
1114 PAN	1975	Autoridad Portuaria Nacional	Fishing Port	24.0	24.0
	Total (less cancellation)			142.1	
	of which has been repaid			14.2	
	Total now outstanding			127.9	
	Amount sold		3.4		
	of which has been repaid		2.5	.9	
	Total now held by Bank[1/]			127.0	
	Total undisbursed				71.0

B. STATEMENT OF IFC INVESTMENTS

(as of August 31, 1975)

Year		Loan	Amount ($ million) Equity	Total
1971	Corporación de Desarrollo Hotelero S. A.	1.2	.3	1.5

[1/] Prior to exchange adjustments.

G. 6. b. PANAMA: Ongoing Projects

Second Power Project

Ln 661 - March 16, 1970 -- US$42 million
Closing Date: April 30, 1976

The project is about 80% completed with an expected delay of about 18 months for the major component, the Bayano Hydropower development. IRHE and the Government are taking steps to accelerate construction, having declared the project of highest national priority. Delayed impounding of the reservoir will only allow partial storage of the 1975 rains so that full output may not be available until the third quarter of 1976. The other major components (Las Minas 40 MW unit with transmission) were commissioned with up to 9 months delay. Discussions are in progress with the Government and IRHE on cost overrun financing.

Tocumen International Airport Project

Ln 783 - August 2, 1971 -- US$20 million
Closing Date: December 31, 1975

Runway paving is proceeding well. The base course is well advanced and concrete paving has now started. Foundation work has now started in the terminal building. Project completion is now estimated for September 1977.

Fisheries Project

Ln 784 - August 2, 1971 -- US$3.4 million
Closing Date: September 30, 1976

The project, which is designed to increase efficiency of the Panamanian shrimp industry, consists of (1) construction of shrimp trawlers; (2) a trawler captains' training program; and (3) a fishing port feasibility study. The captains' training program is proceeding with the assistance of the UNDP and FAO. The fishing port feasibility study was completed in February 1974 and led to the preparation of the loan approved in April 1975. Construction of trawlers is underway with the first trawlers already in service. However, the scope of the project had to be reduced from the originally intended 40 trawlers to 23 trawlers due to escalation of costs.

Livestock Project

Ln 901 - June 8, 1973 -- US$4.7 million
Closing Date: December 31, 1978

The project is the first Bank operation in Panama for livestock development. It is providing financial assistance for development of small and medium-size farms, as well as for land reform enterprises. Technical assistance to farmers is provided by project staff experts. After a slow start in the handling of sub-loan applications, project administration has been improved, but disbursements are still lagging behind appraisal estimates.

Third Power Project

Ln 948 - December 4, 1973 -- US$30 million
Closing Date: June 30, 1978

The project is designed to begin the integration of isolated electricity systems into a national grid. Project implementation is about 9 months late because of delay in engineering, bidding and procurement of major items - the 28 MW diesels, 230 kv lines and substations. Cost overrun is currently estimated at 22%, in large part due to inflation.

Fishing Port Project

Ln 1114 - May 27, 1975 -- US$24.0 million
Closing Date: September 30, 1979

The Loan was declared effective on September 25, 1975 within the original period provided. The Consultants are proceeding with final engineering of the port and the Government has received bids for the access road, which should be ready by early 1976. The Project Director has been appointed.

IFC Investments

Corporación de Desarrollo Hotelero

Investment Date -- 1971

The investment in the Corporación de Desarrollo Hotelero was considerably delayed when some original lenders and equity investors withdrew from the venture and new partners were recruited. Construction of a first class hotel in Panama City is now proceeding well; part has been completed and inauguration is expected by the end of 1975.

TABLE IVA - OPERATIONS AND LENDING PROGRAMS BY COUNTRY AND FISCAL YEAR

COUNTRY NAME PANAMA

POPULATION 1.5 MILLION
GNP PER CAPITA IS 820

OPERATIONS PROGRAM

PROJECT ID	PROJECT NAME	SOURCE	1976	1977	1978	1979	1980	1981
6-PAN-AD-01	RURAL DEVT. I	IBRD		8.0				
6-PAN-AF-02	FISHERIES II	IBRD		6.0				
6-PAN-AL-02	LIVESTOCK II	IBRD		5.0				
6-PAN-PH-02	POWER IV (LA FORTUNA)	IBRD	40.0					
6-PAN-PH-03	POWER V	IBRD			27.1			
6-PAN-TH-03	HIGHWAYS III	IBRD	28.0					
6-PAN-XX-01	UNIDENTIFIED I	IBRD				14.4		

OPERATIONS PROGRAM TOTALS

	1964-68	1969-73	1974-78	1976-80	1976	1977	1978	1979	1980	1981
AMOUNTS										
IBRD		70.1	168.1	128.5	68.0	19.0	27.1	14.4		
IDA										
TOTALS		70.1	168.1	128.5	68.0	19.0	27.1	14.4		
NUMBERS										
IBRD		4	8	7	2	3	1	1		
IDA										
TOTALS		4	8	7	2	3	1	1		

LENDING PROGRAM TOTALS 5/12/75

	1964-68	1969-73	1974-78	1976-80	1976	1977	1978	1979	1980	1981
AMOUNTS										
IBRD		70.1	104.0	71.0	25.0	11.0	14.0	21.0		
IDA										
TOTALS		70.1	104.0	71.0	25.0	11.0	14.0	21.0		
NUMBERS										
IBRD		4	6	6	2	1	1	2		
IDA										
TOTALS		4	6	6	2	1	1	2		

G. 6. d. PANAMA: Future Projects

La Fortuna Hydroelectric Power Project (Power IV)

Proposed Loan -- US$40.0 million

This project is designed to help finance a power expansion program, the main component of which is the 170 MW hydropower plant. Total investment is estimated at about US$290 up to 1980, and is to be financed by the Bank, IDB (about US$60 million including Venezuelan funds) suppliers credits, the Government and IRHE. The project is clearly justified as it would substitute oil imports for power generation and attend to increasing demand. Appraisal scheduled for November. Main issues are improvement in IRHE's Management, as financial planning is very weak and completion of the financial package. Scheduled for Board presentation in FY76; probability 1/1.

Water Supply Project

Proposed Loan -- US$8.0 million

Project preparation for water supply for the city of Colon, an extension of distribution in Panama and a water metering program has proceeded well. President Lakas has expressed interest in the Project. Appraisal scheduled for November. The main issues are expected to be increases in tariffs (about 30% in 1976 and possibly more thereafter), and improvements in IDAAN's Management. Scheduled for Board presentation in FY77; probability 3/2. The loan may be brought forward to FY76.

Bayano Regional Development Project

Proposed Loan -- US$8.0 million

The scope of the project is still under discussion but might include investments to improve irrigation in the State Farms and the financing of basic services for 3000 individual farmers and 9 organized groups of farmers (including 700 families). Services would include potable water, power, construction of feeder roads as well as training. FAO/CP is assisting in the definition and preparation of the project. A small mission to help define the project would travel to Panama in November and a larger one to prepare it would go in February. Possible issues might be the relative importance of investment for the State farms and private farms. Scheduled for Board presentation in FY77; probability 1/1.

Second Livestock Credit Project

Proposed Loan -- US$5.0 million

Feasibility study contract with consultant is due to be signed in October. Study would determine feasibility of livestock credit program on Atlantic Coast. Possible issues might be interest rates for sub-loans, beef and dairy product pricing and export policies. Scheduled for Board presentation in FY77, probability 3/2.

H

EL SALVADOR

Sector/Title/Number	UNDP CONTRIBUTION	Remarks
A. PRODUCTIVE SECTORS		
Agriculture, Forestry and Fisheries		
Forestry Development and Watershed Management (ELS/73/004)	865,806	
Livestock Development (ELS/74/008)	413,293	
Agricultural Training (ELS/74/010)	11,000	
Subtotal:	1,290,099	
Industry and Trade		
Industrial Consultancy Unit (ELS/72/005)	382,250	
Study and Promotion of Industrial Projects (ELS/73/005)	300,350	
Industrial Programming and Policies (ELS/74/014)	115,650	
Assistance to the Institute of Foreign Trade (ELS/74/014)	562,500	Approved in Principal
Subtotal:	1,360,750	
Mining		
Subtotal:	-	
Total Productive Sectors :	2,650,849	
B. INFRASTRUCTURE		
Transport		
Civil Aviation (ELS/73/001)	144,674	
Subtotal:	144,674	

Communications		
Postal Administration (ELS/72/013)	73,400	
Telecommunications (ELS/73/010)	224,660	
Technical Assistance in Telecommunications (ELS/74/012)	58,200	
Subtotal:	356,260	
Energy and Natural Resources		
Hydro-Meteorology (ELS/72/010)	196,000	
Petroleum Exploration and legislation (ELS/74/003)	1,050,880	
Land Use Survey (ELS/74/011)	7,500	Preparatory Activities
Subtotal:	1,247,630	
Total Infrastructure :	1,748,564	

C. SOCIAL SECTORS

Education, Culture, Science and Technology	
Teacher Training (ELS/73/013)	673,500
National Network of Cultural Centres (ELS/74/004)	118,950
Subtotal:	792,450
Health and Population	
Environmental Sanitation (ELS/73/002)	72,200
Subtotal:	72,200

Labour, Manpower Training, Employment and Social Security		
Social Security Policy (ELS/73/011)	68,150	
Subtotal:	68,150	
Housing and Urban Development		
Housing (ELS/73/008)	5,000	Preparatory Activities
Subtotal:	5,000	
Community and Rural Development		
Community Development (ELS/73/003)	443,318	
Subtotal	1,154,436	
Total Social Secotrs :	1,154,436	
D. PLANNING AND PUBLIC ADMINISTRATION		
Financial and Operational Plans (ELS/73/012)	65,482	
Technical Assistance (ELS/74/007)	31,950	
National Planning System (ELS/74/017)	498,000	Approved in Principle
National Data Base System (ELS/75/001)	59,636	
Subtotal:	655,068	
Total Planning and Public Administration :	655,068	
GRAND TOTAL :	6,208,917	

GUATEMALA

Sector/Title/Number	UNDP CONTRIBUTION $	Remarks
A. PRODUCTIVE SECTORS		
Agriculture, Forestry and Fisheries		
Agricultural Statistics (GUA/71/009)	60,000	
Assistance to the National Institute for Agricultural Marketing (GUA/71/519)	514,250	
Assistance to the Forestry Sector (GUA/72/006)	1,078,550	
Improvement of Sheep Production (GUA/72/021)	226,572	
Maritime Artisanal Fishery (GUA/74/013)	246,900	
Subtotal:	2,126,272	
Industry and Trade		
Radioisotopes in Industry (GUA/69/004)	7,486	
Audiovisual Aids in Industry (GUA/71/001)	137,491	
Export Promotion (GUA/72/012)	256,600	
Industrial Development and Promotion (GUA/73/005)	543,108	
Subtotal:	944,685	
Mining		
Subtotal:	-	
Total Productive Sectors:	3,070,957	

B. INFRASTRUCTURE

Transport

Civil Aviation (GUA/72/014)		149,068
	Subtotal:	149,068

Communications

Telecommunications (GUA/73/002)		184,684
Organization of Postal Distribution (GUA/70/008)		140,636
	Subtotal:	325,320

Energy and Natural Resources

Hydrometeorological Services (GUA/72/010)		249,650	
Groundwater Study (GUA/72/011)		1,016,695	
Petroleum Development (GUA/74/014)		108,500	
Geothermal Resources (GUA/74/009)		3,000	Preparatory Activities
	Subtotal:	1,377.845	
	Total Infrastructure :	1,852,233	

C. SOCIAL SECTORS

Education, Culture, Science and Technology

Primary Education Particularly in Rural Areas (GUA/70/004)		97,150
Adult Education (GUA/73/001)		96,000
Scientific Policy (GUA/74/012)		128,300
Assistance to the National Plan for Education (GUA/75/002)		142,400
	Subtotal:	335,690

GUATEMALA

Health and Population

Integrated Laboratory for Food (GUA/72/004) Control	839,207
Subtotal:	839,207

Labour, Manpower Training, Employment and Social Security

Human Resources Training (GUA/72/013)	459,500
National Employment Service (GUA/74/005)	43,000
Subtotal:	502,500

Housing and Urban Development

Subtotal:	-

Community and Rural Development

Subtotal:	-
Total Social Sectors :	1,341,707

D. PLANNING AND PUBLIC ADMINISTRATION

National Accounts (GUA/71/011)	151,058
Evaluation and Establishment - Data (GUA/72/017) Processing System	82,300
National Civil Service (GUA/74/003)	20,500
Preparation of Development Plan (GUA/74/004)	150,161
Co-ordinating Development Planning with (GUA/74/010) the Public Sector	97,000
Public Administration (GUA/74/011)	72,000

Energy (GUA/75/015)	Project to ascertain fish and wildlife damage from oil spill in Guatemalan Waters	23,000
	Total Planning and Administration:	605,019
	GRAND TOTAL :	$6,869,916

HONDURAS

Sector/Title/Number	UNDP CONTRIBUTION $	Remarks
A. PRODUCTIVE SECTORS		
Agriculture, Forestry and Fisheries		
Agricultural Statistics (HON/68/005)	214,309	
Agrarian Reform Training and Development (HON/71/509)	501,000	
Agricultural Development of selected zones (HON/72/011)	680,583	
Forestry Management and Lumber Production (HON/75/004)	1,091,800	Approved in Principle
Forestry Planning, Management and Administration (HON/71/511)	756,169	
Subtotal:	3,243,861	
Industry and Trade		
Subtotal:	-	
Mining		
Subtotal:	-	
Total productive sectors :	3,243,861	
B. INFRASTRUCTURE		
Transport		
Transport Planning (HON/72/007)	58,115	
Civil Aviation (HON/72/008)	131,697	
Subtotal:	189,812	
Communications		
Subtotal:	-	
Energy and Natural Resources		
Subtotal:	-	
Total Infrastructure:	189,812	

C. SOCIAL SECTORS

Education, Culture, Science, and Technology

Teacher Training (HON/72/010)		552,200
	Subtotal:	552,200
Health and Population		
	Subtotal:	-
Labour, Manpower Training, Employment and Social Security		
	Subtotal:	-
Housing and Urban Development		
	Subtotal:	-
Community and Rural Development		
	Subtotal:	-
Total Social Sectors	:	552,200

D. PLANNING AND PUBLIC ADMINISTRATION

National Development Plan (HON/73/001)		202,850
	Subtotal:	202,850
Total Planning and Public Administration:		202,850
GRAND TOTAL	:	4,188,723

N I C A R A G U A

Energy and Natural Resources

San Juan River (NIC/71/513)	717,000	
Hydrological and Meteorological Services (NIC/72/011)	299,650	
Geothermal Resources (NIC/74/003)	98,000	
Geological Survey of the Yalaguina Area (NIC/74/008)	6,450	
Subtotal:	1,121,100	
Total Infrastructure :	1,220,386	

C. SOCIAL SECTORS

Education, Culture, Science and Technology

Subtotal:	-	

Health and Population

Rural Health (NIC/74/007)	5,000	Preparatory Activities
Subtotal:	5,000	

Labour, Manpower Training, Employment and Social Security

Subtotal:	-	

Housing and Urban Development

Subtotal:	-	

Community and Rural Development

Community Development (NIC/73/013)	77,500	
Subtotal:	77,500	
Total Social Sectors :	82,500	

N I C A R A G U A

D. PLANNING AND PUBLIC ADMINISTRATION

Technical Assistance to the National (NIC/73/020) Planning Office	122,911
Administrative Support (NIC/74/005)	58,794
Subtotal:	181,705
Total Planning and Public Administration :	181,705
GRAND TOTAL :	2,954,301

N I C A R A G U A

Sector/Title/Number	UNDP CONTRIBUTION $	Remarks
A. PRODUCTIVE SECTORS		
Agriculture, Forestry and Fisheries		
Bilogical Control of Cotton Pests - (NIC/70/002)	359,239	
Soil Conservation and Watershed Management (NIC/74/001)	77,750	
Nueva Segovia Pine Forest (NIC/74/002)	88,000	
Basic Grains (NIC/74/006)	794,801	
Subtotal:	1,319,790	
Industry and Trade		
Industrial Priorities (NIC/74/014)	135,000	
Management of Enterprises (NIC/74/015)	14,920	
Subtotal:	149,920	
Mining		
Subtotal:	-	
Total Productive Sectors:	1,469,710	
B. INFRASTRUCTURE		
Transport		
Civil Aviation (NIC/73/001)	75,000	
Subtotal:	75,000	
Communications		
Telecommunications (NIC/73/010)	24,286	
Subtotal:	24,286	

UNDP Activities (Res. Rep. Mr. Angel Herrera)

In the past UNDP has directed its assistance towards the identification of mineral resources. Under these programs deposits of copper and Cerro Colorado (see notes on the Governments Investment Program D-d) and at Petaquilla were identified. The emphasis on natural resources will continue in the future but the programs will attempt to identify non-metallic minerals and geothermal sources of energy. UNDP has also helped prepare a Regional Development Strategy paper which was released in December 1974 and continues to provide an expert in this field (Mr. A. Solow). The UNDP program for 1976-77 is in preparation and should be ready by December.