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GROENVELD, D.R. - ARTICLES and speeches (1958 - 1968)



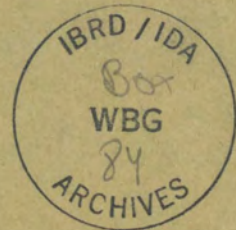
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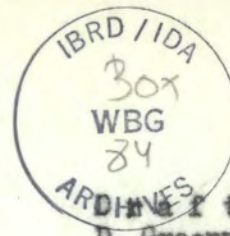
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GROENEVELD

5/27/58 - Fwd. to Mr. Graves by D. Groenveld:
"Attached is a draft of my contribution to the
Meeting of International Agencies on Agricultural
Credit Training and Study Programs in Latin America,
organized by CEMLA from June 2-5, 1958"



May 27, 1958

Contribution for CEMLA meeting, June 2, 1958

It will be obvious that the International Bank, being a financial institution, is primarily interested, as far as her relations with agricultural credit institutions are concerned, in helping those institutions financially. For the Bank, offering technical assistance is a sideline although a very important sideline. It is important because improving the ability of agricultural credit institutions to operate efficiently enlarges the scope for sound financial relations between the Bank and these institutions.

However, since making loans is the World Bank's main business, I would like to begin by informing you, as far as is necessary, about the loans which the Bank has made to farm credit institutions in Latin America. We have made the following loans:

two loans to the Caja de Credito Agrario in Colombia,
totalling \$10 million;

two loans to Nicaragua (one to the Banco Nacional and
one to the Instituto de Fomento Nacional), totalling \$2.7 million;

two loans to the Banco de Fomento Agropecuario in Peru,
totalling \$10 million;

one loan of \$1.2 million to the Instituto de Fomento Economico
in Panama;

one loan of \$5 million to the Government of Paraguay
mainly for farm credit purposes;

one loan to the Banco Central in Costa Rica for the
amount of \$3 million.

In the period 1949-1957, the World Bank made nine loans in this category totalling \$31.9 million equivalent. Most of this money was spent on imported machinery, materials and breeding cattle.

Turning to the field of technical assistance, I would like to draw your attention to two of the Bank's programs: the Economic Development Institute and the group of Training Programs. This group includes three programs: the General Training Program, the Public Finance Training Program and the Special Training Program.

The E.D.I. is a staff college for senior government officials from underdeveloped countries. So far, it has provided three six-month courses of intensive study to a group of about 20 participants. The subject of "Agricultural Credit" is included in the course on "Agricultural Development".

The Bank's General Training Program started in 1949. Each year a group of eight or nine younger nationals of member countries follow a six-month course of theoretical and practical training. The purpose of this program is mainly to acquaint the participants with the work of the Bank, but there is room for training in special subjects, such as farm credit. However, such special training is better included in the Public Finance Training Program, which has been in operation since 1950. The courses in this program, which lasts for 3 - 6 months, are tailored to the needs of each participant and they would give an excellent opportunity for intensive study of farm credit problems.

Finally there is the Special Training Program which also works on an individual basis and it is used to familiarize officials of new member countries with the Bank's operations.

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As you will have noted, the courses of the E.D.I. and the Public Finance Program afford the best opportunities for the study of farm credit issues. Moreover the Bank has participated in some of the Farm Credit Seminars organized by other agencies, such as the Seminar in Panama in 1957.

cc: Messrs. Chadenet
Graves
Honsi
Spiro

THE ECONOMIC EVALUATION OF LAND DEVELOPMENT PROJECTS¹⁾

D. GROENVELD

International Bank, Washington, U.S.A.



SUMMARY

1 Most methods recommended for the economic evaluation of land development projects are too refined for application to projects in underdeveloped areas. The author suggests, therefore, the use of a simple method in these areas.

2 The economic effect of a project should be estimated with respect to the national economy, to the entrepreneurs (farmers) in the project region, and to the government.

3 Most evaluating methods ask for an estimate of net benefits. There is however doubt whether this is necessary and feasible. An estimate of gross benefits seems all that is really required.

4 The traditional cost/benefit ratio calls for a conversion of investments into an annual figure. This conversion has to be done in an arbitrary way and is undesirable.

5 It is therefore proposed to compare project costs (investments) with the increase in gross value of agricultural production, in other words: to use a capital/output ratio.

6 The article discussed briefly how to find the maximum acceptable capital/output ratio.

7 However, one has to estimate the increase in costs (in terms of current expenses) for the private interest test. In many cases this increase in costs will be small if compared with the increase in output, in view of the importance of non-monetised costs and of fixed costs.

8 The repayment capacity of the farmers will usually increase adequately if a project has a favorable capital/output ratio, and if it passes the private interest test. However it is also important that the investor (usually the government) earns a reasonable return on his investment.

INTRODUCTION

In the minds of the present generation the need for a justification of investments in large projects arose during the depression of the thirties. This need became even stronger in the postwar period, first for reconstruction works and later for development works. The need originates from a situation in which there are a great number of claims for a limited quantity of means to satisfy them. Investment capital is the most general means "in short supply".

During the last three decades a great number of studies have been made seeking a satisfactory way to measure the economic feasibility of major projects, so that a priority rating could be established. Several more or less refined methods have been developed, and several ways to test the economic feasibility of a project have been formulated. Most of the methods require more data than can reasonably be made available, as we will discuss later.

The list of publications, appended to this article, includes only a small selection out of the sea of literature on this subject. Most of the original thinking has been in the advanced countries (see however 1) and some of the methods developed for use in these countries have been transplanted without critical scrutiny to underdeveloped areas (see 2 and 5).

This practice may lead to wrong conclusions since the evaluators who use a refined method on a project in an underdeveloped area may feel obliged

¹⁾ Received for publication January 30, 1959.

to quantify categories of costs which cannot under those conditions be expressed in sums of money.

For instance there is usually a great deal of disguised unemployment and underemployment in those regions, which means that the "real" value of labor is less than the wages paid for construction work. On the other hand capital is often in short supply and the "real" rate of interest may be higher than the rate charged to construction firms and farmers. Prices of construction equipment and materials also do not always reflect their real economic value; they are often manipulated prices.

With respect to farming: most of the work on the farm is usually done by members of the farm family, without money transaction. Often the labor supply is such that labor hardly has an economic value. It is also true in many cases, especially under pre-project conditions, that the farm is primarily run to supply the needs of the farm family and that only a limited amount of the production is sold for money. In the case of mixed farms there is the problem of intra-farm deliveries (feed crops to cattle, manure to croplands, etc.), which can only be disentangled by painstaking and time-consuming research work. It is for these reasons, combined with a shortage of competent research workers in underdeveloped areas, not surprising that reliable data about expenses of farmers in such areas are very rare.

With respect to benefits: these are in many cases very large, in the sense that increases in gross production of 100%—400% are sometimes foreseen in areas where a primitive form of dry-farming is practised before the project begins to operate. In many cases irrigation means the difference between no crop at all and a rich crop.

To sum up: the special conditions under which cost/benefit analysis has to be applied in underdeveloped areas are: underemployment of labor, scarcity of capital, manipulated prices of materials, lack of cost data on farm operations and possibility of large increases in gross production.

It is in most cases advisable to investigate the economic feasibility of a project with respect to:

- a the national economy (influence on national income, balance of payments);
- b private enterprise (farmers);
- c the government (or the project agency).

The benefit/cost ratio is usually recommended to assess the economic merits of a project with respect to the national economy. This ratio will be discussed first and it will be shown that the benefit/cost ratio is not a good instrument for this purpose, at least not for projects in underdeveloped areas. The capital/output ratio, which will be discussed later, seems a more suitable determinant.

THE BENEFIT/COST RATIO

This ratio is established by estimating the annual benefits produced by the project and by dividing them by an estimate of the annual costs.

Great care should be taken to include in both categories only those elements that really should be included. If one calculates the benefits on the basis of ex-farm prices (direct benefits) one should include only costs required to produce the crop on the farm (project costs and associated costs). However, if one includes indirect benefits one should also include the indirect costs.

Although the difficulties of estimating the direct benefits should not be belittled, they are certainly less in number than the problems connected with an estimate of annual costs. The total annual costs of the project are in a simplified example (page 41 of the U.N.-Ecafe report 2) shown as the sum of the annual equivalent of capital costs and the annual costs of operation, maintenance and replacements. This report recommends (page 38) for translating the capital costs into an annual figure, taking the average long-term borrowing rate of government offerings. Such rates are however not available in many underdeveloped countries, since their governments are often not in a position to borrow in a free market. Also a rate of depreciation has to be established. The report includes a table which gives in great detail the conventional "estimated lives" of many construction features. The estimated life of dams is put at 100 years, of canal linings at 50 years, etc. These are all very rough rules of thumb. The useful life of a dam depends very much on special conditions, such as the type of construction, the rate of silting of the reservoir, maintenance, etc. Moreover the rate of interest and the rate of depreciation are very arbitrary figures, and the question arises whether they can be used for refined calculations.

Many publications conceive of benefits as the increase in net annual farm income, which means that one has to deduct farm costs from the estimate of the increase in gross farm income. Some reasons why it is difficult to collect reliable and meaningful cost data about existing farm operations have already been mentioned; however attention should be drawn to a difficulty that arises when one has to estimate costs of future operations, if the character of the farm business changes completely. The effect of an irrigation project is often the transformation of a simple nearly mono-crop farm into a much more complicated diversified farm. This raises such questions as: what will be the effect of more manure on crop yields; what is the food or fodder value of unsaleable portions of crops; what is the fertilizing value of a legume crop; what are the costs of using a multi-purpose animal for farmwork, etc.? The whole problem of the effect on costs of transforming a simple farm into a complicated one with supplementary and complementary "divisions" makes it rather unrealistic to try to estimate future costs of production. This holds with even more force if the project involves development of an entirely new type of enterprise in the region since there is no source of comparative cost data.

The combination of these difficulties and the inaccurate character of many of the data, make the benefit/cost ratio a rather unsuitable concept for the measurement of the economic merits of a project. The ratio, often given in two digits behind the decimal point, suggests a measure of accuracy which it really does not have.

THE CAPITAL/OUTPUT RATIO

The capital/output ratio is established by dividing the sum total of the investments in the project (public and private investments) by the estimate of the increase in gross farm production.

In "capital" should be included the investments in all the public works that serve directly or mainly the purpose of increasing farm production (the costs of irrigation works, drainage facilities, farm to market roads, power lines to farms or pumping stations, but not buildings for general governmental pur-

poses, or general schools). Investments in the farms necessary for using the irrigation facilities should be included (farm ditches, levelling and terracing, farm buildings, equipment, working capital).

The Italian concept of "gross saleable production" is probably the best way to measure "output". This concept includes the goods actually sold, plus imputed sales to farm households. However, "sales" of feeds to the livestock department of the farm are excluded (see 4 and 6).

By using this ratio one eliminates all the problems of reducing capital costs to an annual figure and of deducting farm costs from gross benefits. However is it right to disregard costs of operating and maintaining the project works, and the costs of farming? In the opinion of this writer one is justified in doing this at this stage of the research work, that is, while ascertaining the effect of the project on the national economy.

The costs of operating and maintaining the project works are only partly "costs" to the nation and they are as a rule insignificant if compared with national income or government budget, so that hardly anything is lost in eliminating them at this stage.

More consideration ought to be given to disregarding farm costs. They consist broadly of the following elements: purchases of farm requisites, payments for services (transport, veterinarian, etc.), rental payments, interests on loans, wages for outside labor, taxes. All these elements are costs to the farmer, however several of them are not costs to the national economy, especially not in the conditions prevailing in underdeveloped areas. The use of farm requisites has to be considered as a cost because they, or at least the raw materials used in manufacturing them could have been used in a different way, if there were no project. Part of the payments for services are no social costs, because several of these services would be used by the farmers also without the project. Payments for rent, taxes and interest are not costs to the national economy, but transfers of income. Wages for outside labor can be counted only for a certain portion as a social cost in view of the assumption of underemployment. Depreciation of farm equipment has not been mentioned as a cost element, because it can be considered in the simple farm economy as covered by the sum of purchases of farm requisites.

All this means that the costs of farming for the economy in an underdeveloped area are reasonably well expressed in the expenses of the farmers for the purchase of requisites and the services of people that have been distracted from other economic activities. How large are these costs?

In this connection the reports included in a series published by the Economic Commission of Europe and FAO (4) are enlightening. The ECE/FAO report discloses that current operating expenses²⁾ vary from 45% of gross output in the U.K. to only 8% in Greece. For the Netherlands the percentage is 25% and for Italy 17%. In underdeveloped areas the figure will probably be close to that mentioned for Greece. As a rule of thumb, to be used if no information is available, one could say that current expenses will be about 10% of gross output in underdeveloped areas where most of the labor is done by the farm family or by otherwise unemployed people.

²⁾ Materials bought by farmers, plus fees paid for services, plus maintenance and depreciation.

It should also be kept in mind that we are really chiefly interested in the increase in costs due to the project and not in the absolute figures. The costs should increase less than proportionately with the increase in gross output because of the importance of fixed or overhead costs (most important of which is the value of the labor of the farm family).

This explains why one does not make a great mistake by disregarding farm costs while considering the significance of a project to the national economy. The margin of error in the estimate of gross benefits may well be larger than 10% and it will certainly become larger in the process of reducing gross benefits to net benefits as required for the calculation of the benefit/cost ratio.

Consequently it is the opinion of the writer that the capital/output ratio gives a reasonably correct indication of the economic feasibility of a project.

It will be understood that the lower the ratio the better the project. The question may arise however, of how high a ratio can still be accepted? In other words, where is the limit? Some projects have a ratio of 3 : 1, others 5 : 1, or even 8 : 1.

The answer to this question depends mainly on two factors: the rate of depreciation of the project, and the free market rate of interest for long-term loans.

A basic rule in judging investment projects should be that they should at least make good their real costs to the economy. It is clear that these costs will increase with the rate of depreciation and the rate of interest. Although the maximum acceptable capital/output ratio has to be established in each case anew, one will often find that the limit is a ratio of about 6 : 1.

These remarks should not be taken as an indication that the author does not see the importance of research in farm economics, especially in farm cost-accounting. To the contrary such research work should be pushed and every reliable piece of information should be used in the evaluation of a project. It should be realized that the time for detailed and refined economic analyses of land development projects has not yet come about, and that therefore a simple test should be used rather than a sophisticated one, for which there is not a sufficient basis of information. For most areas of the world it will be a long time before we have such a basis, and maybe we will never be able to analyse sufficiently the economics of peasant farming.

EFFECT ON FARM INCOME

Despite all that has been said about the difficulty of collecting reliable data on the costs of operating farms, it is nevertheless necessary to estimate the increase in farm costs in order to consider the effect of the project on the economy of the farm.

This consideration should be guided by the conviction that it is necessary for the speedy success of the project to get the wholehearted cooperation of the farmer, and that the best way to solicit this cooperation is to show him that his net earnings (in kind and money) will increase greatly as a result of the project.

In order to show this to the farmer one has to collect information on the probable increase in the expenses of the farmer. This increase in expenses will in many cases stem from larger purchases of fertilizers, insecticides, etc., expenses for machines, payments for the use of water, increased tax payments.

It will usually not be too difficult to collect the amount of information about this increase in current expenses that will enable the investigator to find out whether this increase will cut too large a portion out of the expected increase in gross output. The conclusion of some research work will usually be that costs will increase by only a fraction of the increase in gross income so that it can be expected that net income will increase rapidly and considerably. As mentioned above, part of the explanation of this phenomenon is that a large portion of the farm costs are non-monetized costs or non-variable costs.

EFFECT ON GOVERNMENT FINANCES

Governments, or specialized government agencies, are usually very much involved in the investments in an irrigation project. It is therefore legitimate to investigate whether the government receives a reasonable return on its investment. Moreover there are the costs of operating the project.

As a matter of principle farmers should be expected to reimburse the government for the capital and operating costs, although it may sometimes for social or political reasons be decided not to adhere to this principle.

The principle does, however, not imply that reimbursements ought to be made by way of a water charge. Part, or even all, of it may be collected in the form of general or special taxes.

No matter what the administrative arrangements are in any specific case one has to estimate the future increase in government income in the form of larger tax collections and of special rate collections resulting from the project. This estimate can be compared with the amount of government investment in order to establish whether there will be a reasonable return.

A second question to be considered is whether the farmers will be able to repay the government for the services provided in the project. This estimate of the repayment capacity of the farmers receives much attention in the U.S.A. and also in other regions (see 5). It is, however, of less importance in underdeveloped areas because the increase in gross value of production is relatively larger in those areas than in a well-developed country. It will appear that in most cases the repayment capacity is adequate if the project passes the two earlier tests (effect on the national economy, and effect on farm income).

ACKNOWLEDGEMENT

Although the author is a member of the staff of the International Bank, the opinions expressed in this article are his, and they do not necessarily represent the views of the Bank. The author wants to express his gratitude to those who read drafts of the article.

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1960-61

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Seminar 6: Agricultural Development

Session 1: Tuesday, January 3

Topic: Agricultural development; problems, programs
and investment requirements

Reading: IBRD, The Agricultural Development of Colombia
(Washington, 1956), Chapters I and XII

Speaker: Mr. Douwe Groenvelde (IBRD)

Outline: Attached

I

1. Agricultural growth and industrial growth interact and stimulate each other. This was notably the case in countries as the United Kingdom, where an agricultural revolution preceded the industrial revolution, and Japan, where early efforts towards agricultural growth made possible the collection of taxes to finance industrialization, and provided food for a fast-growing population and silk for expanding industrial and export sectors, and also in Mexico and the United States. Where agriculture has been neglected or lagged substantially, real growth or its maintenance in other sectors has been seriously jeopardized (e.g., Turkey, China, Brazil, the Soviet Union).
2. The interdependence of agricultural development and that of other economic sectors is based on several relationships. (a) Agriculture provides almost all the food, many raw materials and a market. (b) As per capita income increases, consumption of non-agricultural products and services grows more rapidly than that of food and other agricultural products. (c) Economic development involves a shift of labor from agriculture, which does not require more people and may require fewer people to produce more, to other sectors, which require more labor.
3. The underdeveloped countries, characterized by predominantly agricultural populations of low productivity, are sometimes urged to industrialize, as the fastest if not the only way to economic development. Sometimes, on the other hand, they are urged to concentrate on agriculture. In deciding whether agriculture or industry "comes first", population, resources, technology and trade need to be considered. Development is usually possible in either sector. In most real situations, political and social as well as economic considerations suggest concurrent growth; and each sector, as it grows, feeds the other.
4. In any given country, the fairly simple relationship between agricultural and industrial development is complicated by the relation of its population to its resources and by restrictions on international movements of goods and people. The impact of agricultural and of industrial growth could be shifted abroad through migration of people across borders and through trade. Increased agricultural output could be entirely exported and manufactured goods to meet domestic demand imported; or expanded industries could seek their markets and their supplies of food and raw materials abroad rather than at home. Thus a trading country need not have growth in both sectors so long as it can maintain its trade at an appropriate level. (Japan and the United Kingdom both provide examples.)

5. In the real world of the 20th century, the movement of people is limited; it is difficult to build up an export trade for manufactured goods in competition with developed countries; and social stability requires a leveling out of the differences between sectors. There exists also a natural concern for the vulnerability of food and raw material supplies which suggests balanced development.
6. The conclusion to which these statements are intended to lead is, not that agriculture must be given first priority, but that the sectors are inextricably linked, that the commonly heard alternative of "agriculture or industry" is rarely a real one, and that some kind of balance is necessary (taking account of foreign trade) between the agricultural and the other sectors. (Arthur Lewis says that "though this is rather an obvious conclusion, it conforms neither to current practice nor to current recommendation," for the general tendency is to stress expansion of agriculture or of industry, rather than balanced growth of both.) If this is so, is the question of where to start, a question of principle or a question of timing, taking account of the population, resources, technology and trade of the country? In what sense (if any) is industry more productive than agriculture? And what does "balanced development" mean so far as the relation between agriculture and industry is concerned?
7. Agriculture is one of the more difficult sectors of the economy to change. It is to a considerable extent dependent on purely natural forces such as climate, terrain and soil conditions. But, in addition to these factors and, in part, because of them:
 - a. The farmer's relation to his land and his relative isolation make him more tradition-minded and less amenable to change.
 - b. The typical small scale of farm enterprise makes it more difficult to introduce innovations.
 - c. Increase in agricultural productivity requires a wide variety of carefully planned and executed government actions, e.g., construction of roads, health and sanitation facilities, research and education, in addition to a tremendous number of individual innovations and decisions.
 - d. In many underdeveloped countries, the rural population is treated as an inferior group.
8. Agricultural development does not mean a simple change from a "primitive" to a "modern" technology. It requires changes in values and the retraining of large masses of population. The difference between primitive and modern agriculture is the difference between a rural population which follows a traditional method of cultivation and one which is adaptable, responsive to changing methods and to new opportunities.

II

9. The preparation of a program for agricultural development is not a simple thing. Account must be taken of the many links between agriculture and other sectors in a developing economy; of the pervasive influence of tenure arrangements; of the complexity of the services the government must provide, as agricultural development depends on the action of a vast multitude of small farmers; of the innate conservatism of the farmer, who must be shown to be persuaded; of the careful technical and economic analysis that must precede any project to expand cultivation; of the facilities required to carry agricultural produce to its ultimate market; of the need for farm credit. A program must provide for changes in attitudes (among farmers and civil servants, for instance); for public services (research, education, extension, welfare); for changes in the traditions and legal framework of tenure and other agricultural institutions; and for funds to cover investments and current expenses foreseen in the program.
10. The preparation of such a program requires, at the very start, a clear conception of purpose, for the objectives of the program (assistance to a particularly depressed area or increasing the supplies of food or raw materials required by the country or self-sufficiency in war time) will determine its main features. The program will be heavily influenced by the social and political structure and situation of the country. These in turn affect the means by which the government can try to achieve the targets that make up an agricultural program. In any given situation the effective scope of a program is strictly limited, not only by the political and social situation, but also by the resources available and other factors.
11. Preparation of a program must begin with a knowledge of the nation's agricultural requirements and of its physical and human resources, so as to determine the possibilities of, the limitations on, the needs for, and the trends of agricultural production and consumption. Only after a survey has provided such knowledge is it possible to establish in a preliminary way the goals of an agricultural program. In this connection it is worth noting that estimates of consumption and demand for agricultural commodities are even more difficult to make than estimates of production and supply. About the former only guesses can be made on the basis of projections of populations and income growth. Although tastes change relatively slowly and the typical consuming unit (the family) is fairly stable, forecasts are still fraught with many uncertainties. Not enough is known about present consumption and diets or about the way in which changes in occupation, or moves from rural areas to cities affect consumption patterns. On the other hand, studies of production are of limited value since they generally take into account the conventional inputs, and leave aside the effects of changing technology and improving education and since the typical production unit (the farm) changes in a developing economy.

12. The next step should be consideration of the measures required to achieve the goals. Such measures may vary from persuasion through incentives of various kinds to several varieties of control. Only in the light of the measures available is it possible to fix the goals of the program with fair precision.
13. It is then necessary to review the obstacles to the achievement of these goals. The main obstacles are, in most cases, the low level of general education and the low technological level of the farmer, the insufficiency and poor organization of government services, the lack of confidence in government policy, and the insufficiency of financial resources. In the light of these obstacles the specific measures can finally be fixed; they should concentrate on the major deficiencies and obstacles.
14. Heavy government expenditures might be involved, for instance, for large-scale irrigation or land-clearing projects or for credit facilities; but government investment is generally less important in an agricultural program than the policies, facilities and services necessary to induce the farmer to cultivate in a different and better way and to show him how to do so. At every stage of its preparation, the program should be thoroughly discussed with the farmers, so as to assure their understanding and cooperation. And it should have the agreement of the various government departments involved in its execution.

III

15. If it is considered necessary to develop the agricultural sector, questions arise as to how much capital it requires, where it is to come from, and how it is to be used.
16. The amount of investment in agriculture in underdeveloped countries is difficult to estimate. Much of it comes, as it does everywhere, in modest amounts, from the efforts of the farmer himself in the improvement of his land and buildings, in the acquisition of farm animals, in improving access to his land. Information on such improvements is usually unavailable for underdeveloped countries. There is, moreover, great difficulty in distinguishing in many cases between what is truly an investment that will yield returns over a long period of time and what is a current outlay. Certain kinds of government investments are not directly related to agriculture but have a direct impact on it and other kinds of outlays are current and recurring but are clearly in the nature of long-term investments. Despite these and other sources of error, a review of available information concerning underdeveloped countries suggests that in the recent past, i.e., in the period in which deliberate efforts have been made to increase the rate of investment, agricultural investment has represented a smaller part of total investment than agricultural output has been of total output.

17. In general, agriculture produces in underdeveloped countries more than 50% of G.N.P. Nevertheless, less than 30% of gross investments are, in most cases, allocated to agriculture. In developed countries the share of agriculture's contribution may drop to 15% or even less, and the share of agriculture in gross investments may be reduced to less than 10%.
18. This is not necessarily in all cases alarming, since in the process of development the demand for non-farm goods and services will rise faster than the demand for food. Also, a more rapid decline of the share of agriculture in investments than of the contribution of agriculture to G.N.P. would not be alarming if by the development of the technique of agriculture the I.C.O.R. ^{1/} of agriculture would be lower than the I.C.O.R. of industry. Figures collected by the U.N. show that in recent years the I.C.O.R. for agriculture was in some countries higher than the I.C.O.R. for other sectors. In other countries the reverse was the case. (World Economic Survey 1959). Nevertheless, it is necessary to warn against complacency, as it is possible that in the planning of development too little attention is paid to investments in food production.
19. Attention has been called to the imbalance of investment in a recent study of agricultural production in Latin America. (See Joint Report of ECLA and FAO, The Selective Expansion of Agricultural Production in Latin America, U.N., 1957.) In the 20 countries examined, the growth of agricultural output has fallen so far behind other production, that it has been unable to meet demand without affecting foreign trade. The capital stock in the agricultural sector in those countries increased only 6.5% from

^{1/} Incremental Capital Output Ratio

1950 to 1954, compared with 40% in industry and 20% in services. One result has been an actual decline of fixed capital stock per person employed in agriculture, while there have been substantial gains in the other sectors. Thus, in Latin America and elsewhere, the suspicion persists that agricultural investment has been neglected. But, is it more investment that is required to stimulate the agricultural sector, or a different allocation of investment within that sector?

20. Private money investment in agriculture has been low largely because its returns are low compared with investment in other types of economic activity, and because of inflationary pressures, exchange and price policies, lack of incentives, unsuitable tenure systems, etc. Governments, given their predisposition for certain types of investments, have found relatively few opportunities for direct investment in agriculture. Foreign private capital invested in agriculture is almost exclusively in plantations; these are highly commercial operations, which have command, not only of capital, but also of skilled management, personnel and modern techniques, and are linked closely to foreign trade and highly developed markets.
21. The participation of government in agricultural investment has grown in recent years in underdeveloped countries, but it has in general been limited to projects in such fields as water control and land clearance. The scope for government action in providing the capital required for higher productivity is very great; for while much of the capital in agriculture must come from the farmer himself, he is incapable of providing alone for roads, marketing and storage facilities, machinery, buildings, research facilities, etc.
22. Governments have tended to prefer investment in particular agricultural projects, which are relatively simple to deal with, are spectacularly visible to the naked eye, and are limited in regional scope. They often neglect the broader programs to provide essential services, whose effects may be more pervasive but are not literally so monumental and may be slower to take effect. In any plan for agricultural development the latter must have a large part; they are cheaper in terms of financial resources, more pervasive in their effects, yield greater returns from existing investment, encourage new investment in agriculture, and lay the groundwork of institutions and education necessary for continuing development. An agricultural investment program cannot be carried out and continued growth cannot be assured without a solid foundation of coordinated and consistent policy, research and extension, and working capital, and the institutional machinery they require. The share of agriculture in total planned investments cannot be based on any rule of thumb or formula, because the needs vary considerably and because the possibilities to satisfy these needs vary even more from country to country. Some countries still have easy access to natural resources, while others do not.

The amount of required public and private investments can only be established after the careful drafting of a development plan, and after detailed studies have been made of the investment costs of the various projects and measures recommended by the plan. It is, however, significant that in several cases a second or third development plan allocated a larger share of total investments to agriculture than did the first plan. Apparently the needs of agriculture had been underestimated in the beginning.

IV

23. The World Bank Missions which formulated agricultural programs for Colombia and Peru went through processes of thought and analysis described above, within the limits of information and time available, in preparing their program. In considering the subject, the following questions raise some significant issues.
- a. Was a program for agriculture necessary? Will it be a national program or should special programs be formulated for various regions of the country?
 - b. Should the program aim at expansion of export crops, or an increase in agricultural raw materials, or an increase in and improvements of the nation's diet, or a combination of these? Can specific tasks be assigned to distinct groups of farmers?
 - c. How large an increase in agricultural production should be planned for a given period?
 - d. Should the desired increase in production be attained mainly by expansion of the area in production, or by increasing yields per unit, or by a combination of these alternatives?
 - e. Should the program aim at labor-intensive farming or at capital-intensive farming.
 - f. What measure of protection can be accepted for the development period?
 - g. What kind of action in the agricultural sector needs to be taken to make the program work, and what kinds of action outside of agriculture are necessary in order to support agricultural development?
 - h. What are the main obstacles to increasing agricultural output, and what measures may be used to overcome them?
 - i. What kind of governmental organization is needed to carry out an agricultural program?
 - j. How do you achieve coordination of the government departments involved?
 - k. How do you get the "cooperation" of the farmer?

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Groenweld

ON THE PREPARATION OF PROJECTS FOR
AGRICULTURAL DEVELOPMENT



In recent years much attention has been paid to discussing ways in which the development process in the poorer nations could be accelerated. One important issue in the debate was the matter of the sum to be made available for investments in development works. In this context the replenishment of the almost exhausted resources of the International Development Association (IDA, an affiliate of the World Bank) drew much attention.

It is of course equally important to pay attention to, and to study continuously the matter of how the funds, if available, should be spent. This question can be sub-divided in at least two sub-questions: a) what sector of the economy (or what mix of sectors) should have priority; b) within the priority sector funds must be allocated to high priority projects; in order to do this in a meaningful way there must be ample choice between a series of "good", well-prepared projects; but how does one assure that there is within the selected sector(s) a sufficient number of good projects from which a selection can be made?

This article is especially concerned with the last part of question (b) since it is the author's opinion that the speed of development is just as much affected by the availability of good projects as by the availability of funds. In this respect the present situation is less favourable than that encountered by the capital supplying agencies in the early fifties. At that time, when several nations had just emerged as independent countries, there were in the files of the ministries of these nations as a rule several projects for the construction of dams, power plants, roads, etc., which had been prepared by the staff of the colonial administration. Most of these projects have been executed since and there has not been an adequate production of new projects up to the execution stage. The

same applies, and probably even more so, to non-construction projects in the agricultural sector (research, extension, training, settlement, credit, trade, etc.). And as Andrew M. Kamarock wrote: "For development to occur, concrete investment plans for individual projects must have been prepared - investigating technical feasibilities, computing the costs and benefits, and dealing with problems of administration and management"¹⁾.

The former President of the World Bank, Mr. C. Woods, was well aware of the seriousness of the two issues mentioned above. Consequently he spent much of his time and energy on negotiations with "donor countries" about replenishment of IDA's funds. But he also took two decisions designed to help increase the flow of economically attractive, well prepared projects. First the Bank and FAO established in 1963 a Co-operative Programme, designed to help prepare agricultural projects to the stage at which they could be presented to Bank or IDA. Second, the Bank established in 1965 two Permanent Missions in Africa, one in Abidjan for Western Africa, and one in Nairobi for Eastern Africa. The purpose of these offices is - inter alia - to assist the Government in the identification and preparation of projects in the fields of agriculture and transportation essentially for presentation to the Bank or IDA. It should be stressed from the beginning that in this work great care is taken to enlist as much as possible the active co-operation of officials of the agency, which will be charged with the execution of the project, in the preparation phase. They should feel that it is "their project". We consider that this is essential for the successful execution of the project, and that it also provides an opportunity to train officers in the techniques of preparing projects.

1) The Economics of African Development, as quoted in Development Digest, January 1968, p.26.

The author is a member of the staff of the Co-operative Programme FAO/IBRD¹⁾, and he has been seconded to the Office of the Permanent Mission in Eastern Africa (PMEA). Over the last two or three years a great deal of experience has been accumulated regarding the problems of preparing projects for presentation to financing agencies, and this article intends to record some of these experiences. It points out some of the difficulties encountered and some of the ways in which it is tried to overcome these difficulties.

In general one can distinguish three phases in the process of project preparation:

- (1) the idea to do something emerges;
- (2) a project is identified, sometimes to the status of an "avant-projet";
- (3) a project is "prepared" and ready for negotiations about financing its execution.

Although this article will mainly deal with phase (3), some remarks will also be made about phases (1) and (2).

Phase (1) can be initiated in many different ways. The idea to do something may arise in the head of a technical officer, or of a local politician, a businessman, a trade organization, etc. It may be presented in a report, a newspaper article or at a meeting. If the idea is to be executed by a Government Agency it may be brought to the attention of the Director General or the Minister, and they may order some of their staff to see what it is all about, and what could actually be done about it.

1) A similar agreement between Bank and UNESCO resulted in the creation of the Co-operative Programme UNESCO/IBRD.

We enter then the phase of "Identification" (phase (2)) and the idea is now put into a form that will enable serious discussion primarily about the question whether or not detailed investigations about the merits of the original idea are justified.

In our modern days there is still another way in which phase (2) may be reached. The "idea" may arise in the minds of the members of a survey team, or survey mission (geographical, geological, economic, sociological or other survey), or the idea may be brought to the attention of members of a survey, and be included in their report. In the process the survey team may elaborate on the idea already, and put it in the form of an identified project, or it may recommend that an "Identification Mission" be sent to do that work. It is also possible that an Identification Mission visits a country with rather general terms of reference, for instance to identify agricultural, or other, projects all over the country.

Once the "identified project" has received the backing of possible executors, the question arises of who will do the detailed preparation work, how should this be done to satisfy possible financiers, and who will pay for this work?

We leave now the phase of project identification and enter phase (3), that of project preparation proper. Rosenfeld*, in discussing the technique of analysing projects, points out that the phase of preparation of projects must be considered as a separate phase although sometimes some

* F. Rosenfeld; Techniques d'Analyse et d'Evaluation des Projets d'Investissements; Presses Universitaires de France, Paris, 1966; use is made of the text of pages 11-15.

investments must be made already at this stage. However the execution of the project starts only after the preparation has led to the decision to go ahead. When that decision is taken the phase of preparation is completed and the phase of establishment or creation starts. Rosenfeld divides the preparatory phase into eight steps, as follows:-

1. a study of the environment and of the problems for which a solution is sought, and which consequently motivated the effort to formulate a project;
2. a specification of the objectives of a project, the type of action to be taken, and the order of magnitude of the proposed action;
3. a study of market conditions; supply and demand questions as well as matters of techniques and procedures;
4. a study of the technical problems to be solved, leading up to cost estimates, investigations into supply questions, methods of construction, estimates of the life of the structure proposed, and a time schedule for realisation;
5. a study of the required organization, including management;
6. a study of the economic merits of the project;
7. a study of the financial rentability of the project, leading up to a plan for its financing;
8. the selection of the best alternative and the decision to go ahead or to abandon the project.

It seems to us that steps 1 and 2 could very well be taken during the phase of project identification during which a rough idea about the economic merits of a project should be formulated. Project preparation in the sense in which we use the term here starts actually with step 3. In fact most

of the time of experts will have to be spent on steps 3, 4 and 5. Once these have been completed properly steps 6 and 7 will not prove to be very time consuming, since all the raw material should then be available.

There are various ways to perform steps 3-7, which we want to include in the process of project preparation proper. Step 8, the decision, must of course be made by the future executors of the project and is beyond the scope of the work of agencies assisting possible executors in project preparation work.

One possibility is that the staff of the agency concerned (let us say the Ministry of Agriculture) is strong, that it has done or is capable of doing all the work of data collecting and data evaluation, and of writing the project proposal, which, after approval by the Government, may be sent to the financial agencies for their consideration. The only subject for which the staff requires assistance is probably for items 6 and 7 of the above list, because they are, being basically technical officers, unfamiliar with these subjects and with the requirements of the financing agencies.

Another possibility is that the staff was strong until recently, but that the agency has recently gone through a process of renewal of staff and that the presently available officers are either new to their job, or over-burdened with day to day duties. It is still possible in this situation, that much of the preparatory work of data collecting and accumulating of experience has already been done. But the present staff may not be able to evaluate the accumulated data properly and they may not have the time to write the lengthy reports that are required by financing agencies. Obviously in this situation more assistance in project preparation is required than in the first situation.

Finally it is possible that the future executing agency has never had a strong staff, that hardly any data are available, and that the present staff is unfamiliar with the process of project preparation and with the requirements of financing agencies.

Of course, a large number of mutations of the situations sketched above can be designed, but the three mentioned above illustrate the situation sufficiently.

The First Case

In the first case project preparation can be done fairly quickly. The future executing agency knows what it wants, it has the information available and knows how to execute the project. Assistance is needed with respect to steps 6 and 7, and this can be given by a small mission of, say, two experts who are familiar with the requirements of the financing agencies. They may have to make two visits to the country. During the first one they will discuss the general issues, prepare an outline for the project application and give guidance about the writing of the report. Later they may make (say after two months) another brief visit, check on what has been written by the staff of the agency and help finalize the text of the application, so that it can be submitted to the decision makers of the country.

This technique was followed with respect to a forestry project. The Forestry Department of the country concerned had done all the "spade work" before assistance was requested. A member of the FAO/IBRD Co-operative Programme's headquarters at Rome indicated then in detail to the Department's officers how the accumulated information could best be presented. This was done in part during discussions in the Forestry Department's offices, and for the rest by drafting sections of the application in Rome. Thereafter a second series of discussions were held at Department Headquarters, in which the author participated. During these discussions various issues, specially in the fields of economics and finance, were clarified, and the text of a draft application was agreed upon. This draft was then completed by Department officers, approved by the Government (in particular the Planning Office and the Treasury) and submitted to the World Bank.

A similar procedure was followed with respect to a Range Management Project for another member of the Bank.

The Second Case

In the second situation more intensive and more time consuming assistance is required. In the first place it is necessary to make the new staff members familiar in detail with the requirements of project preparation. Also they may not realise what is involved in executing a project according to the requirements which financing agencies consider essential for achieving adequate benefits. The project preparation mission may, after general discussion of the issues, again begin with drafting an outline for the project report, discuss this intensively with the national staff, indicate what data might be available in files, or locally produced reports, and on what issues policy decisions ought to be sought from higher echelons. After this has been done, the preparation mission may leave the country for some time, and the local staff will do preparatory work (data collecting mainly) on steps 3, 4 and 5. Then the preparation mission will have to return, assist in writing the sections of the project report concerning steps 3, 4 and 5, and if all goes well it may also assist in writing the sections concerning the economic and financial aspects (steps 6 and 7). They should also see whether the necessary policy decisions have been taken (or whether adequate preparatory actions have been taken, so that policy decisions can be expected when required). It may not be possible to finalise the project report at this time, and a third visit by the foreign experts may be required.

Preparation work done for a farm-credit project may serve as an example of this case. In the agencies, responsible for preparing the project, were actually only one or two qualified officers available who could devote part of their time to this subject. They managed to organise the co-operation of various agencies, who all submitted proposals for the development of certain sections of agriculture by means of making credits available to farmers. If all these proposals had been included in the application an unwieldy project would have emerged, difficult to manage and asking very large funds.

Long discussions were conducted by the author and his colleagues with the originators of the various proposals, explaining what the World Bank might consider as a workable project and what supporting data would be required (on crops, possible increases in yield, farm costs, prices at farm level, staff requirements, training programs, organizational arrangements, costs of running the project, etc.). These discussions resulted in eliminating unattractive proposals, and in reshaping others, in order to give the whole of the project a good chance of being acceptable for the Bank's consideration. Also detailed assistance in writing sections of the application was given starting with a chapter on "Background" followed by sections on the project, financing and justification. Frequent contacts were maintained with all national agencies concerned to ensure that the project as it was shaping up step by step would be something that agencies would want to execute, and would be able to manage. A preliminary draft of the project report was shown to a Bank mission which recommended substantial modifications, requiring reconsidering and rewriting of large sections of the draft.

This process took more than two years of intensive work, and many visits to the country, as well as visits by Government officials to the Nairobi Office of IBRD.

The Third Case

Even more, and more time consuming, assistance is required in the third case. Here a step by step approach is advisable, and one or two short missions will do little good. They may be able to produce a project report, but there is then the very real danger that the national authorities consider this report as just another product of a foreign mission for the execution of which they do not feel full responsibility. May be they do not even fully agree with the contents of the report, but consider that they better go along with it, because they need the loan from the financing agency which sponsored the preparatory mission. In such cases the success of the execution of the project is already in doubt. In short, in the case which we are considering now, frequent visits by the foreign experts are advisable, and it may even be necessary to station one or two experts for a considerable time in the country.

During the initial visit the national agency's officers ought to be made familiar with the concept of a project in the sense in which it is used nowadays in financial circles. This concept may be completely foreign to officers who have learned to propose actions for inclusion in Government budgets. They should also be made familiar with the requirements of financing agencies, and with the idea that such agencies seldom finance all the cost of the project. Also a clear distinction between investments and current expenditures must be given at this stage. Thereafter a careful review of the information available, how up-to-date it is, and in how far it will stand up to scrutiny by foreign experts must be made. On this basis an assessment can be made of what data are not readily available and which ought to be collected either from files, or libraries, or in the field. At this point the preparation mission may encounter some difficulties. Sometimes the local officials are not quite convinced that all these data are really required to launch a project successfully. In other cases they do not know how to go about collecting the required data, or they do not have the staff or the financial resources to do this work. This last remark may sound trivial, but it has actually occurred to us, that field investigations could not be made because there was no money to buy petrol to run the landrover or to pay per diem to the officers while on "safari". In case a considerable amount of information ought to be collected in the field there may be need for a provisional project, that can be executed under an agreement with UNDP, or another source of finance, by members of the staff of a UN organization, or a private consulting firm. In our region ADS¹⁾ can play a very useful role in such cases, provided finance is available to pay for its services.

1) The Agricultural Development Service (ADS) is an autonomous unit attached to the World Bank's Permanent Mission in Eastern Africa, established for the purpose of assisting governments in that region in the organization and execution of agricultural development programmes. To that end ADS may contract with interested governments to second staff to assist them primarily in management and secondarily in field organization of agricultural development projects. ADS participation in the preparation of a project in no way implies a commitment by the World Bank to its financing.

If a provisional project is indicated (research project, pilot project, training project) the preparatory mission would probably do well to leave the country after it has made clear why this provisional project is needed, what is involved and how it can be organized and financed. In other words the mission should in this case plan to assist in preparing the provisional project instead of the full scale project. The authorities of the country need then some time to consider the issue and to take the necessary decisions. The preparation mission should return when field work on the provisional project is on its way to check whether it will produce the information required for the preparation of the full scale project.

After the necessary field data have been collected (and this may take a year or even more) the preparation mission should return again and take up the discussion on the main project. It is now time to compose a detailed outline for the project report, and to start writing it. From the first draft of the report it will become clear what policy decisions and organizational arrangements will have to be made to secure a successful operation of the project and what the probable consequences are for the national budget. During this stage the most difficult discussions are sometimes those about staffing of the project organizations, and especially when the authorities must be convinced that the success of the project depends very much on the quality of the management of the executing agency, and that, for this reason, it may be advantageous to include in the estimates of the ~~fixing~~ financial requirements of the project funds for the hiring of a few highly qualified officers for managerial posts. This may in fact be more economical than trying to operate the project with presently available, already fully occupied, talent.

The local authorities will now again need some time to digest these issues, and to make up their mind whether or not they want to go ahead with the project. It is thus again time for the preparation mission to leave the country and to return after a few months in the hope that it may then assist in finalising the project report. In our experience more than four or five visits are sometimes required to arrive at a good, well prepared report, that has the full backing of the national and local authorities and private groups.

This procedure can be illustrated by reporting the procedure followed with respect to a farm credit project in a country where till now little success has been obtained with agricultural credit. This is because the present credit agency does not penetrate sufficiently into the farming area, and because the agricultural services do not have sufficient practical proposals on hand about how to increase farm production. Uncertainties about land tenure are in this country also a hindrance for rapid expansion of farm credit operations.

Initially a joint FAO/IBRD mission visited the country, but it became soon clear that the basic information required for the writing of a project report was not available, and that the national agencies were not equipped to provide such information. The joint mission could do not more than discuss the principles of farm credit operations, indicating the fields in which data should be collected, and assisting in selecting possible areas for initial project operations.

Thereafter certain surveys had to be organized under the guidance of staff of the Co-operative Programme and the Nairobi Office, and FAO was moreover so kind to station a credit expert for several months in the country. Frequent and prolonged visits to the country were required, to help the surveys along, to evaluate the data collected, and to help build up sections of the project report. At every step care was taken to see whether the authorities agreed with the form of the project, as it became gradually clearer, and whether they were prepared to allocate funds and manpower to further preparation work and - later - to execution.

This work has taken about a year and a half and it was only then that a draft was available for discussion at the Ministerial level and with an exploratory Bank mission. It became than clear that more assistance, also from ~~the~~ ADS, was required before an application for financial assistance from the Bank could be produced.

A variant of the third case is that of a country that would like to have the Bank's assistance for a project for the development of crop and livestock production, and whose agencies are manned to a considerable degree by staff obtained under agreements with foreign nations and U.N. organizations. The small number of high-level nationals are overloaded with day to day work, and cannot pay sufficient attention to preparing a paper for submission to the Bank. Moreover they are not sufficiently familiar with the Bank's requirements. Another difficulty in this country was that most of the foreign experts were not fully acquainted with the characteristics of the country and its people. Consequently they were reluctant to make specific proposals and estimates of costs and benefits. However they were expected to be able to draft sections for an application to the Bank, once the major issues have been sorted out, a clear picture of local problems and possible solutions has emerged, and the Bank's requirements with respect to project preparation were understood. These requirements were discussed with local and foreign officials during two preliminary visits to the country by the author. It appeared then that some on-going, U.N.-financed, surveys would probably produce much of the information required for project preparation. It was then decided not to visit this country for some time in order to allow the surveys to be completed, and to give the local and foreign officials time to sort out their ideas. Once this was done the time had come to discuss which of these ideas might possibly be transformed into a bankable project, and what procedure should be followed in the writing of a proper application. These discussions were conducted by an exploratory mission, which concluded that more time should be allocated to accumulating data, and to gaining experience with modern cultivation and trading methods, before a bankable project could be organized.

Another variant of case three is that of a request by a Development Corporation for Bank assistance in the financing of a ranching project. It appeared in this case that the high level staff of the Corporation were too few in number and were too busy with day-to-day work to be able to spend adequate time on project preparation. It also appeared that much of the information which the Corporation wanted to use for project preparation was insufficiently specific and solid for that purpose. In

this case it appeared that the best way to move forward was for the Corporation to make a contract with ADS. A team of staff members of ADS spent a few months in the field for on-the-spot investigations about soils, water, cattle diseases, availability of cattle, growth rates of animals, marketing arrangements, costs of developments, etc. They made detailed and specific plans for the development of existing and new ranches, which were laid down, with the assistance of staff of the Nairobi Office, in a report to the Corporation. The report was accepted by the Corporation (which was expected, because frequent consultations had taken place between officers of the Corporation and those of ADS and the Nairobi Office), and after approval by the Government, the report was submitted to the Bank as an application for financial assistance. This was a special case because in the normal course of its work the Permanent Mission prefers to assist national agencies in writing their own reports, rather than writing complete reports for them.

Conclusion

To return to the first case: this type of project preparation can conveniently be done by a mission sent to the country from headquarters of a U.N. organization. In the second case this becomes already more difficult because three (or even more) visits are required. And this is a fortiori so in the third case, when often five, six or more visits are required. It is obvious that in these cases officers of regional offices, or those stationed in the country, should be called upon. In these cases one cannot properly talk any more about "a project preparation mission". What is called for is a period of assistance, with several visits, field investigations, intensive correspondence, several phone calls and frequent consultations.

From our experience we know that the first case (a strong staff almost able to write the project report) is rare, and will become even rarer. The second case (there was a strong staff, but the present one is not fully able to write the report) is becoming more common, and it is to be expected that there will be quite a number of the third category cases.

It might be of interest to the reader to note that the Nairobi Office of the Bank together with ADS, and often in connection with the Co-operative Programme FAO/IBRD, have in the past three years been involved, in one way or another, in assisting in the preparation of some 30 agricultural projects in 10 Eastern African countries. For about half a dozen of these projects finance has now been arranged, and for another half a dozen negotiations are in progress. This gives a general idea of the scope of our work but also of the fact that the preparation of a good project is a time consuming process.

D.R. Groenveld

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