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LOAN COMMITTEE 1971

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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

March 5, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Kenya - Kamburu Power Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated March 5, 1971 from the Eastern Africa Department, entitled "Kenya - Kamburu Power Project" (LC/O/71-30).

2. Comments, if any, should be sent to reach Mr. Kaji (ext. 4917) by 5:00 p.m. on Monday, March 8.

3. It is planned then, if the Committee approves, to inform the Government and representatives of the Kingdom of Sweden, the Tana River Development Corporation and the East African Power and Lighting Company that the Bank is prepared to begin negotiations for the proposed loan on the terms and conditions referred to in the attached memorandum.

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

CONFIDENTIAL

LC/O/71-30

March 5, 1971

LOAN COMMITTEE

Memorandum from the Eastern Africa Department

KENYA: Kamburu Power Project

I. INTRODUCTION

1. In September 1969, the Government of Kenya requested assistance from the Bank for financing the Kamburu power project which forms the second phase of the Seven Forks hydroelectric development on the Tana River and the first development under the scheme agreed between Kenya and Uganda for the coordinated development of power sources in the two countries.

2. While the proposed project constitutes the Bank Group's first operation in the power sector in Kenya, the history of the Bank's involvement with the development of generating facilities in the country dates back to 1966 when an economic mission studied the power sector in Kenya and Uganda and recommended that possibilities for interchange of power between the two countries, utilizing the existing bulk supply transmission line, be investigated. Meetings were held between representatives of the respective Governments and power companies during 1968 and 1969 to discuss, on the basis of studies prepared by consultants, possibilities for coordinating development of power sources in the two countries. Bank representatives attended the principal meetings as observers. The outcome of these meetings was an agreement in principle to coordinate the development of power sources and a tentative agreement was reached on the phasing of specific projects in the two countries through 1975. The Kamburu project in Kenya was selected as the first development to be undertaken under this scheme.

3. The project was appraised in the field in April 1970. Power generation, transmission and distribution in Kenya were in the hands of three companies (see paragraph 9 below) and completion of the appraisal has had to await decisions by the Government on key issues relating to organizational and financial aspects of the project. In fact, between April and July 1970, the Government made an offer to purchase shares of the main company, the East African Power and Lighting Co. Ltd. (EAP&L) and, by July 1970, had purchased a sufficient number of shares to gain control. During the period May 1970 to February 1971, correspondence was exchanged and discussions were held with representatives of the Government, the power companies, their consultants and their principal creditors. The proposed loan has been prepared on the basis of the

proposals for the organizational and financial framework explored during such discussions.

4. The proposed loan would be the sixth to Kenya; previous Bank lending amounts to $43.0 million. In addition, there have been eleven IDA Credits totalling $61.3 million. The FY 1971-75 lending program for Kenya is attached.

II. THE PROJECT

5. Attached is a draft yellow cover report entitled "Appraisal of the Kamburu Power Project of the Tana River Development Company Ltd." The report recommends a Bank loan of $23 million for a term of 25 years including a three and one-half year grace period. Tana River Development Company Ltd. (TRDC) would be the borrower, and the loan would be guaranteed by the Republic of Kenya.

6. The project, which would meet the demand for electric power in Kenya up to 1976, consists of a hydroelectric generating plant with related step-up substation, a 220 KV single circuit transmission line from Kamburu to connect it to the national grid, and a 132 KV single circuit transmission line to connect Kamburu with the existing Kindaruma power station. The capacity of the hydroelectric station would be 60 MW (two units of 30 MW each) with provision for addition of one more 30 MW unit when needed. Concurrently with the work on this project, the East African Power and Lighting Co. Ltd. (EAP&L) may have to install a 12 MW industrial gas turbine for commissioning in 1973 to meet any anticipated shortfall in supply prior to commissioning of Kamburu in 1974. Should this be necessary, the EAP&L would finance this investment from its own funds.

7. The project is estimated to cost $37.5 million excluding interest during construction. Of this, $26.1 million (70%) would be foreign exchange. Sweden has offered to provide $6 million towards meeting the foreign exchange costs. The proposed Bank loan of $23 million would cover the balance of the foreign exchange costs amounting to $20.1 million as well as interest during construction on the Bank loan estimated at $2.9 million. The local currency expenditures amounting to $11.4 million would be financed from internally generated funds of the power companies; TRDC would provide an estimated amount of $2.3 million towards local currency expenditures from surpluses expected to accrue to it and the balance of $9.1 million would be provided by a loan from EAP&L to TRDC on terms similar to those of the proposed Bank loan except that there would be no commitment charges and interest would be 9% per annum.

8. The internal financial rate of return would be between 13% and 20% with a likely intermediate rate of about 16%.

III. STRUCTURE OF THE POWER INDUSTRY

9. The industry is currently composed of three entities: The East African Power and Lighting Co. Ltd. (EAP&L), Tana River Development Company Ltd. (TRDC) and The Kenya Power Co. Ltd. (KPC). The EAP&L is the only entity of real substance. The other two, TRDC and KPC, were set up to own facilities for hydro generation in Kenya and importation of power from Uganda and are in fact operated and managed by EAP&L. EAP&L provides the necessary staff for operating the facilities and purchases all power produced and imported at "ascertained cost", i.e., actual operating costs and debt service. The nominal share capital (K£ 100) of TRDC, until its recent acquisition by the Government, was held equally by the Government, the EAP&L, Power Securities Corporation (PSC), the parent company of the Balfour Beatty Group which until recently dominated EAP&L management, and the Commonwealth Development Corporation. The share capital (K£ 100) of KPC is held equally by the Government, EAP&L and PSC.

10. The Government, in fulfillment of its avowed policy that the affairs of this important industry should be in public hands, has acquired, through a bid on the open market, over 51% of the outstanding voting stock of the EAP&L. The Government has also acquired 100% control of TRDC and on completion of formalities plans to do likewise with respect to KPC. Having obtained control of all the companies in the industry, the Government plans to integrate them in order to rationalize the structure of the industry. Such a measure, however, will need to be preceded by a study of the legal and financial complexities involved, and we propose to seek assurances from the Government that consultants will be retained, on or before December 31, 1971, to recommend how the existing structure should be rationalized. Since any rationalization plan must affect TRDC, our borrower, the Bank's approval would be required before implementation of any measures to alter the structure of the industry.

11. Rationalization will take some time and the Government has devised interim arrangements which call for two operating entities -- one for power generation and transmission and the other for distribution. The Government intends that until it finalizes plans for integration of the industry, major new generation and transmission facilities should be carried out by an entity under its exclusive control, which limits the choice at this time to TRDC. EAP&L will continue to own and operate the generation, transmission and distribution facilities it has at present. It will also continue to provide the management and staff for operating TRDC and KPC. EAP&L's role in the industry will only be affected to the extent that, apart from previously planned additions to its existing thermal generating station, it will henceforth limit its new investment in the power sector to the development of distribution facilities. KPC, even after acquisition by the Government, may exist as a separate company for a while because immediate merger with TRDC may entail complications

in respect of outstanding debentures. KPC will not, however, undertake any new investment.

12. These interim organizational arrangements proposed by the Government are satisfactory. I therefore recommend that the Bank accept TRDC as the borrower provided we receive assurances that:

(a) EAP&L would, under a revised Bulk Sales Agreement acceptable to the Bank, undertake to purchase and/or pay for at least 1 kwh of power from TRDC. This additional provision in the existing agreement would make EAP&L liable for the full "ascertained costs" of TRDC which would include debt service (amortization and interest) and operating costs irrespective of the amount of power actually purchased by EAP&L.

(b) EAP&L would, and the Government would permit it to, earn a minimum rate of return which would be sufficient to cover debt service, reasonable dividends and operating costs of the industry as well as provide a reasonable amount for financing future investments in the industry. We believe that a minimum rate of return of 10 percent per annum during 1972-74 and 8.5 percent in other years would meet the requirements. This can be achieved without raising the rates applicable to EAP&L's customers.

13. Such assurances are essential as TRDC's ability to service its debts is entirely dependant on EAP&L's commitment and ability to meet such obligations.

IV. ISSUES AND HIGHLIGHTS

Financing Plan for Local Currency Expenditures

14. During discussions with the Government and EAP&L/TRDC it was agreed that the industry's revenues which presently accrue only to EAP&L would be redistributed between EAP&L and TRDC in a manner more appropriate to their future roles so that each would earn reasonable amounts for future development.

15. In view of the need to achieve the desired redistribution of revenues with the least possible legal and legislative formalities, which could delay commitment of financing for the project and hence its commissioning by mid 1974 when additional power is expected to be required, a "surcharge" mechanism was evolved to permit TRDC to sell power to EAP&L at a price which would not only cover operating costs and debt service

(interest and amortization) as at present but would in addition provide cash for meeting a part of TRDC's investment program. On the premise that both EAP&L and TRDC should earn adequate amounts for financing future development while at the same time ensuring that EAP&L would continue to earn a reasonable rate of return and be able to maintain its dividend, it was proposed that the level of surcharge be initially fixed at 75 percent of TRDC's "ascertained cost" for the project implementation period 1971-74. This level of surcharge would have yielded about $5.3 million which TRDC would apply towards financing the local currency expenditures for the project estimated at $11.4 million. The balance of $6.1 million of the local currency costs was to be met by a loan from EAP&L to TRDC. The EAP&L was a party to these discussions and concurred with these arrangements.

16. Subsequent detailed financial analysis by the Bank indicates that payment of the 75 percent surcharge by EAP&L and the resultant redistribution of earnings could lead to a marked disparity in rates of return (net operating income as percentage of average net fixed assets in service) earned by EAP&L and TRDC/KPC (the two bulk supply companies whose accounts have been consolidated by us for purposes of meaningful comparison).

17. As the Appraisal Report (paragraph 6.17) points out, objection might be raised to the disparity between the rates of return earned by EAP&L (average 9 percent for period 1971-74) and the Government owned TRDC/KPC (average 13 percent for period 1971-74) as adversely affecting the book value of shares held by the minority shareholders of EAP&L. The report therefore recommends an alternative approach for redistribution of revenues based on the criterion that the rates of return earned by EAP&L and TRDC/KPC combined should be approximately equal each year. On the basis of current estimates it is believed that a variable annual surcharge (paragraph 6.18 of the Appraisal Report) yielding approximately $2.3 million during the period 1971-74 would permit both EAP&L and TRDC/KPC combined to earn a roughly equal rate of return each year. The balance of the local currency expenditures would be met by a larger loan of $9.1 million from EAP&L.

18. From the Bank's point of view as a creditor and development finance institution the sharing of revenues between EAP&L and TRDC is of limited interest. Our primary concern is to ensure that the industry has adequate revenues to meet its commitments. This we hope to achieve by seeking assurances recommended in paragraph 12 of this memorandum. While we see merit in the alternative approach recommended by the Appraisal Report in that it attempts to be more equitable, it is quite possible that this whole exercise may in fact have very short-lived relevance if the integration of the industry is implemented in the very near future. Further the proposal of a fixed 75 percent surcharge was one that was worked out after extensive discussions not only between the Bank and the parties concerned, but perhaps more importantly between the

Government and the EAP&L. In light of what is stated above, I recommend that we start negotiations on the basis of the alternative approach recommended by the Appraisal Report, pointing out the possible danger of a substantial disparity in the rates of return earned by the two companies, but be prepared to revert to the original proposal should the Government and the power companies press strongly to retain it.

Financial Performance Tests

19. The minimum rate of return which we expect EAP&L to earn (10 percent during 1972-74 and 8.5 percent thereafter; see paragraph 12) is computed on the assumption that the alternative approach recommended by the Appraisal Report is accepted. Adoption of this approach would mean that TRDC/KPC combined would earn approximately the same rate of return as EAP&L. If, however, we decide at negotiations to revert to the original proposal of a fixed 75 percent surcharge for the project construction period, this would as stated involve a larger transfer of revenues from EAP&L to TRDC and consequently have the effect of increasing the rate of return (expressed as net income as percentage of net fixed assets) of TRDC/KPC and reducing that earned by EAP&L. Since such transfer is within the power industry we would be satisfied if EAP&L after paying the increased surcharge earned on an average a return of 8.5 percent. An adequate rate of return for TRDC/KPC is ensured by the higher level of the surcharge.

20. In addition to a rate of return covenant, we propose to obtain agreement on a debt service limitation for the industry as a whole. We propose to seek a minimum debt service coverage of 1.5 times, the test to be applied on the basis of pro-forma consolidated accounts for all companies in the industry.

Overrun Commitment

21. The Appraisal Report (paragraph 6.19) recommends that we seek assurances from the Government that it would meet any financing gap that may arise by providing a loan to TRDC. I concur with this recommendation except that I do not propose to stipulate that the Government should make available any such funds required in the form of a loan to TRDC. TRDC is a wholly Government owned company with a nominal share capital and it is possible that the Government may wish to provide the necessary funds as additional equity rather than as a loan. We should be satisfied with the usual assurance from the guarantor to provide necessary funds on mutually acceptable terms.

Security

22. TRDC has outstanding debentures amounting to about $14 million which are secured by a floating charge on all present and future assets (other than land). The Bank would obtain a pari passu charge on these assets, and the Government is in the process of making the necessary arrangements with the existing creditors of TRDC. We have already been

advised that Commonwealth Development Corporation, the principal creditor, has agreed to our participation, and we do not propose to present the proposed loan to the Executive Directors until we have written evidence of consent from the other creditors. Completion of legal formalities finalizing such arrangements would be a condition of effectiveness for the loan. However, if during negotiations it appears that there may be delays in finalizing such arrangements and that work on the project would be held up, we should be prepared to reach an agreement on a limit for allowable disbursements while legal formalities are completed.

TRDC/EAP&L Management

23. EAP&L currently has adequate and competent management. TRDC is negotiating a revised Management Agreement with EAP&L which would provide for its broader management needs. While the Government has stated that it does not intend to interfere with EAP&L's operations, we believe that we have a very direct interest in ensuring that EAP&L has continued good management not only to run its own affairs but those of TRDC as well. To this end we propose to seek assurances from EAP&L that it will not make any appointments to the positions of the Chief Executive, the Chief Engineers in charge of Generation and Planning and the Chief Accountant without the Bank's approval of the qualifications and experience of the candidates proposed.

Water Use

24. The Kamburu power station will be located upstream of the existing Kindaruma power station and will use the same water. Hence, no further allocation of water, other than what has already been allocated for Kindaruma, is necessary. The Government has agreed that water allocated for hydro generation will continue to be available and that it will provide assurances to that effect.

25. An interim report prepared by consultants retained to carry out a preliminary survey of water and land resources of the Upper Tana Basin has indicated that there are perhaps as many as 250,000 acres in the Upper Tana Basin, about 190,000 acres of which are upstream of Kamburu, suitable for improvement by irrigation. An irrigation scheme of such magnitude, if it were to be fully implemented, would reduce the availability of water for power generation and hence reduce power output.

26. Irrigation in Kenya has so far been limited to a number of small-to-medium-scale schemes (6,000 hectares in all) and only modest expansion is planned during the 1970-74 Plan. We have held the view that costly irrigation schemes cannot have a high economic priority while there is still much potential for developing dry land farming, but concur with the Government's view that increasing population pressure will eventually make large-scale irrigation desirable. Obtaining land for resettlement through irrigation may moreover be politically easier than tackling the problem through the redistribution of land between tribes. There are three major areas of

irrigation potential: the Lower Tana area, the Upper Tana and the Kano Plains. By far the largest potential lies in the Tana River Basin and the Bank preinvestment survey mission to Kenya in November 1970 recommended, and the Government accepted, that an integrated survey of the Tana River Basin should be carried out to explore further the possibility of large-scale agricultural development in the area. This survey would also investigate the possibilities of upstream storage which could assist in river regulation and increase the amount of water available for other uses in the dry season by storing flood flows in excess of the amounts required for hydroelectric generation.

27. Subsequent to the issuance of the attached yellow cover report, an analysis to examine the possible effects of upstream irrigation on the economics of the proposed project was undertaken. The results of this analysis are provided in the addendum to the report. In the absence of any plans for irrigation and of much of the data on which such plans could be based, the analysis has had to be made on the basis of necessarily arbitrary assumptions concerning the phasing of irrigation development, the type of crops that might be cultivated and irrigation water requirements. While such analysis must be considered as subject to a fair margin of error, it indicates that the cost of replacing the output at Kamburu that would be lost if the whole potentially irrigable area were in fact to be cultivated is unlikely to have a substantial impact on the economics of the project.

28. The Appraisal Report (paragraph 4.13) recommends that we seek assurance from the Government which would circumscribe the terms of reference of such an integrated basin study in a manner that would give priority to power generation. I do not believe that this is appropriate. We should permit an unfettered study. Accordingly, I recommend that we inform the Government that it would need to obtain the Bank's consent to any alteration in the water allocation for hydro generation, but such consent would not unreasonably be withheld should the Government at some future time decide, on the basis of comprehensive and cogent studies satisfactory to the Bank, that it would be more economic to utilize Tana Waters for irrigation rather than power generation.

Swedish Participation

29. The Swedish International Development Authority (SIDA) has been interested in this project for some time and their representative was associated with the appraisal. SIDA has indicated that Sweden would be prepared to lend $6 million equivalent for the foreign exchange costs of the project. The proposed Swedish Credit would go to the Government on IDA terms and would be onlent to TRDC on terms identical to the Bank loan. Documentation for the financing will follow the pattern for other projects financed jointly with Sweden. It is expected that the documents for the proposed Swedish Credit will be signed at the same time as the Bank loan documents and that the Swedish Credit will be made effective prior to, or simultaneously with, the effectiveness of the Bank loan.

Rural Electrification

30. The EAP&L has in the past devoted a part of its development expenditure to rural electrification. This was done on a commercial basis by selecting financially remunerative schemes from a list prepared by the Government.

31. The Government may wish to utilize the surplus resulting from the difference in the borrowing and relending terms of Swedish Credit for financing an expanded rural electrification program. This program envisages electrification of some 25 to 30 towns and villages; some of these schemes are not expected to be financially remunerative. During negotiation we hope to learn of the Government's plans for carrying out these schemes and the role EAP&L is expected to play. If the Government's plans require that EAP&L undertake some or all of such schemes irrespective of whether EAP&L considers them financially remunerative, we propose to seek assurances from the Government that it would provide the necessary capital funds and underwrite any operating losses suffered by EAP&L on such unremunerative schemes.

Documentation

32. In addition to the Joint Financing Agreement and the Loan and Guarantee Agreements we, in view of EAP&L's pivotal role in this operation, propose to enter into an agreement with EAP&L in which it would accept the usual covenants obtained from a beneficiary of a Bank loan and agree to other requirements within its control.

Retroactive Financing

33. The Bank at the request of the Government and TRDC has already agreed to recommend to the Executive Directors reimbursement out of the proceeds of the proposed loan an amount of about $300,000 paid to the consultants for detailed engineering.

V. THE ECONOMY

34. An economic report entitled "Economic Development Prospects in Kenya" (Report No. AE-6a, in two parts) was distributed on October 31, 1969. The economic mission which visited Kenya in April/May 1969 examined the draft 1970-74 Development Plan and found it to be realistic and generally well conceived. The Plan has since been published. An economic mission visited Kenya in November 1970 and its report is being prepared. In general, the Government has made a good start in implementing the Plan. Economic growth by the end of 1970 was approximately in line with Plan target in spite of climatic setbacks in 1969, and the 1970/71 budget was consistent with the public expenditure goals set by the Plan.

35. On the basis of past economic performance and the sound policies and plans for future development, Kenya will continue to warrant substantial external assistance for a long time. In view of its low per capita income and the limited prospects for its exports, it is desirable that Kenya should obtain the major proportion of external assistance on concessional terms. However, since its debt service ratio is relatively low (6.5 percent in 1969), Kenya can afford to undertake a moderate amount of borrowing on conventional terms.

VI. RECOMMENDATION

36. I recommend that the Bank invite representatives of the Republic of Kenya, the Kingdom of Sweden, the Tana River Development Corporation and the East African Power and Lighting Co. to negotiate a loan of $23 million equivalent substantially on terms and conditions set forth in the Appraisal Report subject to the exceptions stated in paragraphs 18, 21 and 28 of this memorandum, with which the Public Utilities Projects Department agrees.

Michael L. Lejeune
Director

Attachment

Population: 9.9m.
GNP Per Cap.: $120

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

		1971	1972	1973	1974	1975	1976
Livestock II	IDA			8.0			
Irrigation - Kano Plain	IDA					5.0	
Agricultural Credit II	IDA			6.0			
Smallholder Tea III	IDA			3.0			
Rural Development	IDA				4.0		
Crop Development I	IDA			3.0			
Crop Development II	IDA				3.0		
Agriculture Unidentified	IDA					6.0	
Education III	IDA			7.0			
Education IV	IDA				10.0		
Power - Kamburu Hydro	IBRD	29.0					
Tourism	IBRD			4.0			
Airport - Nairobi	IBRD		20.0				
Highways IV	IBRD		10.0				
"	IDA		10.0				
Highways V	IBRD					10.0	
"	IDA					10.0	
Road Maintenance Equip.	IDA	12.6					
Water Supply - Nairobi	IBRD	8.3					
	IBRD	37.3	30.0	4.0		10.0	
	IDA	12.6	10.0	27.0	17.0	21.0	
	Total	49.9	40.0	31.0	17.0	31.0	
	No.	3	3	6	3	3	

Eastern Africa Department 2/16/71

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

March 4, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Afghanistan - Khanabad Irrigation Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated March 4, 1971 from the South Asia Department, entitled "Afghanistan - Proposed Credit for the Khanabad Irrigation Project" (LC/0/71-29).

2. Comments, if any, should be sent to reach Mr. Aiyer (ext. 2778) by 5:00 p.m. on Tuesday, March 9.

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

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

CONFIDENTIAL

LC/O/71-29

March 4, 1971

LOAN COMMITTEE

Memorandum from the South Asia Department

Afghanistan - Proposed Credit for the Khanabad Irrigation Project

1. Attached is an appraisal report (PA-75) dated February 16, 1971 recommending that the Association make a Credit of $4.0 million equivalent to the Kingdom of Afghanistan to help finance the Khanabad Irrigation project. It is estimated that the Credit will be disbursed over a period of about 4 years.

Background

2. To date the Association has made three Credits to Afghanistan. The Education Project (Credit No. 68-AF, for which $3.5 million was approved in 1964) was not implemented, and the Credit was cancelled at the request of the Government in 1970. The Highway Maintenance Project (Credit No. 158-AF, signed in June 1969) provides $5.0 million to improve highway maintenance operations and the secondary road system in the Eastern region of Afghanistan. The Agricultural Development Bank received $5.0 million (Credit No. 202-AF) to help finance farm mechanization, shallow well pumps and improvements in minor irrigation works through a Credit signed in June 1970.

3. Despite nominally high levels of bilateral aid during the last decade, economic growth in Afghanistan has barely kept pace with the increase in population. Investments have been largely for infrastructure projects such as the primary road systems, the Helmand Valley scheme, the Nangarhar Irrigation project, the Mahipar power plant and the Kandahar airport. The benefits from these large projects have been slight compared to the massive amounts of capital expended. About three-fourths of the country's development expenditures have been financed from foreign sources. Efforts at mobilization of domestic revenues have been inadequate, and the short-run prospect for a significant increase in public revenues is not good. The balance of payments continues to show a deficit, and the debt service ratio for 1969/70 was 25 percent.

4. The IDA program for Afghanistan consists of projects which offer a reasonable chance of bringing about economic improvements on a moderate scale in key areas of the economy, such as agriculture, which accounts for over 50 percent of GNP. The proposed lending program is summarized in Annex I.

5. The rehabilitation of irrigation facilities in the Kunduz Khanabad valleys was first suggested as a suitable project for Bank Group financing by the economic mission of 1961/62, and in 1962 the Government formally requested assistance for an agricultural project in the area. The aim was to improve the existing traditional irrigation systems, which required

continuous reconstruction and repair, by introducing permanent structures and better water and soil management. After a long gestation period, during which background studies were prepared by SOGREAH (Reconnaissance Survey, June 1966, financed by an IBRD technical assistance grant), Development and Resources Corporation (Feasibility Study, July 1970, financed by UNDP), and FAO (Summary Project Submission, August 1970), the project was appraised in October/November 1970.

The Project

6. The Khanabad valley of the Kunduz province is one of the most fertile areas in Afghanistan. The irrigation system in the valley consists of loose-stone structures to divert water from the river into irrigation canals, with brushwood drops controlling the flow through the canals to primitive farm turnouts. As there is no regulation of water use, fields at the head of canals receive too much water while those lower down do not get enough. During periods of high water flow, too much water enters the canal breaching their banks and flooding the valley. Several times a year diversion structures are washed away and inadequate flows enter the canal, causing water shortages. Maintenance is carried out by the farmers themselves (Appraisal Report, paragraphs 3.07 and 3.08). There are about 72,000 inhabitants in the area, of whom 42,000, representing about 6,000 families, are classified as rural (paragraph 3.09).

7. The project proposed in the Appraisal Report would be the first phase of a program for modernizing the irrigation system in the valley (paragraphs 4.01 and 4.02). It would cover an area of 30,000 ha and would include civil works consisting of a diversion weir on the river, a main canal and link canals, water control structures, drainage facilities and bridges and culverts (total cost $4.2 million). In addition, consultants services ($635,000) would be included for design and supervision of construction, agricultural extension and preparation of a second project. Land acquisition, vehicles and equipment, local staff cost and contingencies account for another $1,165,000. The total cost of the project is therefore estimated at $6 million, of which we propose that 67 percent, or $4 million, would be provided under the IDA Credit. The Borrower would be the Royal Government of Afghanistan.

8. The major benefit of the project would be a substantial increase in crop production in the valley resulting from improved water control. The rural incomes would be improved as a direct result of the project (paragraph 6.05). The present annual gross value of production in the area is about $5.0 million and at full development it is expected to reach about $9.3 million; of course, some of this increase (i.e. to $6.9 million) might be expected even without the project because of improved supply of fertilizer, seeds, etc. The net value of agricultural production after deducting on-farm costs would be $5.8 million compared with $4.0 million without the project; after deducting operating and maintenance costs, the direct annual benefit to the economy would be about $1.7 million. The project is expected to yield about eighty percent of the benefits, or about $1.36 million, within five

years of completion of construction. The project would help reduce the food grain deficit and improve the balance of payments position through foreign exchange savings (paragraphs 7.02 and 7.03; Annexes 9 and 10).

9. The project would be implemented by the Ministry of Agriculture and Irrigation. Currently the Ministry consists of nineteen departments (each of which is headed by a "President") including one each for the Sardeh, Parwan and Nangarhar irrigation projects and one for a recently approved Asian Development Bank irrigation project in the neighboring Kunduz Valley (Figure 2). We propose that a separate department be established in the Ministry to assume the responsibility for the execution of the Khanabad project. This is in line with present practice and is acceptable to the Ministry. Most of the staff of the Department would be located at Kunduz, including the President who will be directly assisted by consultants.

10. As stated, the total project cost is estimated at \$6 million, and the foreign exchange cost is estimated at \$3 million; the IDA Credit would provide all of the foreign exchange cost and would also meet about \$1 million of local currency expenditures. This is considered necessary to avoid delays in project execution in view of the acute shortage of domestic resources.

11. In addition to roughly \$4 million required for project implementation we propose to include an amount sufficient to enable Afghanistan to repay the Association \$277,000 outstanding under Credit No. 68-AF. This Credit was cancelled last year when the Government requested even more time to re-think the educational needs of Afghanistan before undertaking the investment for which the \$3.5 million Credit had been approved in 1964. Prior to cancellation the only disbursements under this Credit were for consultant services, and the Afghan authorities had originally requested that this \$277,000 be converted into a technical assistance grant. We proposed outright repayment. However, in view of doubts on both sides concerning the current appropriateness of the project and construction standards proposed for its buildings, and also taking into consideration Afghanistan's current foreign exchange situation, it seems best to compromise on the solution proposed here - which represents an admittedly generous re-financing or consolidation of the relatively small amount due on a cancelled project.

12. The attention of the Loan Committee is drawn to paragraph 4.05 which deals with the possible question of international waters.

Issues

13. We agree in substance on all the recommendations in the Appraisal Report (Chapter VIII). There are, however, two issues, both of which relate to the new Department.

(a) Timing: The Projects Department recommends that the establishment of the new department responsible for the project be made a condition of presentation of the Credit to the Board (paragraph 8.03). We agree that the establishment of the new department at the earliest possible date is desirable for proper implementation of the project. The Government also agrees that such a department should be established, and I expect that this can be done by the end of October. However, it would be awkward for the Government to take final steps toward this end before the vote of our Executive Directors on the Credit. Also, by making this a condition of presentation, time will be lost unnecessarily. I recommend, therefore, that we reach an understanding during negotiations that the Department be created before the Credit is declared effective.

(b) Approvals: The Appraisal Report recommends that the appointment of the first president and all subsequent presidents should be subject to prior approval by the Association (paragraphs 8.01 (b) and 5.04 (b)). The department is to be a new entity without any record of management competence; in Afghanistan there is also a real risk of political interference. We agree that good management is very important to the success of the project, but feel that the approval clause is not appropriate. Moreover, it almost certainly will not be acceptable to the Government. There is every indication that the Government will consult with the Association with a view to obtaining our concurrence on the first appointment, and I intend to make it clear to the Government that the Association would expect the first president to remain in his position until the project is completed. Furthermore, this project cannot succeed without close supervision and will require at least semi-annual supervision missions in addition to the continuous monitoring by the Resident Mission and the operational missions of the Area Department. In my judgment, therefore, prior consultation on these appointments, rather than approval, will be sufficient.

Recommendation

14. Except for the reservations explained in paragraph 13, I concur with the recommendation in paragraph 8.04 of the Appraisal Report and propose that the representatives of the Royal Government of Afghanistan be invited to Washington to open negotiations. Taking into account the point made in paragraph 11, I recommend that the amount of the credit be $4.3 million.

Attachment

Gregory B. Votaw
Deputy Director

Annex I: "Afghanistan - 5 Year Lending Program"

Population: 15.8 m
GNP Per Cap.: $70

IVa. AFGHANISTAN - 5 YEAR OPERATIONS PROGRAM
(By Fiscal Year - Amounts in $ millions)

			1971	1972	1973	1974	1975	1976
5-AFG-AC-02	Agricultural Bank II	IDA			5.0			
5-AFG-AC-03	Agricultural Bank III	IDA						5.0
5-AFG-AI-01	Irrigation - Khahabad	IDA	4.0					
5-AFG-AI-03	Irrigation - Farah Rud	IDA				15.0		
5-AFG-AL-01	Livestock I	IDA		4.0				
5-AFG-AL-02	Livestock II	IDA					4.0	
5-AFG-AD-01	Rural Development Unidentified	IDA					5.0	
5-AFG-DD-01	DFC - IDBA I	IDA		3.0				
5-AFG-DD-02	DFC - IDBA II	IDA					3.0	
5-AFG-QQ-01	Tourism I	IDA		2.0				
5-AFG-QQ-02	Tourism II	IDA					2.0	
5-AFG-TA-01	Kabul Airport	IDA	3.0					
5-AFG-TA-02	Air Transportation	IDA				3.0		
5-AFG-TH-02	Highways II	IDA			10.0			
5-AFG-TH-03	Highways	IDA						10.0
		IDA	7.0	9.0	15.0	18.0	14.0	15.0

	1964-68	1969-73	1972-76
IDA	3.5	41.0	71.0

P & B 3/1/71

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

March 3, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Malawi - Lilongwe Land Development Program

1. The Committee is requested to consider, without meeting, the attached memorandum dated March 3, 1971 from the Eastern Africa Department, entitled "Lilongwe Land Development Program - Phase II Project" (LC/O/71-28).

2. Comments, if any, should be sent to reach Mr. John M. Malone (ext. 4901) by 1:00 p.m. on Monday, March 8.

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

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

CONFIDENTIAL

LC/O/71-28
March 3, 1971

LOAN COMMITTEE

Memorandum from the Eastern Africa Department

Lilongwe Land Development Program

Phase II Project

1. The Malawi Government has requested an IDA credit to finance the second phase of the Lilongwe Land Development Program. The first phase was financed by a $6 million IDA credit (113-MAI) signed February 5, 1968. The proposed Phase II project was appraised in September, 1970. The appraisal report, entitled "Lilongwe Land Development Program, Phase II Project" (PA-76) dated February 24, 1971, is attached. It recommends, subject to the conditions set forth in Chapter IX, an IDA credit of $7.0 million.

2. Beginning in 1967, the Bank Group has made six IDA credits to Malawi, totalling $33.3 million. In addition to credit 113-MAI, the Bank Group has made one other agricultural credit to Malawi; this was of US$3.7 million in 1968 for the Shire Valley Agricultural Development Project (Credit 114-MAI), a project with many similarities to the Lilongwe program. Progress on both projects has been good.

The Lending Program

3. On February 24, Mr. Knapp approved a revised five-year lending program for 1972-1976 totalling $40 million. A copy is attached.

The Economy

4. The latest economic report on Malawi (No. AE-5a) is dated December 12, 1969. A mission now in the field will produce an updating memorandum to accompany the proposed project in its presentation to the Board.

5. The Malawi Government still receives an annual grant-in-aid from the United Kingdom. The Government has announced that it intends to make itself independent of grant aid by 1975, a difficult but not impossible objective. In the meantime, any improvement in the budget will result in a lower grant-in-aid from the U.K. and will not add to domestic resources available to the Government for development. These will remain limited to a small amount of non-bank borrowing and an even smaller amount of borrowing from the banking system. This means that if Malawi is to carry out

a reasonable investment program, external finance will be required for a large proportion of public development expenditure, in practice at least 85%. It follows that in the majority of cases, project financing must cover a substantial part of the local expenditure costs.

6. Malawi's present external debt amounts to $147.8 million. The annual service on this debt represents about seven percent of current foreign exchange earnings. In the past Malawi has been able to obtain 80 percent of its development finance on concessionary terms. The Ministry of Finance considers that there may be specific cases, for example for self-liquidating projects, such as the ongoing power project for which an ADB loan was linked with IDA financing, in which it may be preferable for Malawi to borrow on conventional terms rather than not at all. I agree in principle, but the margin for such borrowing is very narrow. For example, if Malawi continued to obtain not more than 80 percent of its requirements on concessionary terms, the external debt ratio would rise to 15 percent in 1975 and 20 percent in 1980 even if exports were to grow continuously at not less than 9 percent a year, which is a highly optimistic assumption. The need for lending on concessionary terms is therefore clear and we do not propose any Bank lending for Malawi over the next five years.

The Project

7. The project would be the second phase of the Lilongwe Land Development Program and would be carried out over a four-year investment period, 1971/72-1974/75. The project would involve:

-- constructing about 540 miles of crop extraction road, 1,700 miles of rainfall diversion channels and boring and equipping 160 boreholes to serve an additional 240,000 acres of the program area;

-- constructing 14 service centers, each including a produce market, a 450 ton fertilizer/seed store, and associated offices and housing;

-- surveying, farm demarcation and reorganization, and land registration over about 375,000 acres of the phase I and phase II project areas;

-- continuing agricultural extension and staff and farmer training services within the phase I project area, and extending such services to an additional 24,000 farmers;

-- providing seasonal and medium-term credit to phase I and phase II project farmers by means of a revolving credit fund operated by the project administration; and establishing arrangements for cash sale of inputs to project farmers;

-- establishing a ranch to provide upgraded feeder stock for program area farmers;

-- establishing a Management Committee responsible for program policy, and for maintaining program developments until satisfactory maintenance can be assumed by central Government agencies and local councils;

-- continuing a project evaluation unit; and

-- providing eleven man-years of specialist personnel assistance to the Malawi Agricultural Bank.

Estimated project costs would total K 6.93 million (US$8.32 million) of which the foreign exchange component is about K 2.51 million (US$3.02 million) or 36% of total costs.

8. The proposed IDA credit of US$7.0 million would finance 84% of estimated project costs. US$3.02 million, or 43% of the credit, would cover the estimated foreign exchange costs. The balance of US$3.98 million or 57% of the credit would finance 75% of local currency costs. The Government would contribute US$0.91 million (11% of total project costs) and the project farmers would provide US$0.4 million (5% of total project costs) through the cash purchase of incremental seasonal farm inputs.

9. Audited accounts of the phase I project for the last two fiscal years have not yet been submitted to the Association. The Appraisal Report (paragraph 5.10) recommends as a condition for negotiation of the proposed credit for phase II that these accounts had been reviewed by the Association. While I do not treat lightly the failure to submit audited accounts promptly as required under Credit 113-MAI, I consider it inappropriate to delay negotiations as a means of resolving a credit administration problem. I understand that the Auditor General's report has in fact been completed and that the remaining problem is one of preparing the necessary extract for the Association and transmitting it. I consider that we should take the opportunity of negotiations to impress on the Government the importance of preparing and submitting accounts promptly and that we should inform the Government that we would not submit the proposed Credit to the Board until the audited accounts under the previous Credit had been reviewed by the Association.

10. It has been necessary to start development of the project ranch to prevent delays in livestock development that would be included in phase II. It is recommended, and I agree, that the Association be prepared to reimburse against the cost of ranch development since October 1, 1970. Assuming that the proposed credit is approved by the end of May, 1971, the amount to be retroactively financed would be about US$105,000. The existing project authority for phase I has followed

satisfactory procurement procedures.

Recommendation

11. I recommend that the Government of Malawi be invited to send representatives to negotiate a proposed credit of US$7 million equivalent, for the Lilongwe Land Development Program Phase II Project, substantially on the terms and conditions set forth in Chapter IX of the appraisal report, except that the condition of negotiation proposed in paragraph 9.04 would instead be a condition of submission to the Executive Directors.

Michael L. Lejeune
Director
Eastern Africa Department

Attachment

Population: 4.5 m
Per Capita Income: $61

MALAWI - PROPOSED LENDING THROUGH 1976
(US$ million)

OPERATIONS PROGRAM

		1972	1973	1974	1975	1976
Karonga Agric. Dev.	IDA	4.5				
Agric. Dev. Shire Irrig.	IDA		7.0			
Agric. Dev. (Unidentified)	IDA					7.0
DFC/Malawi Dev. Corp.	IDA					2.0
Education II	IDA			7.5		
Power II	IDA				7.0	
Tourism	IDA					3.0
Highway II	IDA				11.0	
	IDA	4.5	7.0	7.5	18.0	12.0
	No.	1	1	1	2	3

	Total 1964-68	Total 1969-73	Total 1972-76
IDA	28.0	23.8	49.0
No.	5	4	8

LENDING PROGRAM (2/24/71)

	1964-68	1969-73	1972-76		1972	1973	1974	1975	1976
IDA	28.0	23.8	40.0	IDA	4.5	7.0	7.5	11.0	10.0
No.	5	4	6	No.	1	1	1	1	2

Eastern Africa Department
February 26, 1971

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

March 3, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Senegal - Casamance Rice Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated March 3, 1971 from the Western Africa Department, entitled "Senegal - Proposed'Casamance Rice' Project" (LC/0/71-27).

2. Comments, if any, should be sent to reach Mr. Meda (ext. 4737) by 1:00 p.m. on Monday, March 8.

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

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

CONFIDENTIAL

LC/0/71-27

March 3, 1971

LOAN COMMITTEE

Memorandum from the Western Africa Department

SENEGAL: Proposed "Casamance Rice" Project

I - BACKGROUND

1. Rice is second to millet in importance among food crops in Senegal. It is in increasingly high demand and the Government has decided to intensify its efforts to increase domestic production of paddy so as to reduce rice imports which amounted to 170,000 tons ($20 million) in 1969. Total consumption in that year amounted to about 245,000 tons. Following an official request, an FAO/IBRD Cooperative Program mission identified this project in February 1970 in the Casamance region and prepared it during July and August. The appraisal mission took place in November 1970.

2. The proposed credit of $3.6 million would be the third Bank Group operation in agriculture in Senegal including the "Terres Neuves" resettlement project (US$1.3 million) which we plan to submit to the Executive Directors concurrently with the proposed rice project. It is part of the strategy of the Senegalese Government aiming at diversification of agriculture while at the same time increasing the productivity of the traditional groundnut sector.

3. The latter has been financed by the Bank Group under the agricultural credit project (IBRD loan of $3.5 million (584/SE) and IDA credit of $6.0 million (140/SE) of February 10, 1969). The memorandum to the Loan Committee on the Terres Neuves project which was circulated on February 9, 1971 (LC/0/71-17) gave an account of difficulties encountered in implementing the project, of corrective measures envisaged by the Senegalese Government and of the Bank Group's proposal to adapt its financing to the changed circumstances, in particular through cancellation of the undisbursed $3.5 million Bank loan. Recent discussions with the Senegalese Government and FED have brought out that:

(a) the Government will review the groundnut producer prices, most likely before the next planting season in May;

(b) over the 1970-71 campaign, a 3 franc retroactive bonus to the farmers is envisaged;

(c) farmers' debts will be cleared to the extent possible in such a way that no inequities will be created between those who have paid their debts in the past, fully or partly, and those who are in serious default;

(d) the application to obtain exceptional assistance from FED has been submitted and copied to the Bank. There appear to be serious gaps in the information supplied and FED has already asked the Government for clarification on a number of points. Although FED may recommend to the Government that it take some positive action to improve farmers' incentives, this is not likely to be required as a condition for FED assistance.

It is planned to reach a clear understanding on groundnut policies prior to presentation of the Terres Neuves and Casamance Rice projects to the Executive Directors. The Government has been notified that during the combined negotiations we shall expect a first round of substantive discussions to this effect to be followed by a mission in the field before the meeting of the Directors.

II - THE ECONOMY

4. A report on "Current Economic Situation and Prospects of Senegal" (AW-15a) was circulated to the Executive Directors on June 10, 1970.

5. A brief analysis of more recent economic developments in Senegal was given in the memorandum to the Loan Committee on the Terres Neuves project dated February 9, 1971.

6. The attached 5-year lending program, reviewed in June 1970, includes a proposal for one further IDA credit during the current fiscal year, for a technical education program. Five projects are scheduled to be financed in FY 1972. One of them (Dakar drainage and sewerage) may, however, have to be postponed.

III - THE PROJECT

7. An appraisal report on the project (PA-77) is attached. The project would bring about the cultivation of 9,500 ha of rainfed rice, which would be grown by some 5,000 farm families mostly in rotation with

groundnuts and other food crops. It would also involve improvement of about 2,000 ha of existing swamp rice land and the construction of rice milling and storage facilities. The project period would be ten years, but the bulk of its development would take place within the first five years (1972-1976) covered by the proposed IDA credit.

8. The project would consist in:

(a) strengthening the Sedhiou District Organization of the Ministry of Rural Development (MRD) by employing consultants to provide specialists and by adding additional Senegalese staff, and by providing vehicles and constructing housing and offices for their use. The District Organization would be responsible for carrying out the project and providing extension services to farmers (see paragraph 10). This is the most important aspect of the project, since its successful completion depends upon a strong extension service supported by an efficient project organization;

(b) constructing irrigation and drainage works for 2,000 ha of swamps;

(c) constructing 24 rice mills and related storage facilities;

(d) procuring land clearing winches and crop sprayers for leasing to project farmers;

(e) improving project area roads; and

(f) providing seasonal and medium-term credits to farmers from a revolving fund operated by the Banque Nationale de Développement du Sénégal (BNDS).

9. Project costs during the ten-year period 1972 through 1981 are estimated at CFAF 1.67 billion (US$6.02 million) of which the foreign exchange component is about CFAF 0.65 billion (US$2.6 million) or 39 percent. The proposed IDA credit, US$3.6 million, would cover 75 percent of project costs excluding taxes during the five-year disbursement period (1972-1976) or about 60 percent of overall cost. In addition to the foreign exchange expenditures over the five-year disbursement period, US$2.1 million, the credit would cover US$1.5 million equivalent of local costs. Except for US$0.1 million financed by the farmers (about 2 percent), the remaining costs would be met by the Government, partly through direct budgetary allocations and partly through the Banque Nationale de Développement du Sénégal (BNDS). The French Caisse Centrale de Coopération Economique has indicated its willingness to consider participating in the financing of the project. A CCCE contribution would likely relate mainly to the BNDS share of the project.

10. Procurement of vehicles, clearing and spraying equipment, and rice milling equipment would be by international competitive bidding. Tenders for road construction and improvement contracts would be advertized locally since the small amounts involved are unlikely to attract bidders not established in West Africa. Contracts for the construction of houses and rice milling and storage facilities would be let through tender under local competitive bidding.

11. The Government intends to set up an organization to be responsible for the execution of the project, within the Ministry of Rural Development. The organization would be basically a strengthened form of the existing Agricultural Services, operating under MRD in the Sedhiou District. To assist and train the Project Director Designate, who will manage the project from the third year on, and his staff in their duties during the first five years of the project, Government intends to employ a consulting firm which would operate under terms of reference stating that one of the main functions, from the start, would be on-the-job training of Senegalese counterparts to ensure that during the five following years the project could be managed without further expatriate assistance. An expatriate Project Director for the first two years and a Senegalese Project Director Designate who will subsequently take over management would be selected with the agreement of the Association. The appointment of the Project Organization staff required for the first year of operation would be a condition of effectiveness.

12. The rice mills built under the project would be managed as financially autonomous enterprises responsible to the project organization. They will buy all paddy in excess of family requirements from the farmers deducting a levy on milled rice to ensure recovery of direct investment and maintenance costs borne by Government. The Office National de Coopération et d'Assistance au Développement (ONCAD) will perform groundnut marketing operations for the project as it does for the country as a whole.

13. The Government cash flow as a result of the project shows a net deficit for the execution period of the project, partly because of continued subsidization by the Government of the fertilizers utilized for rice and groundnut production. While subsidization will remain necessary for some time to encourage farmers to make more intensive utilization of fertilizer, a reduction of the subsidy can and should be envisaged as farmers' benefits increase. To that effect we propose to have an annual review of the Government's subsidy policy.

IV - RECOMMENDATION

14. I recommend that the Association invite the Government of Senegal to negotiate a credit of US$3.6 million for the proposed rice development project in the Casamance region. Negotiation would be in accordance with the conditions presented in paragraphs 9.01 and 9.02 of the appraisal report.

Roger Chaufournier
Director

Attachments

Population: 3.7 m
GNP Per Cap: $190

IVa. SENEGAL - 5 YEAR LENDING PROGRAM

		($ millions)							
		Fiscal Year						Total	Total
		1971	1972	1973	1974	1975	1976	1964-68	1969-73
Agricultural Credit II	IDA			5.0					
Rice Development I	IDA	3.6							
Rice Development II - Delta	IDA			4.0					
Agric. Devt. - Terres Neuves I	IDA	1.3							
Land Settlement - Terres Neuves	IDA					5.0			
Livestock	IDA			1.5					
Vegetable Development	IDA					3.0			
Communications	IDA		2.0						
DFC	IDA						3.0		
Education I	IDA	1.0							
Education II	IDA					5.0			
Industrial Estate	IBRD				2.5				
Power I	IBRD		6.0						
Power II	IBRD					5.0			
Airport	IBRD				4.0				
Highway Maintenance	IDA			6.0					
Port	IDA				2.0				
Casamance River Navigation	IDA				2.0				
Railways II	IBRD		6.1						
Drainage & Sewerage - Dakar	IDA		3.0						
	IBRD		12.1		6.5	5.0		4.0	15.6
	IDA	5.9	5.0	16.5	4.0	13.0	3.0	9.0	35.5
	Total	5.9	17.1	16.5	10.5	18.0	3.0	13.0	51.1
	No.	3	4	4	4	4	1	2	13

Western Africa Department

2/26/71

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

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March 2, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Pakistan - Transmission and Distribution Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated March 2, 1971 from the South Asia Department, entitled "Pakistan - Loan for the Karachi Electric Supply Corporation - Transmission and Distribution Project" (LC/O/71-25).

2. Comments, if any, should be sent to reach Mr. Alsegaf (ext. 2775) by 1:00 p.m. on Thursday, March 4.

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

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

Copies for Information:

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

CONFIDENTIAL

LC/O/71-25

March 2, 1971

LOAN COMMITTEE

Memorandum from the South Asia Department

PAKISTAN: Loan for the Karachi Electric Supply Corporation - Transmission and Distribution Project

Introduction

1. Attached for consideration by the Committee is a report "Appraisal of Transmission and Distribution Project of the Karachi Electric Supply Corporation Limited" (No. PU-62, dated February 19, 1971). An established borrower of the Bank with four previous loans, the Karachi Electric Supply Corporation (KESC) has requested a Bank loan of US $10.5 million to finance the foreign currency costs of a project to strengthen and extend its transmission and distribution network.

2. To date, the Bank has made thirty-one loans in Pakistan for a total amount of US $633.4 million (net of cancellations); the Bank's net investment in Pakistan on January 31, 1971 was about US $326 million, compared to about US $282 million on December 31, 1969. The Association has made thirty-eight development credits to Pakistan, totalling US $501.2 million (net of cancellations). During this fiscal year we now expect to recommend five or six projects (including the recently approved US $25 million East Pakistan Reconstruction Credit) for IDA financing, totalling about US $70 million. This is substantially less than proposed in my memorandum on the Second Foodgrain Storage Project (LC/O/71-13, dated February 2, 1971) but the amount might ultimately be somewhat higher than US $70 million depending on the availability of IDA funds and action in Pakistan regarding an overdue reform in trade and fiscal policy. A credit of US $11 million for the Foodgrain Storage Project has just been substantially negotiated, and a credit of US $2.5 million for East Pakistan Consulting Services will be negotiated in March. Credits for EPWAPDA Tubewells (US $9 million) and Second Lahore Water Supply (US $5 million) are also expected to be negotiated well before June 30, 1971. A credit of US $30 million for the Dacca Southwest Irrigation Project should also be ready before June 30 but will be considered by the Executive Directors only after July 1. The East Pakistan Tea Machinery Project (US $5 million) referred to in the memorandum of February 2 has been deferred indefinitely. On the Bank side, a loan to PICIC has been appraised (US $30-40 million), but I am not prepared to recommend that negotiators be invited until after the Government has taken the decision on policy matters already referred to.

Background

3. A large proportion of Pakistan's recent industrial growth has been concentrated in the Karachi area, which now accounts for about 40 percent of West Pakistan's output of manufactured goods. Largely as a consequence of industrial growth, consumption of electricity in the Karachi area, where KESC

is the sole supplier, has increased rapidly -- by over 15 percent per annum -- in the 1960's, a rate which is expected to continue into the 1970's (paragraph 5.02 of the Appraisal Report). Consumption by industrial users which account for 64 percent of KESC's sales, has increased by an annual average of nearly 20 percent.

4. At present KESC has installed generating capacity of 390 MW and is adding 125 MW at the Korangi Power Plant (for which the Asian Development Bank is expected to provide financing). Starting around April this year the Karachi nuclear power plant (KANUPP), operated by the Atomic Energy Commission of Pakistan, is scheduled to start feeding its output into KESC's power system, gradually increasing its output to 125 MW (paragraph 3.02).

5. In the past the Bank has assisted the expansion of KESC's generating capacity, including some transmission and distribution, with four loans totalling US $51.7 million/1 of which the first has already been fully repaid and two others have been fully disbursed. The latest loan is expected to be fully disbursed by the middle of this year. The Bank's experience with the implementation of these projects has been satisfactory.

The Project

6. The proposed project consists primarily of additions and improvements to the transmission and distribution facilities of KESC (paragraph 4.01). It also includes the training of technical staff and engineering studies not only for transmission and distribution works included in the proposed project, but also for the further extension of the Korangi Power Station (which the Asian Development Bank will probably finance).

7. The total cost is estimated at just under US $24 million, of which US $10.5 million would be in foreign exchange (paragraphs 4.02 and 4.03). As the components of the project are links in a complex system which has developed over a long period, it is not feasible to calculate a meaningful internal financial rate of return for the project itself. However, for a two-year period (1972-1973) of development of the system as a whole, including the project, the rate has been calculated at about 24 percent, within a range between 17 and 26 percent (paragraph 5.06).

8. At present KESC has at its disposal sufficient installed generating capacity to meet the estimated demand up to 1974. However, the capacity of its transmission and distribution lines is lagging behind generation and additions are needed to provide a margin for reliability and to meet expected increases in demand. The project is required to correct this imbalance and would meet KESC's need for transmission and distribution facilities until the end of 1973.

9. With the exception of professional engineering services, procurement of goods and services to be financed under the proposed loan would be on the basis of international competitive bidding. The project does not include any equipment of a type manufactured in Pakistan (paragraph 4.08).

10. In order to avoid delays in the implementation of its expansion program, KESC consulted with the Bank's staff late last year regarding the possibility of financing from the proposed loan for engineering expenditures incurred before

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1/ Loan No. 120-PAK in1955; Loan No. 191-PAK in 1958; Loan No. 234-PAK in 1959 and Loan No. 488-PAK in 1967.

the loan itself is finalized. In accordance with our usual policy on these matters we agreed, subject of course to the Executive Directors' approval of the loan itself. Such expenditures began only at the end of last year and are not expected to amount to more than US $750,000 by the time the loan is presented to the Executive Directors.

11. KESC has a successful financial record and its present position is satisfactory. With the increase in scale of its operations, however, problems in management and organization have become more and more apparent; there is also a need to improve financial and cost control. The Appraisal Report includes recommendations directed at preserving the corporation's favorable financial position and encouraging the continuation and extension of efforts, already initiated by KESC, to improve its management and organization (paragraph 8.01). I am in agreement with these proposals.

12. The loan would be made to KESC and guaranteed by the Government of Pakistan. The Trust Deed under which the previous four loans are secured would be amended to provide equal security for the proposed loan. I do not expect the Government to charge a fee for its guarantee, nor do I consider the fee necessary in this case. Nevertheless, the matter will be discussed during negotiations.

Recommendations

13. I agree with the conclusion of the Appraisal Report (paragraph 8.03) that the project is suitable for a loan of US $10.5 million for a period of 20 years including a three year grace period, subject to the conditions proposed in the report. I recommend that we invite representatives of KESC and the Government of Pakistan to negotiate loan and guarantee agreements.

Gregory B. Votaw
Deputy Director
South Asia Department

Attachment

Population: 120 m
GNP Per Cap: 90

IVa. PAKISTAN - EAST - 5 YEAR OPERATIONS PROGRAM
(By Fiscal Year - Amounts in $ millions)

			1971	1972	1973	1974	1975	1976
5-PAK-AI-09	Irrigation - Dacca Southwest	IDA	30.0					
5-PAK-AI-11	Irrigation - Karnaphuli	IDA		14.0				
5-PAK-AI-15	Irrigation - Muhuri	IDA			7.0			
5-PAK-AI-17	Irrigation - Belkuchi	IDA			5.0			
5-PAK-AI-18	Irrigation - Chandpur North	IDA			10.0			
5-PAK-AI-19	Irrigation - Little Feni	IDA				10.0		
5-PAK-AI-20	Irrigation - Barisal I	IDA				20.0		
5-PAK-AI-24	Irrigation - Pabna	IDA					18.0	
5-PAK-AI-23	Irrigation - Comilla	IDA					15.0	
5-PAK-AN-02	Food Grain Storage II	IDA	10.5					
5-PAK-AI-12	Tubewells EPWAPDA II	IDA			8.0			
5-PAK-AI-22	Tubewells EPWAPDA III	IDA				25.0		
5-PAK-AN-03	EP Tea Prod. & Processing	IDA	5.0					
5-PAK-AA-03	EPWAPDA Consultants II	IDA	2.5					
5-PAK-AA-04	EPWAPDA Consultants III	IDA			2.0			
5-PAK-AA-05	EPWAPDA Consultants IV	IDA					2.0	
5-PAK-AD-01	EP Rural Infrastructure	IDA	10.0					
5-PAK-AA-06	Seed Multip. & Dist.	IDA	5.0					
5-PAK-AI-26	EPWAPDA I Tubewells	IDA	9.0					
5-PAK-EE-05	Education Unidentified	IDA		7.0				
5-PAK-TH-07	EP Highways II	IDA			12.5			
5-PAK-TH-08	EP Highways III	IDA			13.5			
5-PAK-TR-10	EP Railways	IDA		8.0				

Totals

	1964-68	1969-73	1974-76
IBRD			
IDA		184.2	177.0
Totals	95.3	184.2	177.0
No.			16

	1971	1972	1973	1974	1975	1976
IBRD						
IDA	72.0	29.0	58.0	55.0	35.0	
Total	72.0	29.0	58.0	55.0	35.0	
No.	7	3	7	3	3	

P & B 2/19/71

IVa. PAKISTAN - WEST - 5 YEAR OPERATIONS PROGRAM
(By Fiscal Year - Amounts in $ millions)

			1971	1972	1973	1974	1975	1976
5-PAK-AI-10	Scarp V	IDA		7.0				
5-PAK-AI-16	Scarp VI	IDA			12.0			
5-PAK-AI-21	Tubewells - Dipalpur	IDA				15.0		
5-PAK-EE-06	WP Education Unidentified I	IDA			8.0			
5-PAK-EE-07	WP Education Unidentified II	IDA					5.0	
5-PAK-IC-02	WP Fertilizer Plant II	IBRD		30.0				
5-PAK-PM-01	WAPDA Power Distribution	IDA	23.0					
5-PAK-PD-01	WP Power V - KESC	IBRD	10.5					
5-PAK-TH-06	WP Highways III	IDA			20.0			
5-PAK-TH-10	WP Highways V	IDA				20.0		
5-PAK-TP-06	Port Constr. III - Karachi	IDA		15.0				
5-PAK-TP-07	Port Constr. IV - Karachi	IDA				20.0		
5-PAK-TL-05	Sui Northern Gas IV	IBRD			5.0			
5-PAK-TL-06	Sui Northern Gas V	IBRD				5.0		
5-PAK-WW-04	Water Supply II - Lahore	IDA	5.0					

	Total 1964-68	1969-73	1974-76
IBRD		179.2	40.0
IDA		99.0	122.0
Total	84.3	278.2	162.0
No.	6	18	12

IBRD	10.5	30.0	5.0	5.0		
IDA	28.0	22.0	40.0	55.0	5.0	
Total	38.5	52.0	45.0	60.0	5.0	
No.	3	3	4	4	1	

P & B 2/19/71

IVa. PAKISTAN - EAST & WEST - 5 YEAR LENDING PROGRAM
(By Fiscal Year - Amounts in $ millions)

			1971	1972	1973	1974	1975	1976
5-PAK-AC-04	Agric. Credit ADB IV	IDA		15.0				
5-PAK-AC-05	Agric. Credit ADB V	IDA			30.0			
5-PAK-AC-06	Agric. Credit ADB VI	IDA					30.0	
5-PAK-GG-01	Reconstruction	IDA	25.0					
5-PAK-IC-03	Industry - Petro Chemicals	IDA		30.0				
5-PAK-DD-10	DFC - PICIC IX	IBRD	30.0					
5-PAK-DD-12	DFC - PICIC X	IBRD			40.0			
5-PAK-DD-14	DFC - PICIC XI	IBRD					40.0	
5-PAK-DD-11	DFC - IDBP II	IDA		10.0				
5-PAK-DD-13	DFC - IDBP III	IDA					20.0	

	Total 1964-68	1969-73	1972-76		1971	1972	1973	1974	1975
IBRD		110.0	80.0	IBRD	30.0		40.0		40.0
IDA		191.0	135.0	IDA	25.0	55.0	30.0		50.0
Total	314.7	301.0	215.0	Total	55.0	55.0	70.0		90.0
	13	12	8		2	3	2		3

	TOTAL 1964-68	1969-73	1972-76		1971	1972	1973	1974	1975
IBRD	162.0	289.2	120.0	IBRD	40.0	30.0	45.0	5.0	40.0
IDA	332.3	484.2	434.0	IDA	125.0	106.0	128.0	110.0	90.0
Total	494.3	773.4	554.0	Total	165.0	136.0	173.0	115.0	130.0
	25	53	36		12	9	13	7	7

	1971	1972	1973	1974	1975
* Note: the IDA lending program is to be adjusted to --	70.0	90.0	90.0	90.0	90.0
the IBRD lending program is to be adjusted to --	30.0	-----------120.0---------			

P & B 2/19/71

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

March 2, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Ethiopia - Coffee Processing Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated March 2, 1971 from the Eastern Africa Department, entitled "Ethiopia - Coffee Processing Project" (LC/O/71-26).

2. Comments, if any, should be sent to reach Mr. Roeloffs (ext. 3553) by 1:00 p.m. on Thursday, March 4.

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

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

Copies for Information:

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

CONFIDENTIAL

LC/0/71-26

March 2, 1971

LOAN COMMITTEE

Memorandum from the Eastern Africa Department

ETHIOPIA - Coffee Processing Project

Introduction

1. The proposed project is designed to increase Ethiopia's export earnings from agriculture by improving coffee processing methods. By full development in 1976-77, it would increase Ethiopia's foreign exchange earnings by about US$2.4 million per year through switching some 11,000 MT/annum of Ethiopian coffee, now processed by traditional sun drying methods, to mechanical processing into higher priced washed coffee. It would provide reasonable investment earnings for private and cooperative washing-station owners and increases in cash incomes of approximately 10-15% for some 33,000 farm families, compared to the incomes they would have earned without the project. The project would fit into the Government's agricultural strategy of concentrating resources on regions or crops of high potential of encouraging the growth of cooperatives and of improving the feeder road network.

2. This project, which was prepared by the Ethiopian National Coffee Board (NCB) with the assistance of staff was appraised in September/October 1970. The project is described in the attached draft yellow cover appraisal report dated January 27, 1971. The Office of the Director, Projects, has agreed that this draft be circulated to Loan Committee in place of the normal green cover report, with the following comments:

(a) The grey cover report would specify, in the Project Cost table, the amount of import duties included in project costs. These are estimated at E$270,000 (US$108,000). The Bank loan would not be disbursed against them.

(b) The grey cover report would emphasize, in paragraph 6.04, that the financial and economic analyses of the proposed investments in the project depend largely on the differential which might be expected between Ethiopian washed and unwashed coffee prices and are only marginally affected by their absolute levels.

The report recommends that, subject to the conditions set forth in paragraphs 8.01 - 8.03, the proposed project is suitable as a basis for a Bank loan of US$6.5 million equivalent for 18 years, including a grace period of 5½ years. I support this recommendation except that on country grounds, I propose that the term of the loan be 25 years instead of 18 years (see paragraph 18 below).

3. To date we have made eleven loans to Ethiopia totalling $97.8 million and five credits totalling $35.0 million. Negotiations have been substantially completed for a proposed credit of $9.5 million for a Second Education Project, and negotiations are under way for a proposed credit of $4.3 million for a Dairy Development Pooject. A proposed Bank loan of $9.3 million for a Water and Sewerage Project in Addis Ababa is under appraisal. The 1972-76 lending program as approved by Mr. McNamara in December, 1970, is attached.

4. If approved, the proposed project would be the third agricultural operation and first Bank lending directly for agriculture in Ethiopia following the IDA credits for Wolamo and Humera development projects in FY'70. Prior to those operations some small amounts for agriculture were provided under the 1950 and 1961 loans to the former Development Bank of Ethiopia.

The Project

5. The proposed project involves the construction of about 100 new coffee washing stations (each of 100 tons seasonal capacity), improvements to about 100 existing stations, construction of about 400 km of dry weather access roads, and technical services for the preparation of follow-up projects, research studies of possibilities of improved grading and forest coffee management, and a survey of the Ethiopian coffee economy. The project would be located in selected areas of the provinces of Kaffa and Sidamo, where the coffee has been identified as particularly suitable for the washing process and where water supply is ample during the processing season. Total cost is estimated at US$10.1 million. The proposed Bank loan of US$6.5 million would finance approximately 65% of the total cost; the Government and the Agricultural and Industrial Development Bank (AIDB) would provide US$3.1 million and the coffee industry would contribute the remaining US$0.5 million.

6. The foreign exchange component of the project is estimated at US$4.5 million or 44% of the total. It is proposed that the loan covers this amount plus US$2 million of local expenditure. The proposed financing of local expenditure is considered to be justified since, even given a reasonable increase in Ethiopia's efforts to mobilize domestic resources, at least half of its public investment program needs to be financed externally. Since parts of the program are not suitable for foreign assistance, those projects that can be assisted externally must include a percentage of financing high enough so as to maintain the 50% average for the total investment program.

7. The Borrower would be the Government, which would bear the foreign exchange risk. Some US$2.9 million of the proceeds of the Bank loan would be onlent to AIDB at an interest rate of 7-$\frac{1}{4}$% p.a., for further onlending at 9-$\frac{1}{4}$% to private and cooperative washing-station owners. The remainder of the proceeds of the Bank loan would be passed on as grants to a Cooperative Union, to be established under the project, for road construction, technical services and project preparation, and to the Institute of Agricultural Research (IAR), for coffee research.

8. The only appropriate credit channel available is the state-owned AIDB, which was created in November 1970 by reorganization of two predecessor institutions. It is too early to appraise AIDB's financial position and prospects, but the Bank has been closely involved in drawing up guidelines for the reorganization and the creation of AIDB, and the Government has declared its intention that AIDB should be run in accordance with sound development banking principles. AIDB has inherited an adequate accounting division and some staff experienced in assessing the financial viability of sub-borrowers. We hope that AIDB can be appraised within the next few months and found suitable for the loan included in the FY'72 lending program. It is in my view highly desirable that AIDB effectively take up its function as principal credit channel as soon as possible and thereby gain the experience that it at present lacks. It is proposed in the appraisal report that all Bank loan funds used for credit purposes under the coffee processing project be channeled through AIDB but that, to minimize the uncertainties of operating with an institution that has not yet been appraised and found satisfactory, the project funds be operated by AIDB through a separate trust fund. However, a question has recently been raised concerning the legality of the proposed trust fund under Ethiopian law. I support the trust fund recommendation provided that it is possible under Ethiopian law, but if it causes legal difficulties, I would consider that the conditions proposed in the appraisal report concerning AIDB policies, procedures, and staff to supervise the credit operation, would provide adequate safeguards without a trust fund.

9. This arrangement differs from the proposal contained in our Loan Committee Memorandum on the proposed Addis Ababa Dairy Development Project (LC/O/70-120 of November 24, 1970) where we proposed that credit operations be handled as one of the functions of the proposed Addis Ababa Dairy Development Corporation. This reflects, in part, the fact that the Dairy Project Appraisal Report was completed before AIDB had been created. During negotiations for the Dairy project which have just been substantially completed, the Government requested that we consider channeling the credit through AIDB. After careful consideration and taking account of the differences between the Dairy and Coffee Processing projects (such as the ease in having the Dairy Corporation deduct loan repayments from the price of milk purchased), we proposed to the Ethiopians that AIDB should carry out some of the credit functions under the Dairy project, although these functions would not be as broad as under the proposed Coffee Processing project.

10. The report proposes that a Cooperative Union be set up with Government participation and control in its initial development period to (i) construct and initially operate some 70 new washing-stations to be constructed in Sidamo Province, (ii) stimulate the development of primary societies of farmers eventually to take over these washing-stations, (iii) provide technical services for the other washing-station owners - private enterprises and cooperatives - financed under the project/1, (iv) carry out the road construction program and (v) prepare follow-up projects. All sub-loans made under the project by the AIDB would be appraised technically by staff attached to the Cooperative Union who would also supervise construction of washing-stations and their initial operation.

11. In its project preparation report, the Government had suggested that cooperative societies of coffee farmers would be formed to own and operate the 70 coffee washing-stations which are proposed for construction in the Sidamo Province, and, therefore, that the project organization would only be required to give them technical assistance in site selection, washing-station design, installation of machinery and initial operation. However, cooperative development is still in its infancy in Ethiopia, and there are only 3 primary cooperative societies in Sidamo Province at this time. The draft appraisal report therefore proposes that a strongly managed Cooperative Union be established to own and operate these 70 stations until such time as primary societies could be formed and developed to the point where they could take over ownership and management.

/1 These entities would own the remaining 30 new washing-stations to be constructed under the project, as well as the 100 existing stations to be improved.

12. The proposal to establish a Cooperative Union with functions as described in the preceding paragraphs is known to the Government and has the support of various key officials, but the Government has not yet officially indicated whether it is acceptable. There are other forms of organization than the one suggested (for instance, a state-owned Chartered Agency or Corporation) which might be equally acceptable, but which would probably take longer time to establish. Agricultural Projects Department proposes to take a flexible attitude on this issue during negotiations and to accept any organizational form which the Government might suggest which would be equally capable of carrying out the project. I support this proposal.

13. The project would contribute some 11,000 MT per annum to Ethiopia's washed coffee production, which is likely to grow from its present level of about 10,000 MT to some 27,000 MT (inclusive of the output of the proposed Bank project) by 1976-77. This increase in washed coffee production would be counter-balanced by a similar reduction in the production of unwashed coffee and thus would have no effect on Ethiopia's obligations under the International Coffee Agreement. However, it is also estimated that the road network to be constructed in the project area might give rise to an additional production of some 1,000 MT of coffee per annum, over and above present production in the area. This is only about 1% of the current Ethiopian share of exports to quota markets (some 83,000 tons per annum) and would be unlikely to have any measureable effect on Ethiopia's ability to comply with its obligations under the International Coffee Agreement. The projected increase in the proportion of washed coffee in Ethiopian output would be unlikely to affect significantly the prevailing relationship between world market prices for washed and unwashed coffees, since the resulting increase in world output of washed coffee would be marginal, less than 1%, and demand for washed coffee is increasing.

14. A staff member of the Coffee Diversification Fund of the International Coffee Organization (ICO) participated in the appraisal to investigate the project's suitability for possible joint financing. The ICO later decided that it did not wish to participate in the joint financing of this project, although it may finance separately the survey of Ethiopia's coffee economy. Their decision was based on wide policy considerations, the project itself being recommended for support by the ICO member of the appraisal mission. Representatives of ICO informed us, during informal discussions, that they concur with out conclusions regarding the impact of this project on the world coffee market, and have recently requested them to let us have ICO's official views. We expect to receive their reply shortly.

15. A paper analyzing world coffee markets and projecting coffee prices has recently been drafted by the Economics Department. It is expected that this paper will be circulated prior to presentation of the project to the Executive Directors.

16. The financial and economic results of the project do not depend significantly on the absolute level of coffee prices, but are largely dependent upon, and are quite sensitive to, the differential in prices between Ethiopian washed and unwashed coffees. A simplified form of risk analysis has therefore been carried out, based on probabilities assigned to various differentials between washed and unwashed coffee prices. This analysis indicates that the mean economic rates of return of the proposed investments in washing-stations would be between 17% to 21%, depending on the degree of road construction needed. The mean financial rate of return to a typical washing-station owner would be about 17%. Although there appears to be about a 10% risk that price differentials may not be sufficient to provide satisfactory economic and financial rates of return, I consider that this risk is more than offset by the relatively high levels of the mean economic and financial rates of return.

17. In order to avoid delays in construction of the roads under the project, planning and survey staff would have to be recruited in March 1971 and invitations to bid on the necessary road construction equipment would have to be issued by the end of April 1971. With negotiations scheduled for March and Board presentation for May, up to US$100,000 might be required on the project prior to loan signature and bid invitations would need to be issued between negotiations and Board presentation for about US$600,000 worth or equipment. With the concurrence of the Chairman of the Loan Committee, I have informed the Government that, subject to the approval of the Executive Directors, we would (i) be prepared to include in the proposed project provision for retroactive financing of up to US$100,000 for expenditures on planning and survey staff prior to loan signature, and (ii) agree that invitations to bid for the road construction equipment of approximately US$600,000 be issued before the loan is signed.

Economic Situation

18. An Economic Report on Ethiopia (AE-9) was distributed to the Executive Directors on October 22, 1970 (Secretary's Memorandum R10-199). The main conclusions were summarized in my memorandum to the Loan Committee entitled "Ethiopia - Addis Ababa Dairy Development Project" dated November 24, 1970. Based on the recommendations of the Economic Report, the Ethiopian Country Program Paper envisaged a softening in the blend of Bank/IDA lending to Ethiopia (see attachment 1). It concluded that, while Ethiopia has some margin for some further borrowing on conventional terms, such borrowing should be kept as low as possible since it is clear that the economy will need foreign assistance for many years and the outlook for export earnings is uncertain and subject to wide fluctuation. With these considerations in mind, I propose that the term of the loan be extended from 18 to 25 years.

Recommendation

19. I recommend that the Government of Ethiopia be invited to negotiate a Bank loan of US$6.5 million for the proposed coffee processing project on the terms and conditions set forth in paragraphs 8.01 - 8.03 of the appraisal report, subject to the change in term proposed in paragraph 18 and the possible changes referred to in paragraphs 8 and 11.

Attachments (2)

Eastern Africa Department
March 2, 1971

Population: 25 million
Per Capita Income: $63

Attachment 1

ETHIOPIA: ACTUAL AND PROPOSED LENDING THROUGH 1976

		Through 1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1964-68	1969-73	Total 1972-1976
Wolamo Agriculture Development	IDA							3.5									
Wolamo Agriculture Development II	IDA												5.0				
Awassa	IDA										5.0						
Humera Agriculture I	IDA							3.1									
Humera Agriculture II	IDA											5.0					
Grain Storage	IDA												5.0				
Land Settlement	IDA										6.0						
Minimum Package I & II	IDA										5.0		5.0				
Awash Irrigation I	IDA									10.0							
Awash Irrigation II	IBRD													15.0			
Livestock I - Dairy	IDA								4.3								
Livestock II	IDA									8.0							
Livestock III	IDA											8.0					
Livestock IV	IDA													10.0			
Coffee Processing I	IBRD								6.0								
Coffee Processing II	IBRD											10.0					
Coffee Processing III	IBRD												8.0				
Agriculture unidentified	IDA												5.0				
Telecommunications I and II	IBRD	4.4															
Telecommunications III	IBRD			4.8													
Telecommunications IV	IBRD						4.5										
Telecommunications V	IBRD										12.0						
Development Finance Company I & II	IBRD	4.0															
Development Finance Company III	IBRD									4.0							
Development Finance Company IV	IDA											6.0					
Development Finance Company V	IDA													10.0			
Education I	IDA			7.2													
Education II	IDA								8.0 1/								
Education III	IDA										20.0						
Education IV	IDA													20.0			
Rural Education & Training	IDA									5.0							
Power I	IBRD	23.5															
Power II	IBRD						23.1										
Power III	IBRD											30.0					
Roads I and II	IBRD	20.0															
Roads III	IDA	13.5															
Roads IV	IBRD					13.5											
"	IDA					7.7											
Roads V	IBRD									10.0							
Roads VI	IDA											10.0					
Roads VII	IDA													15.0			
Aviation I	IDA										5.0						
Port Development	IBRD										5.0						
Tourism	IDA												5.0				
Water Supply - Addis I	IBRD								7.0 1/								
Water Supply - Addis II	IBRD												10.0				
Gross Program	IBRD	51.9		4.8		13.5	27.6		13.0	14.0	17.0	40.0	18.0	15.0	41.8	71.6	104.0
	IDA	13.5		7.2		7.7		6.6	12.3	23.0	41.0	29.0	25.0	55.0	14.9	82.9	173.0
	Total	65.4		12.0		21.0	27.6	6.6	25.3	37.0	58.0	69.0	43.0	70.0	56.7	154.5	277.0
	No.	8		2		1	2	2	4	5	7	5	7	5	4	20	29
Net Program	IBRD	51.9		4.8		13.5	27.6		6.5	14.0	14.0	25.0	11.0	12.0	41.8	62.1	76.0
	IDA	13.5		7.2		7.7		6.6	12.5	15.0	25.0	22.0	22.0	30.0	14.9	59.1	114.0
	Total	65.4		12.0		21.0	27.6	6.6	19.0	29.0	39.0	47.0	33.0	42.0	56.7	121.2	190.0
	No.	8		2		1	2	2	3	3	5	4	4	4	4	15	20
IBRD Loans Outstanding																	
- including undisbursed		45.6	43.0	45.9	43.9	55.1	80.5	77.6	81.4	93.1	104.5	126.7	134.6	142.4			
- excluding undisbursed		20.3	21.8	28.8	33.8	35.7	39.1	48.0	51.7	55.6	58.6	62.1	67.4	73.1			
IDA Credits Outstanding																	
- including undisbursed		13.5	13.5	20.7	20.7	28.4	28.4	35.0	47.5	62.5	87.5	109.4	131.3	161.1			
- excluding undisbursed		2.2	3.8	7.4	10.5	13.7	16.4	25.8	32.9	41.3	50.3	60.5	72.7	86.0			

1/ Since the December 1970 review with Mr. McNamara, the proposed Second Education Credit has been increased to $9.5 million, and the proposed Addis Ababa Water Supply Loan to $9.3 million.

Last Economic Mission

January-February 1970

Attachment 2

ETHIOPIA

INDICATORS OF DEVELOPMENT

ECONOMIC AND STRUCTURAL INDICATORS	Unit	1951-60	1961-65	1966-70 /1	1971-75 /2
1. Gross Domestic Product (in 1961 prices)	% change		4.4	4.5	5.5
2. Manufacturing Output	% change		16.4	16.5	12.0
3. Agricultural Output	% change		2.0	2.2	2.8
4. Imports of Goods and NFS	% change		15.0	1.0	6.4
5. Exports of Goods and NFS	% change		12.6	3.2	6.0
6. Domestic Price Level	% change		3.7	1.5	
		1961	1966	1970 /3	1975 /3
7. Gross National Savings	% GDP	10.9	9.7	12.0	13.8
8. Resource Gap	% GDP	0.6	2.0	1.5	1.7
9. Net Factor Payments Abroad	% GDP	0.2	0.1	0.5	0.5
10. Gross Domestic Investment	% GDP	11.7	11.8	14.0	16.0
11. Debt Service	% Export	3.0	6.1	9.5	10.0
12. Central Government Current Revenue	% GDP	8.0	9.6	9.5	12.0
13. Central Government Current Surplus	% GDP	0.8	1.3	0.8	1.5
14. Public Expenditure on Social Services	% GDP	1.5	2.1	2.5	3.5
15. Military Expenditure	% GDP	1.8	2.1	2.2	2.0
16. Manufacturing Output	% GDP		16.5	12.0	12.0
17. Energy Consumption	million tons				
18. Fertilizer Consumption	.000 tons				
SOCIAL INDICATORS					
19. Population Growth Rate	%		1.8	2.1	2.3
20. Urban Population Growth Rate	%				
21. Birth Rate	per 1,000				
22. Family Planning	Acceptors '000				
23. Income of: Highest quintile	% Total income				
Lowest quintile	% Total income				
24. School Enrolment: Primary and Secondary	% school-age population			8.0	
25. Literacy Rate	% adult population				
26. Unemployment Rate	% labor force				
27. Population per hospital bed	Number			3,400	

/1 1966-69

/2 1970-74

/3 Figures for 1970 and 1975 are the estimates of the economic mission; these may not agree with figures in Attachment 3 which are derived using some long-term parameters.

Eastern Africa Department
December 9, 1970

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LM/M/71-14

March 1, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Attached for information are the Minutes of a Special Loan Meeting to consider "Pakistan - Rural Infrastructure Project, East Pakistan" held at 2:30 p.m. on Friday, February 12, 1971 in Conference Room A.

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

Copies for Information:

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

LM/M/71-14

March 1, 1971

Minutes of Special Loan Meeting to consider "Pakistan - Rural Infrastructure Project, East Pakistan" held at 2:30 p.m. on Friday, February 12, 1971 in Conference Room A.

1. Present: Messrs. Knapp (Chairman), Cope, Cargill, Chadenet, Gabriel, Nurick, Sella, Votaw, Picciotto, Gordon, Wiehen, Goldberg, Hoerr, Segal, J. Thomas (consultant) and Pearce (Secretary).

2. Issues: The meeting had been called to consider Mr. Cargill's memorandum of February 8, 1971, to the Chairman and a pre-appraisal report dated January 18, 1971 prepared by the Special Projects Department, which recommended an $11.4 million credit to help finance a $21 million project to improve rural infrastructure in 50 selected thanas (administrative units) in East Pakistan. There were three main issues for discussion: (a) local expenditure financing, (b) the project area, and (c) short-term credit financing.

3. Discussion: The meeting noted that:

(a) Local Expenditure Financing

(i) Owing to the project's small foreign exchange component, about 85 per cent of the proposed credit would finance local expenditures.

(ii) There was a strong general case for Bank/IDA financing of local expenditures in Pakistan and, assuming the project's economic priority were established during appraisal, a high proportion of local expenditure financing would be justified.

(iii) If the project and IDA's contribution to it were successful, Consortium members would probably help finance subsequent rural infrastructure projects, including local expenditures.

(b) Project area

(i) The 50 project thanas, selected from about 400 by the Government on the basis of their relatively good administration and agricultural potential, were located in about 10 clusters throughout the province, although 75 per cent of them were concentrated in two districts (Comilla-Chittagong) where integrated rural development had already begun.

(ii) Since physical works would be undertaken at many different sites, direct project supervision by IDA would be very difficult. Consequently, further geographical concentration was desirable to ensure satisfactory project execution and to facilitate project supervision. It was particularly important that this project be successful because of its probable "demonstration effect."

(iii) On the other hand, the concentration of the project thanas mainly in Comilla-Chittagong, while certainly facilitating the project's success, would delay the introduction of integrated rural development in other districts. Thus, while further concentration was desirable, it should preferably be in districts other than Comilla-Chittagong.

(c) Short-term Credit Financing

(i) About $5.2 million of the proposed credit would provide agricultural credit for the project thanas, including $4.2 million in short-term loans to enable small farmers to purchase improved seed varieties, fertilizers, etc.

(ii) Agricultural credit was crucial to integrated rural development. Although the number of institutions and cooperatives involved would make the administration of the credit scheme very difficult, IDA funds could properly be used for this purpose provided they were incremental to the funds which would otherwise have been available in the project thanas. The appraisal mission would have to investigate this aspect with particular care.

(d) General

In the peculiar conditions of East Pakistan, rural works were liable to flood damage and would therefore probably require high annual maintenance expenditures. The appraisal mission would have to consider in particular which of the following would be the most economic solution for construction works: high investment but low recurrent/maintenance costs or low investment but high recurrent/maintenance costs.

4. <u>Decision</u>: The Chairman authorized appraisal of the project substantially in accordance with the recommendations contained in the pre-appraisal report, as modified by the discussion recorded above.

David Pearce
Secretary

Cleared by: Messrs. Knapp
Nurick
Chadenet
Votaw/Wiehen/Segal
Picciotto

cc: Loan Committee
Participants

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

February 26, 1971

MEMORANDUM TO THE LOAN COMMITTEE

China - Taipower

1. The Committee is requested to consider, without meeting, the attached memorandum dated February 26, 1971 from the East Asia and Pacific Department, entitled "China - Proposed $55.0 Million Loan to the Taiwan Power Company" (LC/O/71-23).

2. Comments, if any, should be sent to reach Mr. Kalim (ext. 2426) by 1:00 p.m. on Wednesday, March 3.

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

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

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

CONFIDENTIAL

LC/0/71-23

February 26, 1971

LOAN COMMITTEE

Memorandum from East Asia and Pacific Department

CHINA: Proposed $55.0 Million Loan to the Taiwan Power Company

1. Attached is an appraisal report (PU-63, dated February 22, 1971) recommending a Bank loan of $55.0 million to the Taiwan Power Company (Taipower) for the financing of the foreign exchange cost, including interest during construction, of a project which forms part of its 1971-76 expansion program.

2. The economy of Taiwan has developed impressively over the past decade. GNP rose at an annual average rate of about 10% during the sixties and per capita GNP more than doubled from about $160 in 1960 to $335 in 1969. This noteworthy economic progress has been stimulated largely by successful efforts to expand exports, especially of manufactured goods, and a rapid growth of investment. During 1960-70, industrial production grew by about 18% annually and approximately one-third of the increase of industrial output was sold abroad. The Republic of China does not face any serious economic problems and the prospects for continued rapid GNP and export growth remain promising. The debt service ratio, which was 4.5% in 1969, is projected to reach a level of 8% in 1976. The country's ability to service additional debt is not in doubt and it is considered suitable for Bank financing.

3. Gross domestic capital formation in Taiwan increased at an average yearly rate of over 20% during the 1965-70 period. However, public sector investment in some critical areas such as power, transport and education has been insufficient. The Government now recognizes that public expenditure on such facilities needs to be stepped up significantly in order to avoid infrastructure deficiencies from limiting the pace of the economy's continued growth. The Bank's current 5-year lending program (copy attached) aims at helping the Government's effort to increase the flow of resources to the public sector. The latest Country Program Paper on China (approved in September 1970) proposed that the emphasis of Bank lending should gradually be shifted away from fields such as telecommunications, railways and power and move increasingly towards agriculture, highways, sewerage and water supply projects. It was argued that it would be easier to obtain financing from other sources for projects in the former categories. The preparation of some of the projects which the Bank intended to assist in financing during the next year or so has proved to be difficult and time consuming; a recent review indicates that a number of these projects may slip. In view of the accelerated growth of electricity demand (cf. para. 4 below), the Government has requested

that we consider providing some more finance for power in FY 1972. This subject will be discussed further during negotiations for the proposed project.

4. Taiwan's industrial sector is experiencing a structural shift which is expected to become more pronounced in the next few years. Growth in food processing and textiles, the former mainstays of the manufacturing sector in the sixties, is likely to slow down while more complex forms of production like electronic equipment, electrical appliances, chemicals and light engineering goods are expected to show a more rapid increase. This pattern of growth, combined with increasing household use of electricity, will result in a substantial demand for power. Forecasts made in August 1970, indicate that the demand for power, which grew at an average of nearly 15% in the last years of the sixties, will continue to rise by about 12½% annually during the next few years. However, revised operating results for 1969-70, which became available only after the appraisal mission returned from Taiwan, showed an unprecedented increase in demand of about 20% for each of the two years.

5. Taipower has formulated and received Government approval of a six-year expansion program which envisages a 3,500 MW increase of capacity, including the installation of two nuclear units of 600 MW capacity each at Chinshan,by the end of 1976. This represents an increment of 130% to the present installed capacity of 2,720 MW. Taipower's 1971-76 expansion program aims at meeting the rising demand for electricity and providing a certain amount of reserve capacity for the system. Further, Taipower believes that another 1,000 MW capacity may have to be installed during this period on account of the recent spurt of load growth. Taipower may solicit further Bank financing for this item during our fiscal year 1972 (cf. para. 3 above).

6. The total capital expenditure on the 1971-76 expansion program is estimated to be about $1,230 million equivalent. Internal cash generation, sales of equity and consumers' contribution will meet about $500 million (41%) of this. The remaining $730 million needed will have to be met through borrowings. Arrangements for obtaining most of the funds have already been made. However, some $110 million (about 9% of the 1970-76 expenditures on construction) remain to be secured, possibly through issuing bonds. The manner in which the shortfall is to be filled will be discussed during negotiations.

7. The Bank has already made two loans to assist in the implementation of the 1971-76 expansion program. A $50 million loan (574 CHA) was made in December 1968 to help finance the construction of a hydroelectric station with a capacity of 234 MW on the Tachia River in Central Taiwan and its associated extra high-voltage transmission facilities, the first in Taiwan. A second loan was signed in May 1970 for $44.5 million and involved (i) the installation of a 375 MW thermal unit at Talin in the south of Taiwan; (ii) an additional 180 MW of generating capacity at the Lower Tachien hydroelectric station; and (iii) the provision of additional EHV transmission facilities. At the end of January 1971, about $5.7 million had been disbursed drom the proceeds of Loan 574 CHA and

$83,000 from the proceeds of Loan 671 CHA. Progress on both project is satisfactory.

8. The proposed project consists of (i) the installation of a 500 MW thermal unit at Talin: (ii) sub-stations for connection of the Chinshan nuclear plant to the transmission system; and (iii) control equipment for load dispatch. The Bank loan which would cover only foreign exchange expenditures would meet about 64% of a total estimated project cost of $73.2 million. Taipower, with the Bank's agreement, called for bids for the500 MW turbo generator earlier this year. Bid opening, originally scheduled for mid-February, has been postponed to early April at the request of one of the potential suppliers. There is some uncertainty about the cost of the turbo generator since this is probably the first time a machine of this size, which is the largest that the Bank will have financed to date, has been put to international competitive bidding. There are few manufacturers of this large-sized equipment. Although the estimates, which were prepared with help of consultants approved by the Bank, are as realistic as possible given the amount of information presently available, there is nevertheless a possibility that the price of this item may be higher than the amount currently budgeted for it. Provided that the economic justification remains essentially unaffected, I recommend and the Public Utilities Projects Department agrees that the loan amount be adjusted upwards, before the project is submitted for Board consideration, to take account of a rise in the price of equipment if it materializes. On the other hand, in the unlikely event that the successful bids for this item should be substantially lower than now estimated, the amount of the proposed loan would be correspondingly reduced.

9. Taipower's system is operated efficiently and the company is well organized. It is capable of carrying out the expansion program with the help of consulting firms. Taipower's financial management is being reviewed by consultants financed from the proceeds of the Bank's loan 574 CHA. Consultants have also been provided under loan 671 CHA to advise on systems planning and other technical matters.

10. Taipower's financial position will remain satisfactory despite the substantial borrowings contemplated. The level of Taipower's future debt is less of a cause for concern than its structure. Because of the size of the program, the company has had to finance a part of its development program on less than appropriate terms. It is important for Taipower to restrict borrowings of less than fifteen years to a minimum. Thus, continued Bank assistance is essential to maintain an acceptably sound debt structure. A twenty-year term with a 5½ year grace period is recommended for the proposed loan and would correspond closely to the expected life of the principal assets being financed. The proposed Bank loan would include interest during construction to further assist the Company to improve its debt position. The project is well conceived and should yield a satisfactory rate of return of about 24%. The rate of return falls to about 20% after sunk costs of site preparation and transmission facilities are taken into consideration.

11. I agree with the conclusion and recommendation of the appraisal report and propose to invite Taipower and the Government to send representatives to Washington to negotiate a loan for a 20-year term including 5½ years grace. As envisaged in paragraph 8 above, the loan amount would be negotiated by cable in early April after the outcome of the bidding for the turbo generator is known.

Raymond J. Goodman
Director

Attachments

Population: 13.1 m
GNP Per Cap: $250

CHINA - FIVE-YEAR LENDING PROGRAM 1/

($ millions)

		Fiscal Years 1971	1972	1973	1974	1975	1976	Total 1964-68	Total 1969-73
Agric. Mechanization I	IBRD		20.0						
Agric. Mechanization II	IBRD				20.0				
Agric. Mechanization III	IBRD						20.0		
Telecommunications II	IBRD		16.5						
DFC - CDC V	IBRD		18.0						
DFC - CDC VI	IBRD				20.0				
DFC - CDC VII	IBRD						20.0		
Fishery Education	IBRD		2.5						
Power III	IBRD	55.0							
Thermal Power	IBRD				20.0				
Tourism	IBRD			10.0					
Highways I	IBRD			30.0					
Highways II	IBRD					30.0			
Port Development	IBRD			30.0					
Railways IV	IBRD	15.0							
Railways V	IBRD			20.0					
Railways VI	IBRD					20.0			
Sewerage - Taipei I	IBRD			20.0					
Sewerage - Taipei II	IBRD						20.0		
Water Supply - Taipei Regional	IBRD				30.0				
	IBRD	70.0	57.0	110.0	90.0	50.0	60.0	106.7	389.7
	No.	2	4	5	4	2	3	7	16

1/ The above lending program has been revised to reflect the changes agreed with the various Projects Departments since November 17, 1970 when Programming and Budgeting Department last issued Form IVa for China.

East Asia and Pacific Department
February 25, 1971

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

February 26, 1971

MEMORANDUM TO THE LOAN COMMITTEE

India - Fourth Telecommunications Project

1. The Committee is requested to consider, without meeting the attached memorandum dated February 26, 1971 from the South Asia Department, entitled "India - Fourth Telecommunications Credit Project" (LC/O/71-24).

2. Comments, if any, should be sent to reach Mr. Cunningham (ext. 2428) by 1:00 p.m. on Wednesday, March 3.

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

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

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

CONFIDENTIAL

LC/0/71-24

February 26, 1971

LOAN COMMITTEE

Memorandum from South Asia Department

INDIA - Fourth Telecommunications Credit Project

Background

1. Attached is an Appraisal Report (No. PU-64) dated February 23, 1971 recommending that the Association make a credit to India of US $78.0 million equivalent for this project. Also attached is a copy of the gross operating program, based on the timetables prepared for end February; some trimming of this program is under consideration to keep the two year (FY 71-72) lending program for India to about $600 million.

2. The proposed project would finance the foreign exchange requirements to complete the telecommunications expansion program being carried out under the Fourth Five-Year Plan (1969/70 - 73/74), and would be administered by the Posts and Telegraphs Department (P&T), a department of the Government of India (GOI).

3. This project would be the fourth of a series for telecommunications financed by the Bank Group. The most recent was a combined loan/credit (Loan No. 615-IN and Credit No. 153-IN each for US $27.5 million making a total of US $55 million), signed in June 1969 and designed to meet the major part of the foreign exchange requirements for telecommunications over the first three years of the expansion program. At the same time, the Canadian International Development Agency (CIDA) made a loan for US $32.5 million (later increased to US $35 million) to finance selected items for the whole five year program. Experience to date with Indian Telecommunications projects has been satisfactory. The appraisal mission which visited India in November/December 1970 recommends that a further credit to finance the balance of the foreign exchange requirements of the Fourth Five-Year Plan program should be submitted now to permit the timely ordering of equipment.

Bank/IDA Lending Program

4. For this fiscal year, India's allocation from IDA is US $245 million of which US $30.4 million has been approved for two credits (Agro-Aviation US $6 million and Andhra Pradesh Agricultural Credit US $24.4 million). An appraisal report has been prepared for a second Power Transmission Project (US $75 million), which is scheduled for presentation to

the Executive Directors on April 27. Appraisal reports are also being completed for two agricultural credit projects (Tamil Nadu US $27 million and Haryana US $27 million), Pochampad Irrigation Project (US $35 million), and Cochin Fertilizer (US $20 million), and hopefully all of these credits can be negotiated before the end of June. If so, presentation of one or two of these projects to the Executive Directors may have to be deferred to keep within the IDA allocation. In addition, appraisal work is proceeding on several other projects for negotiation early in FY 72.

5. The most recent economic report, "Economic Situation and Prospects of India" (SA-13, April 29, 1970), indicated that the economy was moving out of the recession, brought about primarily by the effect of two bad harvest years in 1965/66 and 1966/67. It also reported an encouraging improvement in the balance of payments. Despite these favorable developments, India still requires substantial aid on concessionary terms for economic development purposes. I do not expect these conclusions to be altered by the economic report for 1971, which is presently being prepared.

The Project

6. The proposed Fourth Telecommunications Credit would finance direct imports amounting to US $26 million (including items such as local exchange systems, coaxial cable, and two microwave systems) and indirect imports amounting to US $52 million representing the foreign exchange content of locally manufactured goods. The project also includes provision for consultant services (US $0.1 million) to Indian Telephone Industries (ITI) to help that organization improve its procurement and production procedures. The borrower would be GOI.

7. P&T's telecommunications expansion program for the Fourth Five-Year Plan is estimated at US $652 million. Approximately 40 percent of this cost is to be financed from internal cash generation with the remainder coming mainly from government loans, CIDA and IDA. The original Fourth Plan targets called for connection of 600,000 new subscribers by March 1974 to make a total of 1.35 million; expanding long distance networks by radio and cable; increasing trunk exchange capacity; and extending telex services. Some of these targets have had to be adjusted downward by up to 10 percent on account of supply difficulties, but generally speaking, performance has been satisfactory.

8. Although the third project was approved in June 1969, only about US $14 million has been disbursed so far, and all of this amount has been in respect of reimbursement for the foreign exchange content of locally manufactured equipment, for which US $35 million had been allocated under the project. US $20 million was allocated for direct imports, and procurement action for virtually the whole amount was initiated by early fall 1970. We expect that disbursements will have reached US $50 million by March 1972 and will be completed before the closing date (December 31, 1972). Experience with telecommunications projects has shown that the lead time for much of the equipment can extend to as much as two years. Assuming that the proposed new credit is approved in April, we expect that the new supplies would start arriving sometime between March and June 1972, that is to say, just when the supply of equipment under the third project would have been completed.

9. The benefits of the program will include the establishment of a system which is more evenly balanced between subscribers and line capacity and which will support the growing needs of industry, trade and government. Hitherto, as earlier appraisal reports have noted, the connection of new subscribers has outstripped the capacity of the system to handle calls with the result that serious delays and breakdowns occur.

10. The proposed credit follows the pattern of its predecessors, and I do not expect that the negotiations should create any difficulties. No special conditions of effectiveness are recommended and the covenants include, as before, a commitment to provide for a rate of return of 11 percent and a requirement that the financial reorganization presently in hand should be continued (para 6.01 of the appraisal report). At the time of appraisal, we asked for an assurance (later set out in Mr. Kirk's letter of December 24, 1970) that appropriate action would be taken to correct imbalances in the supply of crossbar switching equipment from the ITI factory, and we received a satisfactory response from P&T on January 25, 1971. We also asked that an effective organization for the management of stores should be established offering career prospects within the structure of the P&T organization. This was agreed in general terms between the appraisal mission and P&T. Both assurances will be confirmed during negotiations.

11. Procurement under the proposed credit would also follow established procedures. Equipment to be imported directly by P&T would be subject to formal international competitive bidding except for proprietary items amounting to about US $7 million. The foreign exchange content of purchases made by P&T from government factories would be reimbursed in accordance with the formula set out in para 3.20 of the appraisal report. In both the second and third projects, we agreed to the latter procedure because the output of government factories was found to be competitive on an international basis in terms of both price and quality. In addition, the purchasing procedures practiced by the government-owned factories ensured that raw materials are bought at the best price available on the international market. The appraisal mission found that these conditions still apply and therefore, I recommend that we continue to operate as before.

12. Finally, on the more general question of resource mobilization through savings generated by government-owned enterprises, I am satisfied with the progress made to date by the Telecommunications Branch. The requirement under the previous project to prepare commercial accounts has brought about a more realistic basis on which to judge performance, and the tariff covenant for a financial rate of return of at least 11 percent is expected to result in net internal cash generation equivalent to over 40 percent of planned capital expenditures during the five year period of the program.

Recommendation

13. Subject to the views of the Committee, I recommend that the borrower be invited to negotiate the proposed credit of US $78 million on the basis of the recommendations set out in para 6.01 of the appraisal report.

Gregory B. Votaw
Deputy Director
South Asia Department

Attachments

Population: 556 m
GNP Per Cap: $76

IVa. INDIA - 5 YEAR LENDING PROGRAM

		($ millions)							
				Fiscal Year				Total	Total
		1970	1971	1972	1973	1974	1975	1964-68	1969-73
Agric. Credit - Punjab	IDA	27.5							
Agric. Credit - Gujarat	IDA	35.0							
Agric. Credit - Haryana	IDA		27.0						
Agric. Credit - Tamil Nadu	IDA		27.0						
Agric. Credit - Andhra-Pradesh	IDA		24.4						
Agric. Credit - Mysore	IDA			25.0					
Agric. Credit - Maharashtra	IDA			25.0					
Agric. Credit - Unidentified	IDA			25.0					
Irrigation - Kadana	IDA	35.0							
Irrigation - Pochampad	IDA		35.0						
Irrigation - Tawa	IDA			60.0					
Irrigation - Jayakwadi	IDA			30.0					
Irrigation - Unidentified	IDA			55.0					
Agricultural Aviation	IDA		6.0						
Agric. Industry Unident.	IDA			10.0					
Agric. Unident. (7 projects)	IDA				150.0				
Agric. Unident. (7 projects)	IDA					165.0			
Agric. Unident. (7 projects)	IDA						165.0		
Telecommunications IV	IDA		78.0						
Telecommunications V	IDA				40.0				
Telecommunications VI	IDA					40.0			
Telecommunications VII	IDA						35.0		
DFC - ICICI VIII	IBRD	40.0							
DFC - ICICI IX	IBRD			40.0					
DFC - ICICI X	IBRD						40.0		
Education - Agric. University	IDA			20.0					
Education Unidentified	IDA						20.0		
Fertilizer - Nangal (Public)	IDA			20.0					
Fertilizer - Cochin (Public)	IDA		20.0						
Fertilizer - Debottlenecking	IDA		5.0						
Iron Ore - Marcona	IDA				40.0				
Industry - Unidentified	IDA				25.0				
Industrial Imports VI	IDA	75.0							

(Contd.)

IVa. INDIA - 5 YEAR LENDING PROGRAM

(Contd.)		1970	1971	1972	1973	1974	1975	1964-68	1969-73
		($ millions)							
Family Planning	IDA			15.0					
Power Transmission	IDA		75.0						
Power Transmission	IDA			60.0					
Power Unidentified II	IDA				15.0				
Power Unidentified III	IDA					15.0			
Power Unidentified IV	IDA						60.0		
Highways II	IDA			30.0					
Railways X	IDA	55.0							
Railways XI	IDA			50.0					
Shipping	IDA			80.0					
Transportation Projects Unident.	IDA				60.0				
Transportation Projects Unident.	IDA					50.0			
Water Supply - Bombay	IDA			27.5					
Water Supply Unidentified I	IDA				15.0				
Water Supply Unidentified II	IDA					15.0			
Unallocated I	IDA				15.0				
Unallocated II	IDA					35.0			
Unallocated III	IDA						40.0		
	IBRD	40.0		40.0			40.0	189.0	120.5
	IDA	227.5	297.4	532.5	360.0	320.0	320.0	591.0	1560.5
	Total	267.5	297.4	572.5	360.0	320.0	360.0	780.0	1681.0
	No.	6	9	14	14	12	12	13	52
Note: the IDA lending program is to be adjusted to --			245.0	350.0	350.0	350.0	350.0		

2/19/71

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LM/M/71-13

February 23, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Attached for information are the Minutes of a Special Loan Meeting to consider "India - Request for Shipping Credit" held at 3:30 p.m. on Friday, February 5, 1971 in Conference Room A.

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

Copies for Information:

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

LM/M/71-13

February 23, 1971

Minutes of Special Loan Meeting to consider "India - Request for Shipping Credit" held at 3:30 p.m. on Friday, February 5, 1971 in Conference Room A.

1. Present: Messrs. Knapp (Chairman), Cope, Aldewereld, Cargill, Chadenet, Diamond, Gabriel, R.K. Jones (IFC), Knox, Nurick, Mackay, H. Scott, Votaw, Carmichael, Kirk, Pollan, Dunn, Mrs. Hamilton, T.M. Jones and Pearce (Secretary).

2. Issue: The meeting had been called to consider Mr. Votaw's memorandum of January 28, 1971 to Messrs. Knapp and Cargill, which (a) recommended that IDA should consider in principle the Indian Government's request for assistance to finance the purchase of ships, and (b) requested authorization to proceed with pre-appraisal of a project immediately with a view to its presentation to the Directors for approval in FY 1972, and Mr. Carmichael's memoranda of November 19 and December 23, 1970.

3. Discussion: The meeting noted that:

(a) The Indian Government was currently seeking about $200 million to finance the purchase of 4 crude oil tankers of 80,000/100,000 dwt each, 4 ore/bulk/oil carriers of 150,000 dwt each and 4 coastal oil products tankers of 16,000 dwt each. It was exploring several sources of capital for this purpose, including Consortium members and IDA, and hoped to secure substantial IDA assistance, i.e. a credit of up to $80 million.

(b) A recent Transportation Projects Department mission had concluded that, prima facie, investment in shipping by the Indians would be economically justified, principally on the grounds of its contribution, direct and indirect, to foreign exchange savings/earnings.

(c) The Bank had already financed ships directly in the Netherlands (Loan Nos. 7-10-NE), and indirectly through DFC intermediaries in India, Korea, Pakistan and the Philippines, and IFC was presently considering ship financing proposals from India and elsewhere. However, ICICI (India) and IFC would only be able to finance a small fraction of India's overall requirements and in view of India's limited capacity to service additional debt on conventional terms, Bank Group financing would in principle be justified.

(d) Owing to their existing debt structure and involvement in the international general cargo trade, the question whether Indian shipping companies would be suitable intermediaries/recipients of Bank Group funds required further study. The establishment of a Government-owned, non-ship operating company as the principal recipient of eventual Bank Group financing was a possible approach but might be cumbersome and time-consuming. The Government's existing Shipping Development Fund or the Indian Oil Corporation and Minerals and Metals Funding Corporation might be suitable alternative channels.

(e) Until the details of the Indians' proposal had been worked out, it would be difficult to decide what form of international competitive bidding would be appropriate in the circumstances. The order books of shipyards and the premium attached to early delivery might effectively limit bids only to those suppliers able to deliver in 1973-74. This issue and others, such as relending terms and disbursement procedures, would require further careful study.

4. Decision: The Chairman approved the South Asia Department's recommendation (a) that Bank Group financing of Indian ship purchases be considered in principle and (b) that a project be pre-appraised forthwith with a view to its presentation for approval in FY 1972. However, he expressed doubt whether $80 million was an appropriate amount for an initial operation. The proposed project would not preclude further ship financing by ICICI nor prejudice IFC activities in this field at a later date.

David Pearce
Secretary

Cleared by: Messrs. Knapp
Chadenet
Diamond
Knox/Carmichael
Nurick
Votaw/Mrs. Hamilton

cc: Loan Committee
Participants

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

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LM/M/71-12

February 23, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Attached for information are the Minutes of a Special Loan Meeting to consider "Mauritius - Tea Development Authority Project" held at 4:30 p.m. on Wednesday, February 3, 1971 in Conference Room A.

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

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

LM/M/71-12

February 23, 1971

Minutes of Special Loan Meeting to consider "Mauritius - Tea Development Authority Project" held at 4:30 p.m. on Wednesday, February 3, 1971 in Conference Room A.

1. Present: Messrs. Knapp (Chairman), Cope, Aldewereld, Baum, Evans, Lejeune, Nurick, Collier, Hilmy, Takahashi, Rowe, Vita and Pearce (Secretary).

2. Issue: The meeting had been called to consider the Eastern Africa Department's memorandum of January 5, 1971 to the Loan Committee entitled "Mauritius - Tea Development Authority Project" (LC/O/71-2), which recommended a $5.2 million credit to help finance the second phase of Mauritius' smallholder tea development program, and Mr. Malone's memorandum and attachment of January 14 to the Chairman. There were two main issues for discussion: (a) the project's economic justification, and (b) the financial arrangements between the Mauritius Tea Development Authority (MTDA) and the Government.

3. Discussion: Apropos the project's economic justification, the meeting noted that:

(a) Mauritius had a high rate of unemployment and a single crop economy. Sugar accounted for about 95 per cent of the island's cultivated area as well as of exports. Tea had become its second crop and offered a rare opportunity for diversifying agriculture, increasing export earnings, and creating employment.

(b) Most tea produced from the project would be exported, mainly to South Africa, but Mauritius' exports would constitute only about 0.5 per cent of world tea trade. Yields were good and compared favorably with average yields in Kenya, Malawi and Uganda.

(c) The project's principal economic justification, in addition to increased output and foreign exchange earnings, would be the creation at relatively low capital cost of about 4,000 jobs, which would not only have social benefits but would also reduce Government relief payments. The absence of alternative employment opportunities in Mauritius and the prospect of reduced relief payments as a result of the project justified the appraisal report's assumption of a zero shadow cost of labor (cf. para. 8.04).

4. Apropos the financial arrangements between the Government and MTDA, the meeting noted that, instead of the appraisal report's recommendation that the Government's contribution be quasi-equity, MTDA would be required to repay the Government over 20 years, beginning with the completion of the project (cf. Mr. Malone's memorandum, para. 3).

5. Decision: The Chairman approved the Eastern Africa Department's recommendation that negotiators be invited for the proposed credit.

David Pearce
Secretary

Cleared by: Messrs. Knapp
Baum
Nurick
Takahashi
Vita

cc: Loan Committee
Participants

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

February 22, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Brazil - Sao Paulo Water Supply and Pollution Control

1. The Committee is requested to consider, without meeting, the attached memorandum dated February 22, 1971 from the South America Department, entitled "Brazil - Proposed Bank Loans for Sao Paulo Water Supply and Pollution Control Project" (LC/O/71-22).

2. Comments, if any, should be sent to reach Mr. Dutt (ext.2660) by 5:00 p.m. on Wednesday, February 24.

3. It is planned then, if the Committee approves, to inform representatives of the Government of Brazil, the Government of Sao Paulo State, SAEC and SANESP that the Bank is prepared to begin negotiations for the proposed loans on the terms and conditions referred to in the attached memorandum.

David Pearce
Secretary
Loan Committee

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Committee:

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

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Vice President (IFC)

CONFIDENTIAL

LC/0/71-22

February 22, 1971

LOAN COMMITTEE

Memorandum from South America Department

BRAZIL - Proposed Bank Loans for Sao Paulo Water Supply and Pollution Control Project

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1. Attached is Appraisal Report No. PU-61 recommending two Bank loans totalling $37 million to finance the foreign exchange cost of the Sao Paulo Water Supply and Pollution Control Project. The proposed loans would be:

(i) $22 million to Superintendencia de Agua e Esgotos da Capital (SAEC), the retail water and sewerage agency; and

(ii) $15 million to Companhia Metropolitana de Saneamento de Sao Paulo (SANESP), the bulk sewerage authority.

These would be the first Bank loans for water supply and pollution control in Brazil. The two agencies complement each other in serving the Sao Paulo metropolitan area and work under the guidance of the State Government.

The Lending Program

2. An $8.4 million Bank loan for the Technical and Agricultural Education Project and a $70 million Bank loan for the Salto Osorio Hydroelectric Project are under negotiations. Appraisal Reports are currently being prepared for all the other projects scheduled for the fiscal year. The five-year program (fiscal years 1971-1975) is attached.

The Economy

3. The recent economic report on Brazil (WH-203) issued on November 4, 1970 indicates that in the last three years the Brazilian economy sustained rapid growth while the country's international liquidity position has been strengthened. Brazil continues to be creditworthy for substantial amounts of Bank lending.

The Project

4. The urban population of Brazil is inadequately served by public water supply and sewerage systems. Only 40 percent receive assured round-the-year piped water, less than 60 percent are supplied by public water systems at all and sewerage services are even more scarce. While the urban infrastructure is weak all over Brazil, its inadequacy is faced

in an acute form in the metropolitan area of Sao Paulo, where of the 8 million people about half have no piped water and two-thirds no sewers. The city's rivers, the main source of water to the city's growing industries, are now practially pure sewage.

5. The Sao Paulo State Government is engaged in improving the situation and has before it a works program totalling $750 million for the 1970s. Since 1968 three institutions have been organized to share the responsibility of serving the metropolitan area: (1) An autonomous company, Companhia Metropolitana de Agua de Sao Paulo (COMASP), with shares held by the State Government and 25 municipalities in the area, is responsible for bulk water supply; (2) SAEC, semi-autonomous entity, distributes the water and collects sewage in Sao Paulo municipality; and (3) SANESP, a state-owned company, is responsible for treatment and disposal of bulk sewage of the metropolitan area. Bank financing has been sought for the programs of SAEC and SANESP for the years 1971-1974, which will enable an additional two million persons to have piped water from the greatly expanded bulk supply expected to be available in the next few years, improve service in the overloaded sections of the network, improve sewage collection and disposal and markedly reduce the pollution of Sao Paulo's rivers. These works are closely coordinated with each other and with those of COMASP and the municipalities in the area.

6. The SAEC project will cost $59.8 million and the SANESP project $81.5 million. These two should be viewed as an integral project, are interdependent financially and technically but on legal considerations two loans are proposed. The proposed Bank loans of $22 million and $15 million respectively will finance the cost of foreign procurement, foreign exchange cost of consultants and the estimated foreign exchange component of local procurements and civil works. About 20 small civil works contracts (each costing less than $1 million; all together about $14 million), with low foreign exchange contents, would be tendered locally but open to foreign bidders. The appraisal report recommends the Bank loans with a 25 year maturity including a 4½ year grace period.

7. In addition to the usual guarantee of the Federal Government, the Government of Sao Paulo State would guarantee sufficient funds for these two organizations and administrative cooperation necessary for successful implementation of the project.

8. The Loan Agreement with SAEC would include covenants for tariff increases so as to yield a rate of return of at least 5½ percent in 1972 and 7 percent thereafter on the net fixed assets; and for reorganization of SAEC to confer on it full administrative and financial autonomy. The Loan Agreement with SANESP would include a covenant for setting tariffs so as to yield a 7½ percent return on net fixed assets. To reduce future water pollution, a covenant will provide for the State Government to enact regulations compelling industry to use waste disposal

facilities where available. These points have already been discussed with the present Government and the Governor-Elect of Sao Paulo and would be acceptable to them. A draft legislation to enable the Government to revise the tariffs is under preparation. From the date of legislation the executive process - issuing a decree on revised tariffs, of examination of objections and confirmation of the higher tariffs - would need about 90 days, and legislative action to enable tariff increases will be a precondition for Board presentation of these loans and executive action for the increase of SAEC tariffs by at least 50 percent a condition for effectiveness of the loans.

Recommendations

9. I recommend that the Bank inform the Government of Brazil, the Government of Sao Paulo State, SAEC and SANESP that it is prepared to negotiate a loan of $22 million to SAEC and $15 million to SANESP for the Sao Paulo Water Supply and Pollution Control Project under the terms and conditions set forth in the attached appraisal report.

Gunter K. Wiese
Deputy Director

Attachments.

Population: 93.3 m
GNP Per Cap: $286

BRAZIL - 5 YEAR LENDING PROGRAM

($ millions)

		Fiscal Year 1971	1972	1973	1974	1975	1976	Total 1964-68	Total 1969-73
Land Settlement I	IBRD		10.0						
Agricultural Credit I	IBRD		20.0						
Land Settlement II	IBRD				30.0				
Agricultural Credit II	IBRD					30.0			
Agricultural Research in NE	IBRD			10.0					
Livestock II	IBRD						60.0		
DFC - Industrial Finance I	IBRD		12.5						
DFC - BNB II	IBRD			35.0					
DFC - Industrial Finance II	IBRD				50.0				
DFC - BNB III	IBRD					40.0			
DFC - Industrial Finance III	IBRD						60.0		
Education I	IBRD	8.4							
Education II	IBRD			20.0					
Iron Ore - MBR	IBRD	50.0							
Steel - USIMINAS	IBRD		40.0						
Steel - COSIPA	IBRD		50.0						
Steel - CSN	IBRD		70.0						
Iron Ore - North	IBRD				50.0				
Power - Salto Osorio	IBRD	70.0							
Power - Sao Simao	IBRD		75.0						
Power - Itumbiara	IBRD				75.0				
Power - Agua Vermelha	IBRD					75.0			
Power - Unidentified	IBRD						75.0		
Highways III	IBRD		100.0						
Highways IV	IBRD			100.0					
Sao Paulo Beltway	IBRD			60.0					
Highways V	IBRD					100.0			
Highways VI	IBRD						100.0		
Ports I - Santos	IBRD	50.0							
Ports II - Recife	IBRD		10.0						
Ports III - Rio	IBRD			15.0					
Railways I - MBR Link	IBRD	45.0							
Railways II	IBRD		50.0						
Railways III	IBRD				50.0				
Transportation Unidentified	IBRD				75.0				
Transportation Unidentified	IBRD					75.0			
Water Supply - Sao Paulo	IBRD	37.0							
	IBRD	260.4	437.5	240.0	330.0	320.0	295.0	291.1	1180.8
	No.	6	10	6	6	5	4	10	28

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

February 18, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Papua and New Guinea - Hydroelectric Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated February 18, 1971 from the East Asia and Pacific Department, entitled "Papua and New Guinea - Proposed US$23.2 Million Loan for a Hydroelectric Project" (LC/O/71-21).

2. Comments, if any, should be sent to reach Mr. John Riddell (ext. 2227) by 5:00 p.m. on Monday, February 22.

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

David Pearce
Secretary
Loan Committee

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Committee:

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

CONFIDENTIAL

LC/O/71-21

February 18, 1971

LOAN COMMITTEE

Memorandum from East Asia and Pacific Department

Papua & New Guinea: Proposed US$23.2 million Loan for a Hydroelectric Project

1. There is attached for consideration by the Committee an Appraisal report dated February 4, 1971 (PU-60) on Phase I of the first stage of the Upper Ramu hydroelectric development in the Territory of Papua and New Guinea ("the Territory"). The Administration of the Territory ("the Administration") through the Commonwealth of Australia ("the Commonwealth") has requested Bank Group financing for the proposed project.

2. The project would be the Bank Group's first involvement in the Territory's power system. A loan of US$7 million for a Telecommunications Project (546 PNG) was made in 1968; IDA credits of US$1.5 million in January 1969 (137 PNG) and US$5.0 million (175 PNG) in January 1970 contributed to the financing of a group of smallholder oil palm, beefcattle ranch and coconut estate projects. The execution of these projects has been satisfactory. Disbursements, however, have been slow. The delays have arisen in the Territory Administration which is hampered by shortages of professional, particularly accounting, staff. Steps are being taken to correct these shortages and substantial amounts of the loan and credits are expected to be drawn down before the end of FY 1971. A highway loan and credit (693 PNG and 204 PNG) were signed in June 1970. Contracts have now been let and disbursements should start shortly.

The Economy

3. A report on the "Economic Position and Prospects of the Territory" (EAP-8a) was distributed to the Executive Directors on September 3, 1969. An economic mission to update this report will visit the Territory shortly. The forecasts made in 1969 did not allow for the effects on the economy of the initial stages of development of the copper deposits on Bougainville Island. The Administration is currently revising the development program (1968/69 - 1972/73) in the light of these activities. The immediate effects of this development are to place an increased strain on the Administration's resources to provide the infrastructure without which the mining company cannot operate. The long-term effects of copper mining will be to generate substantial additional revenue in the Territory and for the Administration. It is expected that in the three years to June 30, 1972 the Administration (as taxing authority, reciver of royalties and part owner) will receive A$22 million from these sources, in the five years to June 30, 1977 A$159.5 million and the five years to June 30, 1982 A$251.2 million. However, in

these periods, it will have to meet capital outlays and debt redemption estimated to amount to A$75.2 million, A$60.9 million and A$92.7 million respectively. In the short term, the heavy additional strains on the Administration require maximum assistance from the Commonwealth of Australia and other external sources.

4. In the year to June 30, 1970, the GNP of the monetized sector (at current priees) increased by nearly 25 percent to A$323 million compared with an annual average increase of 14.8 percent over the preceding four years. The largest single increase was in private capital formation which rose by 156 percent (or A$80.3 million); there was also a rise of 12.6 percent in public sector expenditure on goods and services. Total outlays by the Administration amounted in 1969/70 to A$204 million, a rise of 37 percent. The increase in public expenditure was financed partly by additional internal revenue, up 30 percent, and partly by borrowings which increased from A$7.2 million in 1968/69 to approximately A$34.5 million in 1969/70. A$12.5 million of this borrowing was for the first tranche of the 20 percent participation in the equity of Bougainville Copper Pty. to be held by the Administration as trustee for the people of the Territory. Direct Australian grant assistance (A$97.3 million) financed 48 percent of the Administration's total expenditure.

5. The Bank's current five-year lending program for the Territory is attached as Annex I. Since this program was reviewed in January 1970, cost increases have affected the Highway Loan and Credit and Agricultural Development Credit, signed in FY 1970 and the proposed Hydroelectric project. The second Telecommunications project has been brought forward from 1973 to 1972 and increased to $10 million and the estimated cost of the Ports project in 1972 has risen from $3.0 million to $5.0 million. The second Highway project has been deferred from 1972 to 1973 and its estimated cost raised from $12 million to $15 million. The revised lending program reflects the immediate need for aid, outlined in paragraph 3 above, with smaller annual programs in 1974 and 1975. This program will be reviewed by Mr. Knapp in March.

The Project

6. The project for which Bank assistance has been requested is Phase I of the first stage of a hydroelectric power scheme on the Ramu River in the Territory's Eastern Highlands district. It forms part of the five-year development plan of the Electricity Commission of Papua and New Guinea (Elcom), which provided, as of June 30, 1970, 67 percent of the total generation of power in the Territory. The completed project will consist of three 15MW units in an underground power station and about 300 miles of transmission lines serving the principal centers in the Territory's highlands. The peak demand for power in these centers was 9.2 MW during the year to June 30, 1970 and is expected to have reached about 55MW by June 30, 1978. This assumes an increase of about 25 percent annually, as in previous years. The project, which has an internal rate of return of 17-1/2 percent,

provides a more economic source of supply of energy for the area than the cheapest known thermal alternative.

7. Phase 2 of the first stage of the RAMU scheme would be construction of a dam and two further 15MW units. The effect of Phase I and 2 on the ecology and population of the construction area has been considered and assurances are to be sought during negotiations that all measures be undertaken to minimize the health risk at the time of the construction of the dam. No other adverse ecological impact is expected.

8. Elcom's financial position is satisfactory throughout the project period, and its debt/equity ratio is expected to improve from 88/12, at June 30, 1971 to about 67/33 at June 30, 1978. A covenant would be included in the loan documents, setting a rate of return on net assets of not less than 9 percentfor the FY's 1972 to 1976 and not less than 10 percent thereafter. Assurances will also be sought that Elcom will not incur additional debt unless internal cash generation is sufficient to cover total debt service not less than 1.5 times. As mentioned in paragraph 8.05 of the Appraisal Report, assurances are also to be obtained at negotiations about Elcom's legal title to its fixed assets. This is not expected to give rise to any difficulty.

9. Elcom's management is largely expatriate but steps are being taken to reduce the proportion of expatriate staff from its present level of 42 percent (335) to 5 percent. This involves Elcom in heavy expenditure for training of new staff, and assurances are to be obtained at negotiation that the Administration will provide an annual subsidy for this training program. None of the other covenents to be sought are unusual or are likely to cause difficulty during negotiations. It is not now intended to request the supplementary letters as suggested in paragraph 9.02 of the Appraisal Report. These matters will be discussed and minuted at negotiations, but the Projects Department has agreed that they do not bear directly on the execution of the project.

Financing

10. The total cost of the project is estimated at A$30.3 million (US$ 33.9 million) with an "offshore component" of A$20.7 million (US$23.2 million). As in previous loans to the Territory, which is part of the Australian monetary system, Australian procurement would be treated as a foreign cost and therefore eligible for Bank financing. The proposed loan amounting to US$23.2 million would therefore cover all the "offshore component." Local costs will be financed by loans from the Administration and internal cash generation. The loan, it is estimated, will be fully disbursed by June 30, 1976. Contrary to the proposal in paragraph 7.05 of the Appraisal Report, the Projects Department has agreed that any savings in the "offshore component" would result in the cancelling of an equivalent amount of the proposed loan.

11. As in previous Bank loans the Borrower would be the Administration; the Commonwealth would be the guarantor and Elcom, with which a project agreement is to be concluded, would be the beneficiary. The Commonwealth has stated it wishes the loan to be made to the Administration and not direct to Elcom. In the present state of the Territory's advance toward self-government they do not wish to prejudice either the future relationship of the independent government towards its power authority or the government's external suurces of finance. Elcom, a largely expatriate-staffed institution, would, with a direct debtor relationship with the Bank, be in too strong a position vis-a-vis the future government.

12. Subject to the comments in paragraphs 9 and 10, I recommend that the Administration, the Commonwealth and Elcom be invited to send representatives to Washington to negotiate a Bank loan of US$23.2 million for the Upper Ramu hydroelectric project on the terms and conditions set forth in the attached report.

Attachment

Douglas J. Fontein
East Asia and Pacific Department

Population (million): 2.50
GNP Per Capita 1970 (estimated): $200

Annex I

Papua and New Guinea Five-Year Lending Program
(US$ million)

			1968	1969	1970	1971	1972	1973	1974	1975	Total 1964-68	Total 1969-73	Total 1971-75
Agricultural Development	I	IDA		1.5									
	II	IDA			5.0								
	III	IDA						3.0					
	IV	IDA								5.0			
	V	IBRD								5.0			
Education	I	IDA							4.0				
	II	IDA											
Public Utilities													
Telecommunications	I	IBRD	7.0										
Telecommunications	II	IBRD					10.0						
Upper Ramu Hydro-electric		IBRD				23.0							
Transportation													
Highways	I	IBRD			4.5								
Highways	I	IDA			4.5								
Highways	II	IBRD						15.0					
Ports	I	IDA					5.0						
		IBRD	7.0	-	4.5	23.0	10.0	15.0	-	5.0	7.0	52.5	53.0
		IDA	-	1.5	9.5	-	5.0	3.0	4.0	5.0	-	19.0	17.0
			7.0	1.5	14.0	23.0	15.0	18.0	4.0	10.0	7.0	71.5	70.0
	No:		1	1	2	1	2	2	1	2	1	8	8
	Net:					23.0	15.0	18.0	4.0	10.0		71.5	70.0
IBRD Loans Outstanding													
- including undisbursed			6.7	6.7	11.2	34.2	44.2	59.2	63.9	68.5			
- excluding undisbursed			-	-	0.6	4.0	9.0	20.2	44.2	57.8			
IDA Credits Outstanding													
- including undisbursed			-	1.5	11.0	11.0	16.0	19.0	23.0	28.0			
- excluding undisbursed			-	-	0.7	7.2	12.5	15.3	18.5	22.5			

East Asia & Pacific Dept.
February 1 , 1971

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LC/A/71-3/1

February 17, 1971

NOTICE OF MEETING

Nigeria - Rehabilitation Program Loan

The Committee will resume consideration of the Western Africa Department's memorandum of February 12, 1971 on this subject (LC/0/71-18) tomorrow, Thursday, February 18, 1971 at 10:30 a.m. in Room C-1006.

David Pearce
Secretary
Loan Committee

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Committee:

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

Form No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

February 16, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Yugoslavia - Multipurpose Water Project

1. The Committee is requested to consider, without meeting, the attached memorandum dated February 16, 1971 from the Europe, Middle East and North Africa Department, entitled "Yugoslavia - Proposed $40 Million Loan for a Multipurpose Water Project" (LC/O/71-20).

2. Comments, if any, should be sent to reach Mr. Kopp (ext. 4711) by 5:00 p.m. on Friday, February 19.

3. It is planned then, if the Committee approves, to inform the Federal Government, the Government of the Socialist Autonomous Province of Kosovo and representatives of the Ibar-Lepenac Enterprise (ILE) that the Bank is prepared to begin negotiations for the proposed loan on the terms and conditions referred to in the attached memorandum.

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

CONFIDENTIAL

LC/O/71-20

February 16, 1971

LOAN COMMITTEE

Memorandum from Europe, Middle East and North Africa Department

YUGOSLAVIA - Proposed $40 Million Loan for a Multipurpose Water Project

1. Attached for consideration by the Loan Committee is the Appraisal Report (PU-58) dated January 15, 1971, on the Ibar Multipurpose Water Project. The Bank has made 16 loans to Yugoslavia totalling $475 million, but the proposed loan would be the first for water supply or agriculture. Four previous loans were made for power projects, or projects with a power component. Three more projects are under preparation which should lead to lending operations in FY 1971, two tourism projects and one road project. The Five-Year Lending Program is attached. A recent economic mission to Yugoslavia is now preparing its report; its preliminary findings confirm the priority of the proposed project and Yugoslavia's creditworthiness for Bank lending.

2. The proposed project would be the first phase in the implementation of a master plan for development of water resources in the Kosovo plain and would provide water supply mainly to industries and also to communities, for irrigation of 30,000 ha and for the generation of 95 Gwh of peak power annually.

Project Issues

Devaluation

3. The Appraisal Report was drafted before the devaluation of the Dinar was announced on January 23, 1971 (from Din.12.5 to Din. 15.0 = $1). However, the economic calculations in the report anticipated the effect of this devaluation and the project remains economically fully justified, the economic rate of return being estimated at about 14 percent. Revisions in the presentation of the economic justification reflecting the actual change in the exchange rate will be incorporated in the revised report to be distributed to the Executive Directors.

4. The devaluation affects the project cost estimate in two ways. A simple conversion at the revised exchange rate of the local costs, expressed in dinars, results in a reduced dollar equivalent of the local portion of project costs. A possible further consequence of devaluation, however, is

price increases in Yugoslavia in excess of the 6 percent rate of inflation used in the report's cost estimates. If local costs are simply converted at the present exchange rate the project cost estimate drops to US $84.7 million equivalent, but the probable increased inflation in local prices will tend to increase project costs towards the previous estimate of US $97.0 million.

5. The Yugoslavs are presently reviewing the cost estimate with their consultants. The report's cost estimate is based on data prepared in mid-1969. The consultants are updating these costs to take into account significant price increases in two periods: from mid-1969 to the end of 1970 (based on assessment of actual cost increases in that period), and probable future price increases from 1971 until project completion in 1975. The revised estimate of costs, which should be between US $84.7 and US $97.0 million, is expected to be received before the end of February.

6. The financial calculations need to be adjusted to reflect changes in project cost, financing requirements, amortization of loans and revenue requirements of the Ibar-Lepenac Enterprise (ILE) as a result of the change in the exchange rate. These changes will be made in a working paper which will form the basis of the discussion during negotiations. The adjusted financial calculations will be incorporated in the revised report. No changes in financial covenants are expected as a result of the change in the exchange rate.

Loan Amount

7. I recommend, and the Public Utilities and Agriculture Projects Departments agree with, a loan of $40 million for the proposed multipurpose water supply, irrigation, and power project. This loan amount is justified by the following:

(a) A major objective of our lending program for Yugoslavia is to accelerate development in the lesser developed regions in order to help overcome the substantial regional disparities. The Province of Kosovo is Yugoslavia's most backward area. In absolute terms and per capita it has received as yet only very little Bank assistance. The proposed project is vital for the further development of this Province and is given top priority by both the Provincial and Federal authorities.

(b) Local funds, which would be provided for the project principally by the Fund for Lesser Developed Regions, are very limited. The distribution of loans from the Fund has been fixed on a national level, taking into account the needs of all lesser developed regions. During the recent Bank mission, the Provincial Government reiterated its request for the Bank to consider a loan larger than the \$34 million loan originally envisaged. It was pointed out that other badly needed infrastructure projects in this most underdeveloped region of Yugoslavia would have to be deferred since the Ibar project has first claim in the allocation of their limited funds. Also the Federal Government has strongly supported this request for a loan larger than \$34 million, in line with its policy and ours on assisting less developed regions.

(c) A Bank loan of \$40 million would finance about \$34 million of project costs and about \$6 million for interest during construction. This would mean that the Bank would finance not more than 40 percent of the project costs (depending on the revised project cost), excluding a further \$10.6 million of costs financed outside the Bank-assisted project (see paragraph 3.07). In the last three years the Bank has financed at least 40 percent of all infrastructure project costs in Yugoslavia, most of which have been in much more developed regions.

<u>Local Cost Financing</u>

8. In the estimate of the probable foreign exchange component, it has been assumed that the largest single contract (construction of the Gazivode dam) would be won by a foreign contractor and that Yugoslavs would win all other contracts. This would result in a foreign exchange component of about \$23.6 million. In addition to \$6 million for interest during construction, the proposed loan is therefore expected to finance also \$10.4 million of local currency expenditures. A loan limited to the foreign exchange component of this high priority project would not provide the desirable level of support for infrastructure investment in Kosovo, the least developed area of Yugoslavia. Inclusion of some local currency financing in our loan would be in line with the decisions taken at last year's CPP review in Mr. McNamara's office.

<u>Lending Arrangements</u>

9. The Bank loan would be made to the Socialist Federal Republic of Yugoslavia which in turn would conclude a subsidiary agreement with ILE on the original Bank terms (30 years including six years' grace, usual Bank interest rate and commitment charges). In addition, a project agreement would be signed by the Bank on the one hand and both ILE and the Socialist Autonomous Province of Kosovo on the other hand to ensure proper execution and operation of the Ibar project. Since ILE will not become a fully autonomous enterprise before completion of construction, it would enter into the project agreement initially as an enterprise directed by appointees of the Provincial Government.

Issues for the Negotiations

10. Satisfactory agreement should be reached or assurances obtained on a fairly large number of issues as listed in paragraph 7.02 of the Appraisal Report. These issues are to a large extent already agreed upon in principle, but should be confirmed during negotiations. They include:

(a) provision of adequate local funds for the project (satisfactory loan agreement between the Fund for Lesser Developed Regions and ILE) including a commitment to cover cost overruns;

(b) a margin of preference of 15 percent for local suppliers for the evaluation of bids and a few conditions normally required concerning inter alia continued employment of consultants, exemption of project equipment from import licenses, financial rates of return required to be maintained by ILE, and limitation on further long-term debt of ILE;

(c) related project facilities not financed by the Bank loan to be implemented mainly by the Provincial Government of Kosovo, also including construction of a transmission line by Kombinat Kosovo;

(d) certain studies to be carried out by consultants;

(e) purchase contracts between ILE and its industrial consumers for water or electricity;

(f) inputs required to ensure the realization of benefits in agriculture, including provision of extension services, farm inputs, production credits and Provincial Government's contribution to irrigation water charges in the early years of the project operation.

Recommendation

9. I recommend that the Bank invite the Federal Government, the Government of the Socialist Autonomous Province of Kosovo, and the Ibar-Lepenac Enterprise (ILE) to send representatives to negotiate a loan of $40 million for the Ibar Multipurpose Project on the lines indicated in Section VII of the Appraisal Report.

M. P. Benjenk
Director

Attachment

Population: 19.9 m
GNP Per Cap: $570

IVa. YUGOSLAVIA - 5 YEAR LENDING PROGRAM

		($ millions)							
		Fiscal Year						Total	Total
		1971*	1972	1973	1974	1975	1976	1964-68	1969-73
Forestry II	IBRD			10.0					
DFC - YIB I	IBRD		20.0						
DFC II	IBRD			25.0					
DFC III	IBRD					30.0			
Industry Modern. IV	IBRD				20.0				
Power	IBRD		20.0						
Tourism I - Bernadin	IBRD	10.0							
Tourism II - Babin Kuk	IBRD	20.0							
Tourism III	IBRD		15.0						
Tourism IV	IBRD				15.0				
Roads V	IBRD	36.0							
Roads VI	IBRD			30.0					
Roads VII	IBRD				30.0				
Railways	IBRD					30.0			
Water Supply - Ibar	IBRD	34.0							
Multipurpose				25.0					
Water Supply - Multipurpose II	IBRD								
Unallocated I	IBRD		20.0						
Unallocated II	IBRD			10.0					
Unallocated III	IBRD				10.0				
Unallocated IV	IBRD					15.0			
IBRD		100.0	75.0	100.0	75.0	75.0		175.5	419.5
No.		4	4	5	4	3		5	18

P & B 8/21/70
* revised in accordance with latest timetables: EMENA 2/10/71

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LM/M/71-11

February 16, 1971

MEMORANDUM TO THE LOAN COMMITTEE

Attached for information are the Minutes of a Special Loan Meeting to consider "Pakistan - Second Foodgrain Storage Project (E. Pakistan)" held at 2:30 p.m. on Friday, February 5, 1971 in Conference Room A.

David Pearce
Secretary
Loan Committee

\- DISTRIBUTION -

Committee:

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

LM/M/71-11

February 16, 1971

Minutes of Special Loan Meeting to consider "Pakistan - Second Foodgrain Storage Project (E. Pakistan)" held at 2:30 p.m. on Friday, February 5, 1971 in Conference Room A.

1. Present: Messrs. Knapp (Chairman), Cope, Cargill, Chadenet, Nurick, Votaw, Wapenhans, Melmoth, Gordon, Helmers, Wiehen, Goldberg, J.H. Stewart, Eccles and Pearce (Secretary).

2. Issue: The meeting had been called to consider the South Asia Department's memorandum of February 2, 1971 to the Loan Committee entitled "Pakistan - Development Credit for the Second Foodgrain Storage Project in East Pakistan" (LC/O/71-13), which recommended that negotiators be invited for a $10.5 million credit to finance half the estimated foreign exchange costs of expanding and improving East Pakistan's foodgrain handling and storage system; the other half would be financed by the Swedish International Development Authority (SIDA). The Agriculture Projects Department's detailed recommendations (cf. appraisal report, para. 6) raised several issues for discussion (cf. South Asia Department's memorandum, para. 11).

3. Discussion: The meeting noted that:

(a) The IDA/SIDA credit would include $0.8 million in respect of foreign exchange overruns on the first foodgrain storage project (Credit No. 83-PAK), which was now expected to cost $2.8 million more than originally estimated, owing to higher silo construction costs. The Government would finance $2 million local cost overruns.

(b) The Government's commitment to consult with IDA before making future appointments to the position of Project Director would be the subject of a covenant in the credit agreement, as recommended in para. 6.01(e) of the appraisal report. It was agreed that the principle of requiring borrowers to consult with the Bank/IDA on future appointments to project entities by means of specific covenants in loan/credit agreements was an issue which the Loan Committee should review at an early date, on the basis of data currently being assembled by the Projects Departments concerned.

(c) The appropriate means of improving the organization of the Food Department of the Government of East Pakistan, for which the appraisal report recommended management consultants as a condition of effectiveness of the credit, should be considered further and decided by the departments concerned on the basis of negotiations with the Pakistanis. Whatever was then agreed should be expressed in the form of a covenant, to be complied with by an agreed date, rather than as a condition of effectiveness.

(d) In order, on the one hand, to make international competitive bidding for the godown rehabilitation program meaningful and, on the other, to discourage unqualified local contractors from bidding unnecessarily, the appraisal report recommended that \$500,000 be established as the minimum bid package amount. However, since this amount might also disqualify some competent local contractors, it was agreed that bids could be submitted for sub-packages of anything over \$100,000.

(e) The proposed joint IDA/SIDA credits would finance the project's foreign exchange component, i.e. \$21 million or 54 per cent of total project costs. The question of a possible larger contribution, e.g. 60 per cent, would be discussed with Swedish Government representatives during negotiations. In any event, disbursements against expenditures for godown rehabilitation would be on the basis of an agreed percentage, not actual foreign exchange costs, in view of the difficulty for local contractors of documenting such expenditures.

4. Decision: The Chairman approved the South Asia Department's recommendation that negotiators be invited for the proposed credit substantially in accordance with the conditions proposed in the appraisal report, as modified by paras. 3(c) (d) and (e) above.

David Pearce
Secretary

Cleared by: Messrs. Knapp
Chadenet
Votaw/Wiehen/Stewart
Nurick
Wapenhans

cc: Loan Committee
Participants

FORM NO. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LC/A/71-4

February 16, 1971

NOTICE OF MEETING

A Meeting of the Loan Committee will be held on Thursday, February 18, 1971 at 4:15 p.m. in the Board Room.

AGENDA

Yugoslavia - Babin Kuk Tourism Project

The Committee will consider the attached memorandum from the Europe, Middle East and North Africa Department dated February 16, 1971, entitled "Yugoslavia - Proposed Loan for Babin Kuk Tourism Project" (LC/0/71-19).

David Pearce
Secretary
Loan Committee

\- DISTRIBUTION -

Committee:

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

CONFIDENTIAL

LC/0/71-19

February 16, 1971

LOAN COMMITTEE

Memorandum from Europe, Middle East and North Africa Department

YUGOSLAVIA - Proposed Loan for Babin Kuk Tourism Project

1. Attached for consideration by the Loan Committee is an appraisal report entitled "Appraisal of the Babin Kuk Tourism Project" (PT-1), dated January 15, 1971, which recommends a Bank loan of $20 million to help finance a tourism project.

2. The Bank has made 16 loans to Yugoslavia, totalling $475 million, but the proposed loan would be the first for tourism. Three more projects which are under consideration should lead to lending operations in FY 1971; they include another tourism project, a road project, and a multipurpose water project. The Five-Year Lending Program for Yugoslavia is attached.

Background

3. A recent Bank economic mission to Yugoslavia is now preparing its report. Its preliminary findings confirm Yugoslavia's creditworthiness for Bank lending.

The Project

4. The Babin Kuk Tourism project will establish a large integrated tourism complex at Dubrovnik on the South Adriatic Coast of Yugoslavia. The complex will provide accommodations and associated facilities for over 5,000 persons. The project was first identified during the physical planning of the South Adriatic Region, a joint exercise of the UNDP and the Government. The objective of the South Adriatic Plan is to provide for orderly development while preserving the ecological and physical characteristics that are the primary attraction for the region's main industry, tourism. The project fits well into this overall scheme.

5. There are several unique aspects to the project, to which the attention of the Loan Committee is drawn:

Size of Project

6. Because Babin Kuk is to be one of the largest tourism complexes ever built and will pioneer the application of a number of industrial management techniques to tourism, the organizational and managerial aspects have been

given particular attention. The project will be built and operated by a separate unit within the enterprise. Architects and management consultants of international competence are being chosen and will have considerable power and responsibility.

Borrower - Lending Arrangements

7. In the past all Yugoslav loans have been channeled either through the Federal Government or through the Yugoslav Investment Bank. With the move towards more decentralization in the economy, it is now possible to lend directly to enterprises. Arrangements have therefore been made with the sponsor for a direct loan with a Federal Government guarantee. The sponsor, Minceta, is involved in many activities other than tourism and has substantial expansion plans unrelated to the project; consequently the Bank has required that the loan be made to a separate project unit which will not be liable for the debts of Minceta. This unit will have contractual relationships with the sponsor to guarantee the latter's legitimate interests. The formation of such a unit will isolate the project from possible errors of judgement of the sponsor in its other lines of business and will greatly facilitate supervision. Draft agreements on the formation of this unit have been submitted and reviewed by the Bank's Legal Department and by Yugoslav lawyers retained for this purpose. As a result of these arrangements, the Government has proposed an amendment to the law on enterprises, which would limit the liability of units like the project unit. Passage of this amendment will be made a condition of effectiveness or a condition of presentation to the Executive Directors, depending on progress made by the time of negotiations.

Hotel Subsidies

8. Since completion of the appraisal report, the Bank has received new information regarding hotel subsidies. The Privedna Banka loan (see below) would now carry an interest rate of 9.5 percent, but since the loan would qualify for a federal subsidy of 5.5 percent and a republic subsidy of 1 percent, the cost to the borrower would be only 3 percent. Our loan would not qualify for these subsidies since we do not plan to channel it through a local bank, the present requirement for qualification. In addition to our preference for lending directly to the project entity and avoiding additional delays by having to make new arrangements, we consider that the project is sufficiently profitable without subsidies on our loan. Moreover, the present system of interest rate subsidies is under review and responsibility for them is expected to shift from the Federal Government to the Republics. Should the republic then wish to make subsidies available to our project we would have no objection, especially in light of the almost universal availability of tourism subsidies in the Europe/Mediterranean region.

9. On the other hand, we do not wish to ask for subsidies on our loan, as the recent economic mission has noted that, in general, capital in Yugoslavia is underpriced. Interest subsidies are but one of a number of possible

subsidies (direct and indirect) and they should not be considered in isolation. Moreover, the improvement of the capital market and a more realistic pricing of capital are major undertakings, which cannot be solved within the framework of one tourism project. While accepting the use of subsidies for this particular project, we propose to encourage the Government to review the capital market structure and to improve the criteria and mechanism for the allocation of investments.

Devaluation

10. On January 23, 1971, subsequent to the completion of the appraisal report, Yugoslavia devalued the Dinar from 12.5:$1 to 15.0:$1. A revised cost estimate reflecting the devaluation has been prepared and is attached. In the light of experience following the 1965 devaluation, the contingency allowance for local price increases has been increased from 6 percent to 8 percent a year. Since the current foreign exchange earnings of the project are expected to exceed the foreign exchange costs, the economic rate of return after devaluation is expected to increase from 11.5 percent to 12.3 percent. Profitability is similarly enhanced. These revisions will be incorporated in the revised appraisal report to be distributed to the Executive Directors.

Amount of Loan

11. The Tourism Projects Department considers a $20 million loan is justified on two grounds: first, to secure sufficient leverage with the Borrower, and second to avoid an undue burden on our co-lender Privedna Banka, Zagreb. Preliminary discussions with Privedna Banka were based on a possible Bank loan of $18 million and a contribution by Privedna Banka of Din. 320 million. Because of rapid inflation, the appraisal mission revised these estimates and projected a Din. 360 million contribution by Privedna Banka based on a proposed Bank loan of $20 million. Privedna Banka agreed to this increase with considerable difficulty. Because the contingency for local price escalation has been increased, the Privedna Banka contribution would increase to Din. 385 million, if our loan were $20 million, or to Din, 410 million with a Bank loan of $18 million. Tourism Projects Department considers that it will be sufficiently difficult for Privedna Banka to commit an additional Din. 25 million and to cover cost overruns, and that it should not be asked to commit the further Din, 25 million that would be required if the Bank loan were to be $18 million.

12. I believe, however, that $18 million is sufficient in the light of the overall lending program and the appropriate balance between sectors and republics. The Federal Government has indicated that while they would favor a larger loan to Babin Kuk, they give higher priority to an increase of the proposed loan for the Ibar Multipurpose Project which is located in the poorest region of the country and affects the most neglected sector. An increase in the amount of the loan for that project to $40 million is being considered. This, together with other planned operations, would take our FY 1971 program to about $100 million.

Local Contribution

13. The relatively small size of the sponsor and the unusual importance of banks in the Yugoslav context give the sponsor's bank, Privedna Banka, a central role in the project. In addition to lending Minceta $8 million for investment as "equity" in the project unit, Privedna Banka will be required to provide another loan of $19.4 million plus interest during construction for the project. Privedna Banka will be represented at negotiations as co-lender and also as the major local partner of the sponsor. We will ensure during negotiations that the lending arrangements between Privedna Banka and Minceta are compatible with those of the Bank. In view of the small resources of Minceta, Privedna Banka will be asked to undertake to cover possible cost overruns.

Local Cost Financing

14. The proposed loan of $18 million would cover $15.5 million, or 34 percent of project costs, plus $2.5 million of interest during construction. Since the foreign exchange component could vary between 24 and 38 percent of project costs, depending on the success of Yugoslav manufacturing and construction firms in the bidding, the loan may not be adequate to cover all the foreign exchange costs. However, Yugoslav firms have competed successfully in the past, and the foreign exchange component can be reasonably expected to be $13.8 million, or 30 percent of the total cost. It is thus probable that the Bank's loan would finance a small amount of local costs. A smaller loan would be too small to permit sufficient leverage and the required influence on project implementation and policy. Moreover, Yugoslavia's needs for external capital over the next few years are large, and it is not practicable to provide the necessary external capital by financing only imported capital goods required for high priority projects. Thus, some financing of local expenditure is necessary. In these exceptional circumstances, the Bank is justified in including some potential local expenditure in the proposed loan.

Infrastructure

15. The project will place large additional demands on infrastructure in the Dubrovnik area, particularly on roads, water supply, sewerage and the airport. Preliminary surveys of the needs have been carried out by the Bank and a program of improvement will be assured by the republic. The Bank is planning to include a loan for sewerage and water in the FY 1972 lending program, and it is possible the Government will ask us to expand this loan to cover the foreign exchange costs of the other infrastructure needs. Outside consultants will be needed to ensure that the design of the proposed sewerage system will adequately solve an already serious sewage problem. It is therefore proposed that about $150,000 of the loan be assigned for on-lending by the Borrower to the Enterprise for Sewage and Water Supply of Dubrovnik to cover the foreign exchange cost of this work.

Land Acquisition

16. Acquisition of the land is essential for the proper implementation of the project. Under the Master Plan of Dubrovnik, 92 hectares of Babin Kuk peninsula is reserved for the project. However, some of this land has yet to be acquired. About 70 hectares is presently held by the project sponsor. We recommend that the registration, in the name of the Borrower, of sufficient land to ensure the viability of the project, the exact amount to be determined during negotiation, become a condition of effectiveness (para. 8.06).

Recommendation

17. I recommend that the Bank invite the Federal Government and Minceta to send representatives to negotiate a loan of $18 million for the Babin Kuk Tourism Project substantially in accordance with Section 8 of the Appraisal Report, except as modified by the foregoing.

M. P. Benjenk
Director
Europe, Middle East and North Africa
Department

Attachments

Population: 19.9 m
GNP Per Cap: $570

IVa. YUGOSLAVIA - 5 YEAR LENDING PROGRAM

		($ millions)							
		Fiscal Year						Total	Total
		1971*	1972	1973	1974	1975	1976	1964-68	1969-73
Forestry II	IBRD			10.0					
DFC - YIB I	IBRD		20.0						
DFC II	IBRD			25.0					
DFC III	IBRD					30.0			
Industry Modern. IV	IBRD				20.0				
Power	IBRD		20.0						
Tourism I - Bernadin	IBRD	10.0							
Tourism II - Babin Kuk	IBRD	20.0							
Tourism III	IBRD		15.0						
Tourism IV	IBRD				15.0				
Roads V	IBRD	36.0							
Roads VI	IBRD			30.0					
Roads VII	IBRD				30.0				
Railways	IBRD					30.0			
Water Supply - Ibar	IBRD	34.0							
Multipurpose				25.0					
Water Supply -	IBRD								
Multipurpose II									
Unallocated I	IBRD		20.0						
Unallocated II	IBRD			10.0					
Unallocated III	IBRD				10.0				
Unallocated IV	IBRD					15.0			
	IBRD	100.0	75.0	100.0	75.0	75.0		175.5	419.5
	No.	4	4	5	4	3		5	18

P & B 8/21/70
* revised in accordance with latest timetables: EMENA 2/10/71

BABIN KUK
February 1, 1971

COST ESTIMATE
(millions)

		Dinars			US $ Equivalent			% of
		Local	Foreign	Total	Local	Foreign	Total	Project Cost
i.	Land	18.7	-	18.7	1.25	-	1.25	2.7
ii.	Construction							
	Site Development	40.3	11.1	51.4	2.69	0.74	3.43	
	Buildings	224.3	61.9	286.2	14.95	4.13	19.08	
	Professional Fees	18.0	30.0	48.0	1.20	2.00	3.20	
	Sub-Total	282.6	103.0	385.6	18.84	6.87	25.71	56.8
iii.	Equipment	21.8	48.2	70.0	1.45	3.21	4.66	10.3
iv.	Housing	6.9	2.0	8.9	0.46	0.13	0.59	1.3
v.	Staff Training and Pre-opening Expenses	4.1	1.2	5.3	0.27	0.08	0.35	0.8
vi.	Management Assistance	1.1	7.6	8.7	0.07	0.51	0.58	1.3
vii.	Project Administration	4.9	1.5	6.4	0.33	0.10	0.43	0.9
viii.	Working Capital	17.2	-	17.2	1.15	-	1.15	2.5
	Total before Contingency	357.3	163.5	520.8	23.82	10.90	34.72	
ix.	Contingency							
	Physical Increase	31.8	15.0	46.8	2.12	1.00	3.12	
	Price Increase	84.0	27.9	111.9	5.60	1.86	7.46	
	Sub-Total	115.8	42.9	158.7	7.72	2.86	10.58	23.4
TOTAL PROJECT COST		473.1	206.4	679.5	31.54	13.76	45.30	100.0
Interest and other charges during construction		21.8	42.0	63.8	1.45	2.80	4.25	
Total financial requirements		494.9	248.4	743.3	32.99	16.56	49.55	

FORM No. 60
(3-70)

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

CONFIDENTIAL

LOAN COMMITTEE

LC/A/71-3

February 12, 1971

NOTICE OF MEETING

A Meeting of the Loan Committee will be held on Wednesday, February 17, 1971 at 11:00 a.m. in the Board Room.

AGENDA

Nigeria - Rehabilitation Program Loan

The Committee will consider the attached memorandum from the Western Africa Department dated February 12, 1971, entitled "Nigeria - Rehabilitation Program Loan" (LC/O/71-18).

David Pearce
Secretary
Loan Committee

- DISTRIBUTION -

Committee:

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

CONFIDENTIAL

LC/O/71-18

LOAN COMMITTEE

February 12, 1971

Memorandum from the Western Africa Department

NIGERIA - Rehabilitation Program Loan

1. Attached is a memorandum prepared by the Western Africa Department recommending a loan of $80 million equivalent to the Government of Nigeria to assist in financing its rehabilitation program as set out in Nigeria's Second National Development Plan, 1970-74. I propose to attach this memorandum, appropriately modified, to the President's Report when circulating the loan documents to the Executive Directors for approval. I would hope that negotiations of the proposed loan could start during the week of February 22 so that the Board presentation may be made before the end of March 1971.

2. One loan, for $10 million equivalent, has been extended to Nigeria during FY1971 and this was made to the Nigerian Industrial Development Bank. The lending program for the balance of FY1971 includes an $8.6 million loan for the Western State Cocoa Project and a $25 million loan for Federal and State highways. Negotiations on the Western State Cocoa Project have recently been completed and the loan amount has now been reduced to $7.2 million to reflect a rephasing of the project agreed during negotiations. The appraisal report on the federal and state highways project is under preparation. The lending program through FY1976 is attached.

3. The project consists of an $80 million import program of capital and intermediate goods selected in general from SITC Sections 6 and 7. The import program will help to finance Nigeria's overall foreign exchange requirements for a period of approximately one year, thereby assisting government to implement priority rehabilitation and development investments included in the early part of the Second National Development Plan, 1970-74.

4. It is not our intention to attach any specific conditions to the proposed loan. Rather, we believe that a continuation of the useful discussions we have been having with the Nigerians since the end of the civil war will be a more successful method of influencing policy. Nigeria's record of economic management is encouraging, as is the governments expressed willingness to participate in a revival of the Consultative Group which is now scheduled to meet in May. At this meeting the government hopes to secure the balance of external aid needed to finance its rehabilitation program and will present to the Group a statement of the economic and financial policies it plans to follow.

Recommendation

5. I recommend that the Bank invite representatives of the Federal Republic of Nigeria to negotiate a loan of $80 million for a term of 20 years, including 5 years of grace.

Roger Chaufournier
Director

Attachments

Population: 66 m
Per Capita Income: US$ 65

NIGERIA - 5 YEAR LENDING PROGRAM

($ million)

		Fiscal Year 1971	1972	1973	1974	1975	1976	Total 1964-68	Total 1969-73
Western Cocoa I	IBRD	8.6							
Western Cocoa II	IBRD				15.0				
Agricultural Credit I	IBRD			5.0					
Agricultural Credit II	IBRD					10.0			
Tree Crops	IBRD			20.0					
Agriculture Unidentified I	IBRD					25.0			
Agriculture Unidentified II	IBRD						20.0		
Livestock I	IBRD		5.0						
Livestock II	IBRD				10.0				
Livestock III	IBRD						15.0		
DFC - NIDB II	IBRD	10.0							
DFC - NIDB III	IBRD			12.0					
DFC - NIDB IV	IBRD					12.0			
Education II	IBRD		10.0						
Education III	IBRD			25.0					
Education IV	IBRD					20.0			
Small Industries	IBRD			3.0					
Industry Unidentified I	IBRD				10.0				
Industry Unidentified II	IBRD						10.0		
Power IV	IBRD		35.0						
Power V	IBRD				25.0				
Rehabilitation Program Loan	IBRD	80.0							
Railways II	IBRD				40.0				
Ports II	IBRD			15.0					
Roads V - Federal & State	IBRD	25.0							
Roads VI	IBRD		20.0						
Roads VII	IBRD			20.0					
Roads Unidentified VIII	IBRD					25.0			
Roads Unidentified IX	IBRD						30.0		
Airports	IBRD					5.0			
Unallocated	IBRD						25.0		
	IBRD	123.6	70.0	100.0	100.0	97.0	100.0	144.0	349.7
	IDA							35.5	
	Total	123.6	70.0	100.0	100.0	97.0	100.0	179.5	349.7
	No.	4	4	7	5	6	5	6	19

NIGERIA

MEMORANDUM ON A PROPOSED
REHABILITATION PROGRAM LOAN

I. INTRODUCTION

1. The Government of the Federal Republic of Nigeria has asked the Bank's assistance to finance a portion of its post-war rehabilitation needs as outlined in Nigeria's Second National Development Plan -- 1970-74 (the Plan). If Nigeria is to realize the reasonable growth and recovery targets it has set for itself over the first two years of the Plan, a resource gap of some $200 million -- above and beyond that for which external public financing is assured -- will have to be bridged. This gap can best be covered by external lenders' providing additional resources through program financing of a broad range of capital-goods imports. A transfer of resources of this order of magnitude during a period of two years can be achieved only if aid is made in a form which permits rapid disbursement.

2. A Bank program loan of $80 million equivalent to the Federal Republic of Nigeria is proposed to assist in financing Nigeria's capital and intermediate goods imports during a period of approximately 12 to 18 months. The Government of Nigeria has approached bilateral donors to provide the balance of the country's additional foreign exchange requirements during the first two years of the Plan. A meeting of the Consultative Group for Nigeria is being scheduled for May 1971 to determine how these needs can best be met by the bilateral donors in concert with the Bank.

3. The choice of specific items within the capital goods category to be financed by the proposed Bank loan would remain flexible. The eligible categories have been defined broadly and agreed with the Government in order to permit quick disbursement of the proposed loan. Nigeria's projected import bill for capital equipment over the next two years is sufficiently large to permit disbursement of all external aid expected in the given period. The balance between consumer, intermediate and capital goods imports in the past year has been reasonable and the import policy of the Government suggests that it is likely to remain so in the coming years.

4. The Bank's dialogue with Nigeria which has culminated in the present proposal for program lending was initiated shortly after the end of the civil war in January 1970. Last April/May a Bank economic mission visited Nigeria and in September a Nigerian delegation came to Washington to discuss the Plan which was then under preparation. This memorandum is based on the economic work which has been carried out by Bank staff during the past year and on the findings of a mission composed of representatives of the Western Africa and Controller's Departments which visited Nigeria from January 11 - 22, 1971. The Bank's Resident Mission in Lagos has also contributed to the preparation of this memorandum.

II. THE ECONOMY

5. An economic report, "The Current Economic Position and Prospects of Nigeria" (AW-22a dated January 21, 1971) provides a detailed description of the current Nigerian economic situation, an evaluation of the Plan and an assessment of the country's near-term aid requirements.

6. A year after the surrender of the secessionists the chief legacies of the civil war facing the Nigerian economy are the need to restore vital infrastructure facilities and the scarcity of resources to finance rehabilitation and other development expenditures. Outside the eastern states -- the area directly affected by hostilities -- the economy appears to have been little affected by the war: agricultural production was well maintained and industrial output, spurred by the adoption of war-time controls, actually expanded. There was, however, serious damage to the country's infrastructure, patricularly in transport, reflecting overuse and deferred maintenance of plant and equipment. Moreover, public and private investment (except in certain manufacturing lines) was severely curtailed during the war and the country's administrative structure suffered from the break-up of the four former regions into twelve states and the withdrawal of large numbers of trained civil servants from positions in the Federal Government and in the public authorities.

7. The current situation is marked by continuing inflationary pressures, a substantial backlog of payments due abroad on account of imports and deferred profit remittances, the prospect of a substantial decline in traditional exports this year because of poor weather conditions and mounting unemployment, particularly in urban areas. On the other hand, petroleum production has recovered rapidly since the end of the war and this promises to be a major source of expanding foreign exchange and public revenues during the next few years.

8. Nigeria's Plan -- covering the period April 1, 1970 to March 31, 1974 but announced only in November 1970 -- anticipates that the rate of growth of real GDP will rise from less than 5 percent in 1971 to 9 percent in 1974. Petroleum production and manufacturing are expected to be

the major growth sectors, while agricultural output, still the mainstay of the economy, is projected to rise only 2.4 percent per annum, or at about the same rate as population. Total planned investments of $4.5 billion represent about 20 percent of GDP, almost evenly divided between the public and private sectors. The government expects that nearly half of the anticipated private investment will come from abroad and much of this will be concentrated in the petroleum industry. Government investment, on the other hand, is to be financed primarily (70 percent) from public savings. Projected public capital inflows, during the Plan period are, however, equivalent to nearly 20 percent of public planned investment.

9. The emphasis in the first two years of the Plan period is largely upon reconstruction and rehabilitation with a view to restoring the country's productive capacity and overcoming losses and damage suffered during the war. Roughly $840 million or three-fourths of planned public capital expenditures during 1970/71 - 1971/72 are for rehabilitation with an estimated foreign exchange component of about $335 million. The strategy underlying the Plan is sound, but shortage of foreign exchange, the scarcity of trained manpower and past delays in preparing projects could limit the government's ability fully to implement the Plan, especially at the State level and during the first two years when public investment is scheduled to be particularly high.

III. SIZE AND FINANCING OF THE RESOURCE GAP

10. During the first two years of the Plan a continuing shortage of foreign exchange may well be the most critical factor affecting the Nigerian economy and this will almost certainly impose restraints on the level of investment and the volume of imports, particularly of consumer items. Nigeria's reserves are currently equivalent to less than two months' imports. Short-term liabilities to the private sector representing approved applications for foreign exchange, primarily on account of merchandise imports, amount to £N85 million ($240 million) and have risen sharply in recent months.

11. The Bank estimates Nigeria's foreign exchange gap,net of anticipated private capital inflow and allowing for some slippage in the planned level of investment, to be of the order of $350 million during the two year period 1970/71 - 1971/72. Of this amount some $150 million may be expected to be covered by disbursements from existing commitments of Bank/IDA and bilateral donors. The remaining gap of $200 million must be financed by new commitments which of necessity should be of a quick disbursing nature if the country's rehabilitation needs are to be met. Since Nigeria's foreign exchange reserves are and have been for some time at the minimum level considered acceptable by the authorities, any shortfall in the realization of these additional aid flows is likely to result in some further accumulation of short-term commercial liabilities and/or

a further curtailment of imports. A reduction of imports below the levels envisaged in the Bank's projection would retard the recovery of the Nigerian economy and slow down the program for rehabilitating the country's infrastructure. Tighter import controls on consumer goods would add to existing inflationary pressures, while restrictions on imports of capital and intermediate goods would make realization of investment and production targets that much more difficult. Table 1 provides mission estimates of Nigeria's balance of payments position over the next two years.

Table 1: ESTIMATED BALANCE OF PAYMENTS, 1970/71 AND 1971/72

	1970/71	1971/72
	(£N million)	
Non-petroleum trade		
Exports (f.o.b.)	180	214
Imports (c.i.f.)	-305	-360
Services and factor payments (net)	-100	-110
Net foreign exchange receipts from petroleum	157	228
Unrequited Transfers	8	6
Current balance	- 60	- 22
Financial movements		
Private capital (non-oil)	10	15
Short-term liabilities	-	- 15
Debt servicing[1/]	- 24	- 22
Reserve replenishment	- 2	- 3
Other official obligations	- 1	- 2
Capital Account Balance	- 17	- 27
Foreign Exchange Gap	- 77	- 49
of which		
Disbursements from existing commitments	27	28
Uncovered gap (£N million)	50	21
($ million)	(140)	(59)

1/ On debt outstanding December 31, 1969

Sources: Bank estimates (revised by January 1971 mission)

12. These estimates of disbursements from Bank/IDA and bilateral loans are set forth in Table 2 below. The estimates are based on data provided by a number of bilateral donors, (UK, US, Japan, Canada, Netherlands) and on discussions in Lagos between the January 1971 mission, the Nigerian Government and representatives of donor countries. In addition to the estimated $150 million that is likely to be disbursed against existing commitments, a substantial amount of bilateral assistance is under discussion between various donors and the Nigerian Government. Aid offers in this category, however, do not yet represent firm commitments and are, in any event, inadequate to meet the balance of Nigeria's anticipated needs.

Table 2: ESTIMATED DISBURSEMENTS FROM EXISTING AID COMMITMENTS, EXCLUDING TECHNICAL ASSISTANCE, 1970 - 1972
($ millions)

Country	1970/71	1971/72	Total
U.K.	16.8	6.8	23.5
U.S.	9.7	10.4	20.1
Germany	4.2	10.4	14.6
Japan	5.0	9.0	14.0
Canada	5.6	3.0	8.6
Netherlands	0.3	0.2	0.5
Others	1.9	4.2	6.1
Bilateral sub-total	43.5	43.9	87.4
Bank/IDA	27.6	32.1	59.7
Total	71.1	76.0	147.1

Note: The figures above relate to donors' fiscal years and hence cannot be related to Nigeria's estimated 1970/71 and 1971/72 requirements. However, they provide a reasonably close approximation of probable disbursements available towards covering the deficits indicated in Table 1.

13. Of the $200 million in disbursements to be met from new commitments over the next eighteen months, it is proposed that the Bank provide approximately $80 million in the form of a rehabilitation program loan plus small amounts in disbursements from new project loans now under preparation. This would leave a balance of nearly $120 million to be covered by bilateral donors and other international agencies. A substantial portion of this latter amount is already in sight. Table 3 summarizes available information regarding probable disbursements from existing commitments and the proposed distribution of additional assistance from the Bank and other donors.

Table 3: DISBURSEMENTS FY1971 AND 1972 ($ millions)

	From existing commitments	Additional Requirements	Total
Bilateral and other multilateral lenders and supplier credits	90	115	205
IBRD	60	85 1/	145
Total	150	200	350

1/ Includes $5 million from new project commitments.

14. The need for quick-disbursing aid arises from the coincidence over the next two years of (a) substantial rehabilitation needs in addition to the usual requirements of development; and (b) a reduced pipeline of project-related commitments because of a lack of project preparation in recent years due to the civil war. Only program aid will permit the immediate increase in imports required for the economy to return to a more normal level of activity and help to finance the higher level of investment necessary during rehabilitation. Such quick-disbursing aid will help to assure the necessary flow of external assistance over a relatively short period while foreign exchange earnings and public savings increase. In seeking such help, Nigeria's case is strengthened by its already substantial savings effort and the prospect of a rapid growth of oil revenues.

14a. Hitherto, except in connection with its recent quota increase, Nigeria has not made use of the resources of the IMF. The country's position has been that it must strengthen its reserves and reduce its short-term indebtedness, while husbanding its IMF drawing rights and $31 million SDR holdings as a contingency reserve to be used in the event of a possible unforeseen, short-term crisis. Nigeria could easily qualify for a drawing through the first credit-tranche of $45 million and could go beyond this under appropriate conditions. These resources, together with its SDR's are, however, quite limited in relation to its very large payments backlog. Thus the country's net short-term financial position would remain precarious. Therefore, it is reasonable for Nigeria to seek as much long-term assistance as possible to meet its massive reconstruction needs. Against this background and in view of Nigeria's projected continuing foreign exchange gap, use of Fund resources now would be no substitute for the type of long-term assistance proposed by the Bank.

15. The need for program lending should be confined to the first two years of the Plan period pending the build-up of project-related disbursements. During the latter two years of the Plan, the Bank may be able to disburse a further $80 million against current and proposed project loans. Concurrently with the implementation of the rehabilitation program, new project preparation must be accelerated. The Nigerian Government is giving particular priority to this activity. Recently, teams of foreign consultants and advisers have been recruited on a long-term basis to assist the Nigerian Railroad Corporation in improving its management and to help establish a Transportation Planning Unit within the Ministry of Transport. Foreign advisers have been employed to advise the government regarding the proposed merger of the Niger Dams Authority and the Electricity

Corporation of Nigeria. The Nigerian Government has also agreed that the Bank schedule sector missions in education, agriculture and transport to visit Nigeria during the next few months to identify projects for future financing. These current efforts will help to provide better project selection, preparation and implementation in the years ahead.

16. In addition, there is already a need for closer coordination of aid -- both with respect to meeting Nigeria's short-run rehabilitation requirements and to preparing development projects for future external financing. Nigeria's needs will be discussed at a meeting of the Consultative Group which the Bank proposes to call in May 1971. It is expected that this meeting will provide an opportunity to assess Nigeria's situation as of the start of its second post-war year and also provide background for decisions on bilateral aid to Nigeria for the balance of the current Plan period. The Nigerian Government has agreed to present a statement to the Consultative Group on how it intends to handle the pressing problems confronting the economy. The Bank's approach to the economic policy problems in question is outlined in paragraphs 43-49 below.

IV. THE PROJECT

17. Prompt transfer of additional resources is the essence of any operation undertaken at this time to assist Nigeria in the rehabilitation of its economy. Normal project lending clearly does not meet the test, since even were the Bank prepared to provide 100 percent of project costs it would not be possible to identify, appraise and prepare an adequate number of short-term investments against which to disburse $80 million over the next 12 to 18 months. A rehabilitation program loan to Nigeria could, therefore, take one of two forms (or some combination thereof); financing a portion of the country's immediate reconstruction investment plan on a sector basis or the financing of essential imports. It would not be practicable to disburse $80 million rapidly against sector programs as this would require financing a host of minor rehabilitation projects being undertaken by the Federal and State Governments and the several statutory authorities. This, in turn, would impose a great administrative burden upon the Bank and the Nigerian authorities; it would be almost impossible to supervise and would create problems of coordination and duplication vis-a-vis other donors. Therefore, Bank financing of a capital goods import program would be the most practicable approach in support of Nigeria's rehabilitation program.

18. The proposed project consists of an $80 million import program of capital and intermediate goods selected, in general from SITC[1/] Sections 6 and 7. The import program is designed to assist in financing Nigeria's overall foreign exchange requirements during the period January 1, 1971 through June 30, 1972, thereby helping government to implement priority rehabilitation and development investments included in the first two years of the Plan.

1/ Standard International Trade Classification.

19. The Bank would disburse against imports of capital and intermediate goods described in Annex 1. These items, which include nearly all machinery and transport equipment, and most intermediate products used in agriculture,manufacturing and construction have been chosen bearing in mind the following considerations:

a) To associate Bank disbursement with imports of goods destined directly to rehabilitation and development investment in the public and private sectors;

b) To support Government's policy of encouraging such imports while controlling total foreign exchange expenditures by limiting consumer goods' imports; and

c) To include sufficient imports to permit a resource transfer of \$80 million for approved expenditure during a disbursement period of 12 to 18 months.

20. During the first nine months of 1970, the eligible items accounted for imports worth approximately £N110 million, or \$300 million (Annex 2). During the disbursement period these items may well account for between \$700 million and \$800 million. While this is inevitably a very approximate figure it is certainly much larger than the overall program assistance requirements of \$200 million.

Import Requirements

21. Data on the composition and origin of Nigeria's imports since 1965 are shown in Tables 4 and 5. Up to 1965, imports were rising rapidly, but during the war government restrained imports through increasingly stringent licensing and by raising import duties on consumer goods. Towards the end of the war, even raw materials came under direct import controls. Imports of capital goods shrank as a result of declining private and public investment.

22. The past year, however, witnessed a rapid recovery of imports. In April 1970, imports of a number of commodities, mainly machinery, spare parts and agricultural equipment were put under open general license. Since then, cement has also been placed on open general license. During the first nine months of 1970, total imports were 30 percent, and imports of machinery and transport equipment 80 percent, above the corresponding period in 1969.

23. The 1970 data probably do not yet reflect normal post-war import demand. For many items of capital equipment, investment decisions taken even immediately after the end of the war are not yet reflected in import statistics because of the time required to prepare specifications, place orders and obtain delivery. Thus, during the first nine months of 1970, there were heavy imports of commercial vehicles (24 percent of total

imports of machinery and transport equipment), construction equipment (10 percent), but relatively few imports of railway vehicles (0.6 percent) and agricultural machinery (2 percent).1/ As the economy recovers from the war and investment increases, one can expect the demand for machinery and transport equipment and for intermediate goods to continue to grow as public and private investment decisions are gradually implemented.

Table 4: NIGERIA - COMPOSITION OF IMPORTS, 1965-70
(£N millions)

SITC Commodity Section		1965	1966	1967	1968	1969	Jan-Sept 1970
0.	Food and Live Animals	23.0	25.8	21.3	14.2	20.9	22.2
1.	Beverages and Tobacco	2.1	2.3	1.8	1.2	0.8	1.2
2.	Crude materials mainly inedible, other than fuels	6.6	7.2	5.8	5.3	5.7	5.9
3.	Mineral Fuels, Lubricants and related materials	17.3	3.8	8.8	14.6	15.6	9.5
4.	Animal and Vegetable Oils and Fats	0.2	0.2	0.3	0.3	0.2	0.3
5.	Chemicals	20.2	20.8	21.3	22.4	30.4	30.2
6.	Manufactured Goods classified by material	90.0	79.3	72.3	54.7	72.0	76.2
7.	Machinery and Transport Equipment	92.4	95.5	71.6	60.5	73.2	95.1
8.	Miscellaneous Manufactured Articles	20.5	18.8	17.4	14.0	13.4	13.5
9.	Other Commodities and Transactions, nes	3.0	2.8	3.0	6.1	16.4	5.7
	Total	275.3	256.4	223.6	193.2	248.7	261.2

Sources: 1. Second National Development Plan 1970-74, p.24, Table 5.
2. Ministry of Finance

1/ Cf. Annex 2 for details of machinery and transport equipment imports.

Table 5: NIGERIA - ORIGIN OF IMPORTS, 1965 - 1970 1/

Country of Origin	In millions N£						In percentage of total					
	1965	1966	1967	1968	1969	1970 1/	1965	1966	1967	1968	1969	1970 1/
EEC Countries	68.2	67.8	57.5	53.3	62.7	68.6	24.8	26.4	25.7	27.6	25.2	26.3
United Kingdom	85.1	76.3	64.6	59.9	86.3	79.8	30.1	29.8	28.9	31.0	34.7	30.6
United States	33.1	41.5	27.9	22.3	29.3	40.1	12.0	16.2	12.5	11.5	11.8	15.4
Japan	25.6	14.3	18.8	7.2	9.4	15.6	9.3	5.6	8.4	3.7	3.8	6.0
All other countries	63.3	56.5	54.8	49.9	61.0	57.1	23.8	22.1	24.5	26.2	24.5	21.9
Total	275.3	256.4	223.6	192.6	248.7	261.2	100.0	100.0	100.0	100.0	100.0	100.0

1/ 1970, January - September

Sources: 1) Review of External Trade, Nigeria 1969, table 14.
2) Ministry of Finance.

January 28, 1971

The Plan's projections of imports are shown in Table 6. Total imports during the April-September 1970 period were slightly above the rate anticipated in the Plan.

Table 6: NIGERIA - PLAN PROJECTIONS OF IMPORTS, 1970/71-1973/74

Commodity	1970-71	1971-72	1972-73	1973-74	Total
Value (£N)					
Capital Goods	125.0	143.8	169.7	205.3	643.8
Intermediate Goods	90.0	97.2	106.9	119.7	413.8
Consumer Goods	115.0	121.9	131.6	144.7	513.2
Total	330.0	362.9	408.2	469.7	1,570.8
Percentage Distribution					
Capital Goods	37.9	39.6	41.7	43.8	41.0
Intermediate Goods	27.3	26.9	26.1	25.4	26.3
Consumer Goods	34.8	33.5	32.2	30.8	32.7
Total	100.0	100.0	100.0	100.0	100.0

24. Nigeria does not distinguish (or publish separately) in its import statistics those items imported by or for the public sector. Even were there adequate records of direct public sector imports, this would be of only limited analytical use, since a significant proportion of imports destined for use or consumption in the public sector are imported through private channels. The Ministry of Economic Development provided the mission with estimates of the value of the capital goods imported by the government and the Federal statutory corporations during the first eight or nine months of 1970. Government's direct imports of capital goods in the January - September period were reported by this Ministry at £N4.3 million ($11.9 million) and those of the Federal statutory corporations in the January - August period were given as £N1.5 million ($4.1 million). Another partial indicator of direct public sector procurement from abroad was provided by the Lagos representative of the Crown Agents who informed the mission that the value of orders they had placed for non-military goods on behalf of all public authorities in Nigeria during 1970 amounted to £N7.1 million ($19.9 million). The Crown Agents further estimated that their purchases for Nigeria during the first half of 1971 would amount to £N4 million ($11 million). In addition, further commitments of £N1 million ($2.8 million) would be settled if funds were made available, and another £N2 million ($5.6 million) in indents could be processed were the States granted the foreign exchange allocations they have requested.

25. These measures are, at best, simply indicative of the order of magnitude of direct public sector imports last year. They cover only the immediate post-war months -- a period during which actual deliveries of investment goods to the public sector were presumably still depressed because of the slowdown in development during the war. It is interesting to note, however, that Crown Agents purchases on behalf of Nigeria rose sharply at the end of last year and are projected to run well above 1970 levels this year. Although these figures are almost certainly incomplete as a measure of public sector capital goods imports, they do suggest that such imports alone are not likely to be large enough to absorb anywhere near the full amount of the proposed program loan if this is to be disbursed over a period of eighteen months.

26. The January 1971 mission and the Government agreed that it would not be feasible to project probable direct public sector imports during the disbursement period. Therefore, rather than request that a specific portion of the loan be allocated to the public sector, government has agreed to the disbursement of the loan proceeds against both public and private sector imports on a "first come first serve" basis,[1/] thereby ensuring prompt disbursement of the full loan and providing an incentive to public sector entities to implement priority programs quickly.

27. As may be observed from Annex 2, imports of selected investment items falling within only SITC Section 6 (Manufactured Goods Classified by Materials) and SITC Section 7 (Machinery and Transport Equipment) averaged £N37 million (more than $100 million) per quarter during the first nine months of 1970 and are expected to rise substantially during the next two years as public and private investments revive. Virtually, all these imports of SITC 6 and 7 items originated in Bank member countries.

28. It is proposed that disbursement be made only in respect of expenditures incurred after the date of the loan agreement. However, in view of the present backlog of foreign exchange applications on account of private-sector merchandise imports, this may entail some disbursements against qualifying imports which reached Nigeria as early as December 1970.

29. During the proposed disbursement period, the main items of public sector imports are expected to include transformers and conductors for rehabilitation and extension of the electric power system, equipment for telecommunications development, railway locomotives, rolling stock, track and materials, port handling equipment and craft, road maintenance

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1/ See section on procurement for details.

equipment, farm machinery, water supply materials and educational equipment. However, since existing external financing commitments are to a large extent tied to procurement of imports by the Federal Government and statutory corporations, the scope for public sector disbursement from the program loan may be quite limited. Depending very largely on how quickly the loan can be utilized in connection with private imports and how rapidly public imports develop, the mission estimates that between one-third and one-half of the loan may be disbursed against imports for the public sector.

30. The Bank has agreed with the government on procurement procedures described in paragraphs 31-35. It should be noted that while full international competitive bidding is not a condition of the proposed program loan, the structure of imports by country of origin shows well-diversified sources of supply. Table 5 summarizes imports by origin for recent years, and Annex 2 presents more detailed information in this respect for specific categories of capital and intermediate goods.

Procurement

31. Public sector procurement in Nigeria is handled in a number of different ways. The Federal Government, the State Governments and the Statutory Corporations all have their own tendering procedures. The majority of the contracts awarded by the Federal Government are for construction; therefore a review of the Federal Tenders Board has not been made. The same could probably be said for each of the State Tenders Boards. Because of this, and in view of the number involved, no attempt has been made to review them either.

32. The Statutory Corporations are the entities that account for the bulk of public sector capital-goods purchases. Their procedures permit purchases up to £N5,000 ($14,000) without reference to the Corporations Standing Tenders Board (CSTB). However, for purchases over £N5,000, a notice must be placed in all local newspapers and in the Federal Republic of Nigeria Official Gazette; copies of the notice are distributed to all members of the Tenders Board representing the State Governments. In addition, when large contracts are involved the Corporation purchasing the goods will arrange additional advertising. After bids have been received by the CSTB, the purchasing Corporation evaluates the bids and forwards its recommendations to the Tenders Board for its review and approval of an award. Approval of awards for contracts over £N50,000 ($140,000) are made by the Federal Executive Council; however, the Tenders Board plays the same role in reviewing these contracts as it does in those up to £N50,000.

33. One other form of purchasing that is common in Nigeria is the use of purchasing agents. The purchasing agents are sometimes instructed which goods to purchase and, in this event, there would normally not be any competitive bidding, unless this had been carried out prior to giving

the purchasing agent instructions to place a particular order. However, the purchasing agent is often requested to obtain goods at the best available price and under these circumstances the practice is to employ competitive bidding to accomplish this. This bidding may not be as extensive as Bank procedures, but purchasing agents are usually in a position to obtain competitive prices.

34. Therefore, orders for direct imports over £N5,000 ($14,000) that have been placed through the CSTB and orders for direct imports that have been competitively bid by the purchasing agents have reasonable procedures for procurement and would be eligible for financing from the proposed loan. Lists of orders placed in the above manner will be required monthly and the purchasing agents to be retained will be approved by the government and the Bank.

35. With respect to the private sector, the international marketplace and normal commercial practices should assure reasonably broadbased competitive procurement. A review of Nigeria's 1970 foreign trade statistics indicates that the types of items which will be covered under the Bank loan currently originate in a wide range of countries.

Disbursement

36. All disbursements will be on a reimbursement basis and will cover the CIF cost of qualifying imports.

37. For goods purchased by the Statutory Corporations and the purchasing agents, the Bank's normal documentation requirements can be met. The Ministry of Finance will be responsible for gathering the invoices, evidence of shipment and evidence that the supplier has received payment. Such evidence will be forwarded to the Bank in support of each withdrawal application. Orders for which claims are being submitted would appear on the lists of orders forwarded to the Bank each month. These lists of orders will include information to be provided by the Ministry of Finance regarding any particular source of finance if applicable. This will permit the Bank to confine its financing to orders which have not been assigned to another donor, thus avoiding duplicate financing.

38. Goods procured through commercial channels are subject to foreign exchange control. Normally, no application for foreign exchange will be entertained until the goods have been landed and cleared through customs. At this point, a bill of entry replaces the bill of lading. The bill of entry is evidence that the goods have arrived and includes the name of the ship. The commercial bank completes a foreign exchange application and forwards this with the invoice and bill of entry to the Central Bank.

39. Because of Nigeria's shortage of foreign exchange there currently exists a substantial backlog or pipeline of foreign exchange applications. As of mid-January applications totalling £N85 million ($238 million) -- equivalent to the value between two and three months' imports -- had been approved and were being held by the Central Bank. All private-sector applications for foreign exchange to cover commodity imports and permitted service and remittance payments are classified in one of four priority categories.[1] Twice weekly the Central Bank makes an allocation of foreign exchange to each of the 12 banks and licensed exchange dealers in Nigeria. The total amount of this allocation depends upon the availability of foreign exchange at the moment -- after allowing for anticipated government claims, statutory reserve (currency backing) requirements, etc. During the nine months April - December 1970, it is estimated that approximately £N211 million ($592 million) was released to the Banks. Monthly allocations averaged £N24 million ($67 million) and ranged from a low of £N20 million ($56 million) in June to a high of £N28 million ($78 million) in September. According to the Central Bank, the semi-weekly allotment of foreign exchange to the commercial banks is divided in proportion to each bank's share of approved applications then in the pipeline. The Banks, in turn, are obligated to use the foreign exchange they receive to discharge obligations falling in Category A first. The balance of their allotments is divided among pending claims in Categories B (60 percent), C (25 percent) and D (15 percent). The banks are expected to remit foreign exchange in strict order of the date upon which applications were approved within each category. In mid-January exchange applications in the B, C and D categories were experiencing a delay of approximately 120 days, 130 days and 160 days, respectively, from their date of approval (acceptance) by the Central Bank. When the Central Bank allots foreign exchange to the commercial banks it is up to the latter to make payments to suppliers abroad. The Central Bank itself apparently does not maintain any record of which particular suppliers have been paid, relying on the commercial banks to do this and to treat all applicants for exchange on a first-come first-served basis.

40. Therefore, it is not possible to locate at one point all the documents required by the Bank prior to approval of a reimbursement request for private-sector imports. The Central Bank holds the application for foreign exchange, the invoice and the bill of entry, but only the commercial bank knows precisely which suppliers have been paid and on what date.

41. During negotiations an agreement should be reached providing for the commercial banks to issue to the Ministry of Finance each week a certificate confirming that all applications for foreign exchange submitted to the Central Bank through a certain date have been settled with the suppliers. The Ministry of Finance would then be responsible for obtaining, for eligible goods, copies of the application for foreign exchange, the invoice and bill of entry from the Central Bank. These documents together with a copy of the commercial bank's certificate would be used to support the withdrawal application to the Bank. To avoid many small requests, it is recommended that only payments in excess of a figure to be agreed between the Government and the Bank be included in the claims.

1/ See Annex 3 for a description of these categories.

Supervision

42. Disbursement procedures themselves will assure that Bank funds are used only to finance qualifying capital and intermediate-goods imports. It is our intention to finance only commodities of a clearly investment nature. Since it is anticipated that a substantial portion of the Bank loan will finance private sector imports and since many of these may be in the form of homogenous commodities such as steel sheets, shapes and rods, electrical equipment, spare parts, vehicles, agricultural machinery, etc., it would often be virtually impossible to trace the final user of individual items passing through several hands in the import and distribution network. However, the commodities selected for inclusion in the Bank's list of qualifying imports are such as to assure their essentiality to the economy and their high priority in the country's rehabilitation program.

V. ECONOMIC POLICY ISSUES

43. The January 1971 mission raised with the government a number of issues relating to economic policy and Plan implementation. In view of the brief duration of the mission and the fact that there has recently been a reshuffle of permanent secretaries among several of the economic ministries leading to a general review of financial and economic policies in Nigeria, it was not possible to pursue these matters at any length. The mission indicated that the Bank would revert to them at the time of negotiations. The mission also urged the government to prepare a statement on these topics for presentation to the Consultative Group in the Spring.

44. The main issues in regard to Nigeria's economic policies and Plan financing and implementation are the adequacy of the country's foreign exchange receipts, its import program, plans for reducing the payment backlog, the maintenance of a reasonably balanced domestic financing plan and the steps being taken to improve sector planning and project preparation. Shortage of foreign exchange is currently imposing a restraint upon the initiation of new projects. In view of the low level of Nigeria's reserves, greater resort to domestic borrowing cannot be a substitute for increased aid and would be self defeating. As it is, even the volume of deficit financing explicitly anticipated during the first two years of the Plan is likely to intensify existing inflationary pressures. However, to the extent that external lenders provide additional aid, resort to domestic borrowing should be lessened. Since the Bank is taking the lead in providing substantial program assistance, the government feels that at the Consultative Group meeting it will be able to persuade other donors to provide the additional aid needed.

45. The Bank has stressed to the Nigerians the importance of their presenting to the Consultative Group firm current estimates of their prospective public savings, investment and domestic borrowing this year and over the near term. In the meantime -- particularly during the forthcoming negotiations -- the Bank shall maintain a dialogue with the Nigerians on their progress in implementing the Plan, the probable slippage in planned or anticipated investment and efforts being made to improve development administration particularly with respect to project preparation and implementation.

46. The Nigerians have indicated that they intend to prepare a foreign exchange budget, although at present no such instrument exists in Lagos. The mission strongly encouraged the government in this respect and indicated that the Bank would be most interested in the results of a foreign exchange budget exercise. In particular, the Bank is interested in the steps being taken to keep the growth of imports in line with expected exchange receipts; the criteria employed in granting specific import licences; and the nature of the coordination which exists between the import licensing authorities and those responsible for the allocation of foreign exchange to the private sector.

47. Finally, the mission told the Nigerians that at the time of negotiations the Bank would like the government to indicate its plans for reducing or liquidating the backlog of short-term liabilities which have been built up during and since the war with respect to commercial imports and various service and remittance payments. It is important for the government to come to grips with the backlog problem and announce a realistic program for the discharge of its liabilities.

48. During negotiations of the proposed program loan the Nigerian Government's views and intentions regarding these issues would be sought. It is not proposed that the adoption or implementation of any particular policy prescription be made a condition of the program loan but the dialogue with Nigeria on economic policies and Plan implementation will be continued. The Nigerians' ability, first, to secure additional program assistance from bilateral donors in the context of the Consultative Group and, later, their success in attracting project aid may well depend in large part upon a demonstration on their part that they recognize the importance of these issues and are taking steps to correct them.

49. The Bank has been in close touch with the Nigerian economic scene since before the end of the civil war and, as indicated earlier, has maintained a continuous discussion with the government on economic policy issues during the past year. This dialogue has been useful and it is hoped that it will become more so as the situation improves and as the attention of the Nigerian authorities shifts from the pressing concerns associated with immediate post-war relief and rehabilitation to longer-term issues of development. It is, in part, because the Nigerians have demonstrated an ability to adopt and carry out sound policies

and because it is expected that the full and constructive exchange of views will be continued that it is recommended that the Bank deliberately refrain from suggesting any specific policy conditions being attached to the proposed loan. It is hoped that the dialogue now existing between the Bank and Nigeria can be broadened to include other donors and the IMF at the time of the Consultative Group meeting this Spring.

50. The Nigerian Government is aware that its presentation to the Group will be important in shaping the attitudes of potential bilateral donors toward the country. It appreciates the critical issues which will be of concern to donor countries participating in the Consultative Group. Having agreed to a revival of the Consultative Group and to attend a meeting in May, the Nigerians have indicated a willingness to subject themselves to the scrutiny of aid donors. This is an important demonstration of the Nigerians' confidence in their ability to handle the problems now confronting the country.

VI. CONCLUSIONS AND RECOMMENDATIONS

51. The strategy outlined in Nigeria's Plan is sound. It calls for returning the economy to normalcy during the two years following cessation of the civil war, thus paving the way for future development. The rehabilitation program is well designed to meet these goals and the Nigerian Government has demonstrated its capacity to undertake sound economic and financial policies. Taking into account a possible slippage in the planned expenditures for rehabilitation, the Bank estimates that external aid of the order of magnitude of about $200 million is needed on a quick disbursing basis to finance the rehabilitation program in the next 12 - 18 months. A number of bilateral donors have indicated their interest in providing program assistance to meet a part of Nigeria's rehabilitation financing needs. A Consultative Group for Nigeria, a meeting of which is planned for May 1971, would provide the necessary coordination of the proposed external aid and would enable the Bank and bilateral donors to follow the realization of Nigeria's rehabilitation program. A Bank program loan of US$80 million equivalent for a term of 20 years, including a grace period of 5 years, is recommended as the Bank's contribution towards meeting a part of Nigeria's rehabilitation needs.

Western Africa Department
February 9, 1971

ANNEX 1

DESCRIPTION OF PROJECT

Imports of Capital and Intermediate Goods and Component Parts thereof

Machinery and equipment for manufacturing industries
Agricultural machinery and equipment
Machinery and equipment for building and construction industries
Machinery and equipment for production and distribution of electricity; Electric power machinery
Telecommunications apparatus
Railway vehicles, track and equipment
Commercial vehicles and dual purpose vehicles
Ships and boats
Building and construction materials
Chemicals and fertilizers for agriculture
Non-ferrous base metals
Intermediate iron and steel products
Metal manufactures for use in industry

ANNEX 2

IMPORTS OF SELECTED CAPITAL GOODS BY COUNTRIES OF ORIGIN
JANUARY - SEPTEMBER 1970
(£N thousands)

SITC No.	Commodity Group	U.K.	E.E.C. countries	Other Europe	U.S.	Other America 2/	Japan	Other Asia	Other Countries	Total
67	Iron and Steel	4815	8521	2433	4315	29	4300	60	45	24518
68	Non-Ferrous Metals	769	730	594	70	18	9	6	156	2353
711	Power Machinery	1012	610	175	985	100	27	3	8	2920
712	Agricultural Machinery	1036	274	38	560	8	1	9	48	1974
714	Office Machinery	460	166	126	62	2	7	3	-	826
715	Metal Machinery	146	156	43	65	-	12	36	17	475
717	Textile and Leather Machinery	2168	1447	428	448	5	4269	342	74	9181
718	Machinery for Special Industries (including construction machinery)	2630	2069	224	6458	92	9	65	607	12154
719	Machinery Appliances (non electrical)	4670	3135	371	4838	14	1023	400	25	14476
722	Electrical Power Machinery (switch gear)	1708	683	254	848	10	93	23	2	3621
723	Equipment for Distributing Electricity	1615	195	59	52	61	18	-	7	2007
724	Telecommunications Apparatus	3576	910	43	1529	828	673	90	76	7725
729	Electrical Appliances	2344	736	141	314	2	251	150	10	3948
731	Railway Vehicles	374	47	neg	142	-	-	7	-	570
732 1/	Commercial Vehicles	8854	9904	2233	807	7	812	380	88	23085
735	Ships and Boats	186	375	1	1397	-	-	-	7	1965
	Total	36363	29958	7163	22890	1176	11504	1574	1170	111798

1/ Only sub-section 16 to 80. Excludes passenger cars, motor cycles and scooters
2/ Including Canada.

ANNEX 3

FOREIGN EXCHANGE

All applications for foreign exchange fall into one of the following four categories. With respect to Category A items, the Central Bank provides foreign exchange to the commercial banks immediately upon application. There is a substantial delay in providing foreign exchange for items falling into categories B, C and D.

Category 'A'		(i)	Personal remittances as family and other maintenance allowances, school fees, personal insurance and pension funds contributions.
		(ii)	Purchase of text-books, journals and science equipments by all universities/colleges.
		(iii)	Chemicals for agricultural purposes.
		(iv)	Payment of insurance and freight for produce from Nigeria to overseas centres, and charter fees for vessels carrying the produce.
Category 'B'	60%	(i)	Payment for fuel including petrol, petroleum products and coal.
		(ii)	Payments for essential imports such as machinery and spare parts required for industry, rehabilitation and reconstruction works; essential raw materials for industries.
		(iii)	Payments for heavy duty trucks and lorries.
		(iv)	Payment for cement, salt, medical equipment, drugs and pharmaceuticals.
Category 'C'	25%	(i)	Payments for other education materials, tyres.
		(ii)	Other remittances in respect of invisible items, e.g. air company remittances, gratuities, director fees, etc.
Category 'D'	15%		Payment for other imports other than those in Categories 'A', 'B' and 'C'.