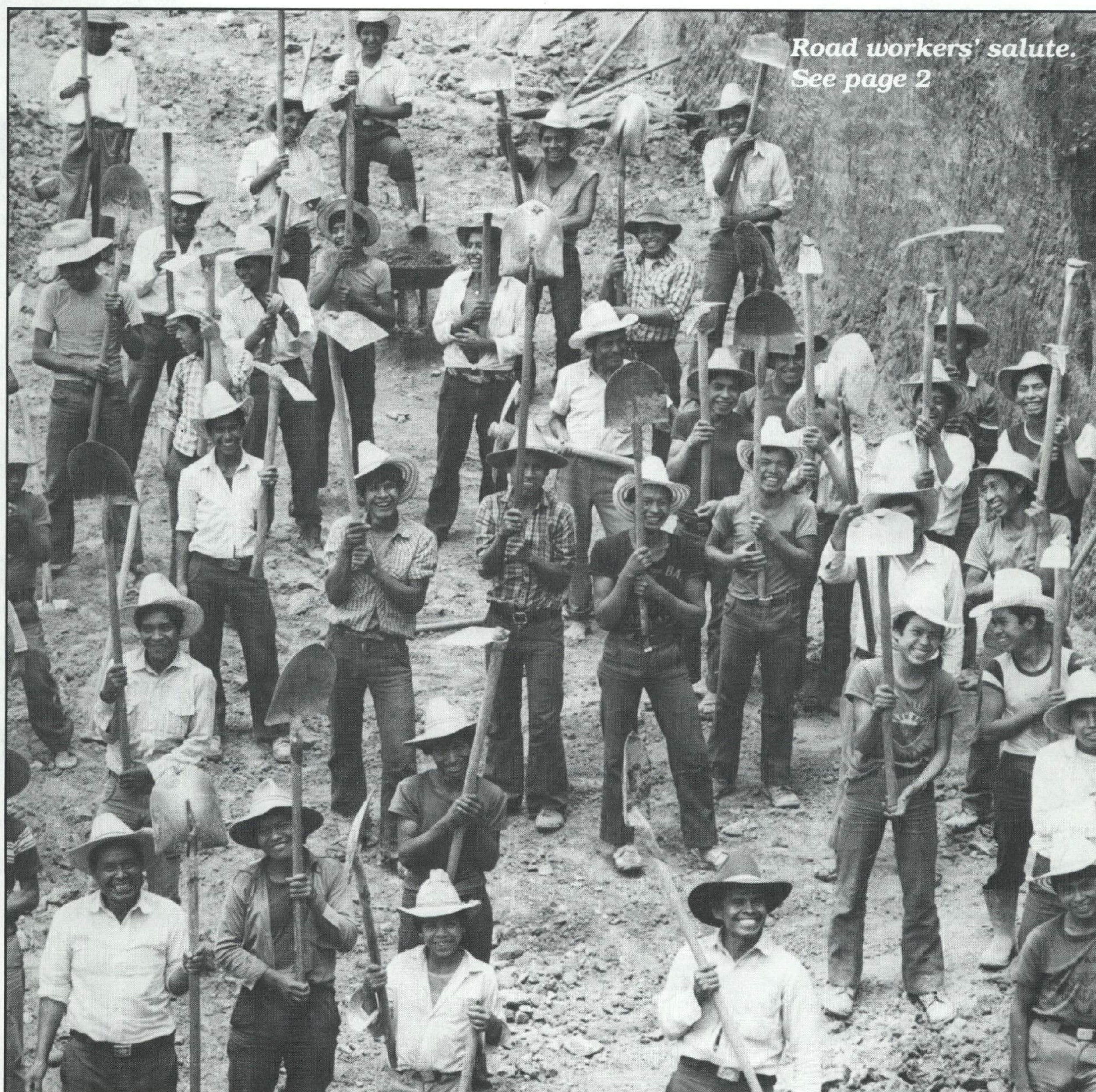
■ Agriculture: the paradox of subsidized credit

THE IDB

Inter-American Development Bank • March 1990



Road workers' salute.
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COVER

Road workers' salute
It's up with the shovels, picks and hoes on a road construction site between San José Poaquil and La Garrucha in Guatemala's central highlands. Most of the 200 laborers are local farmers, for whom the improved road will provide year-round access. Crops were formerly lost when rains turned the existing road into mud, making it impossible for trucks to get the produce to market.

The IDB-financed program will improve 135 kilometers of existing rural roads. It will also construct or rehabilitate 265 kilometers of low-cost feeder roads to link crop-growing areas with marketing and consumption centers.

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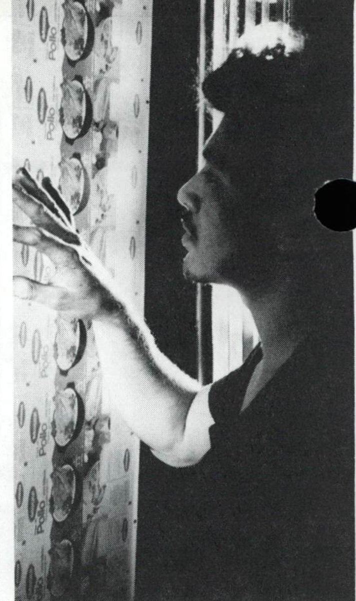

The Bank at a glance
The Inter-American Development Bank is an international financial institution established in 1959 to help accelerate economic and social development in Latin America and the Caribbean. Its headquarters are in Washington, D.C.

The Bank's membership consists of 27 countries in the Western Hemisphere, and 17 from outside the region.

In its 30 years of operations, the Bank has helped to provide, secure and organize financing for projects that represent a total investment of more than $122 billion. The Bank has also fostered a more equitable distribution of the benefits of development, and has been a pioneer in the financing of social projects.

The Bank's highest authority is its Board of Governors, on which each member country is represented. The IDB's 12-member Board of Executive Directors is responsible for the conduct of the Bank's operations.

The IDB's field offices represent the Bank in dealing with local authorities and borrowers and supervise the implementation of Bank-supported projects.

FOCUS

Closing the book on the 'lost decade'

The 1980s have been called Latin America's "lost decade," a characterization that was not contradicted by the region's economic performance in 1989.

According to the IDB's Annual Report, economic growth in Latin America and the Caribbean last year was a disappointing 0.7 percent, repeating the pattern of 1988 and bringing overall expansion of gross domestic product (GDP) for the decade to slightly less than 12 percent. Factoring in the region's continued rapid population growth, per capita GDP during the 1980s declined by approximately 8 percent, regressing to 1978 levels.

Varying results. But the composite picture is made up of some widely varying country results. Some economies emerged from the 1980s quite well. Chile last year posted an 8.5 percent growth in GDP, thanks in large part to strong exports and high levels of fixed gross investment. Paraguay's growth rate of 5.6 percent was due to expansion in the country's agricultural sector. Costa Rica, Guatemala and Suriname grew by around 4 percent, while Colombia and Barbados had growth rates of around 3.5 percent. Brazil and Mexico grew at about 3 percent.

At the same time, many of the countries experienced almost no growth last year, and economic performance was sharply negative for some: -14 percent for Peru, -8.1 percent for Venezuela, -5 percent for Argentina and Panama, and -3.2 percent for Nicaragua.

Almost all of the countries have made serious attempts to carry out macroeconomic adjustments that are expected to pay dividends in the future, according to the report.

The region's economies last year were held back by a combination of inflation, an only modest expansion of exports and the still unresolved debt problem.

In spite of what the report called "determined efforts" to control inflationary pressures, the region's average inflation rate rose for the third consecutive year. Argentina's large fiscal deficit and explosive internal debt fueled inflation in that country. Brazil is threatened by hyperinflation. In Peru, inflation reached an historic high at mid year, and averaged 3,000 percent for the year as a whole. In many countries, expectations of continued and increased inflation left both nominal and real domestic interest rates very high.

Some economies emerged from the 1980s quite well.

The result has been to dampen local investment.

Latin America last year posted an estimated 7.5 percent growth in the value of export earnings for the year. This was lower than the 10 percent growth in export value of all developing countries, suggesting that Latin America has a significant unrealized potential for export growth, according to the Annual Report.

Debt problems persist. Last year's high international interest servicing rates exacerbated the countries' debt problems. The interest servicing obligations on the region's debt in 1989 came to almost $0.23 of each export dollar earned. This was down slightly from the year before, but was still significantly above the ratio of 1987.

"Latin America's debt-service ratio continues to greatly exceed that of any other developing region," states the report, "and limits the resources that the countries can channel to other areas to sustain their economic growth."

Latin America's success in achieving sustained overall growth in the 1990s will depend on improving the region's competitiveness and its export performance, concludes the report. While export performance will depend considerably on internal measures, a favorable international environment is also essential. In particular, a successful outcome of the Uruguay Round of multilateral trade negotiations would give the countries both an incentive to open up their economies and an opportunity to expand exports. More export earnings, combined with debt relief measures, are essential to enable Latin America to rebuild its economies and social infrastructure.

If this scenario does not take place, warns the IDB report, the declining living conditions endured by large numbers of the region's people during the 1980s will continue into the 1990s.

— the editor

AGRICULTURE

The paradox of subsidized credit

It was meant to help, but it probably hurt

by Luis R. Zavaleta

For three decades, the region's governments, in partnership with international development agencies, have carried out programs representing an investment of many millions of dollars to provide farmers with credit at subsidized interest rates. It seemed like a good idea at the time. But now, taking stock of the results, it appears that the objectives of subsidized credit programs have not been met. On the contrary, the policies and the means used to implement them may have backfired, actually worsening the conditions they were supposed to have improved.

This does not deny governments a role in providing rural credit. But particularly during the present economic crisis, we must consider changing key policies and instruments that affect capital markets: credit policy, interest rates, and financial institutions. Taking such a fresh look at rural capital markets will be the first step in truly fostering rural and agricultural development—in spite of the present financial crisis and without adding further to the region's already burdensome debt. Moreover, savings mobilized in rural areas can provide at least part of the financial resources needed for future rural development.

When farmers need financing to plant crops, introduce new ones, or expand production, they have two basic options: the informal financial markets, or their formal counterparts.

The informal markets are important suppliers of credit throughout much of Latin America. In Peru, for example, the network of suppliers, middlemen, truckers, loan sharks and family and friends making up the informal sector is believed to be the country's most important source of farm credit.

Its freedom from cumbersome regulations gives farmers relatively free access to financial agents and to financial resources at low transaction costs. The informal markets' major shortcoming is their inability to match short-term availability of funds to long-term investment needs. However, the potential of informal markets cannot be underestimated when considering future financial policies, as we will see.

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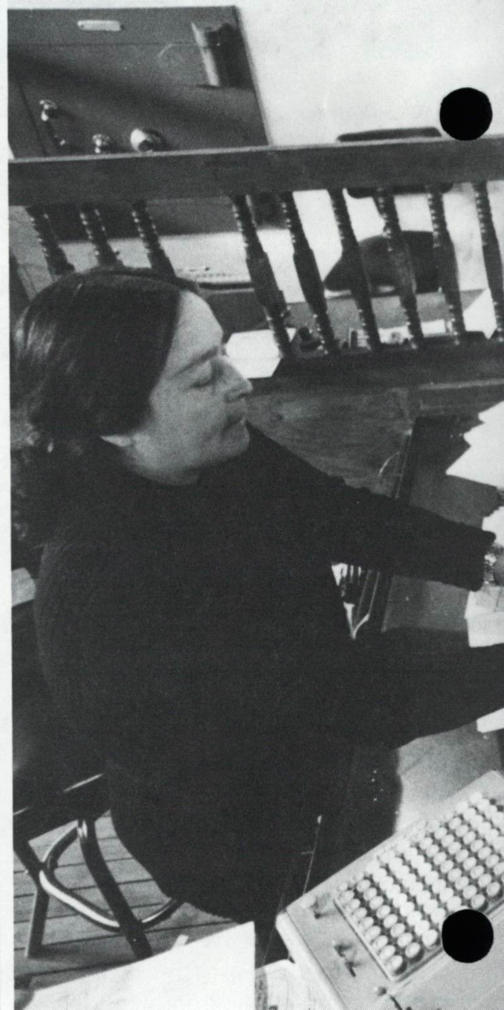
Whereas the informal financial markets have developed on their own, their formal equivalents have been created as part of government policy.

For many years, economists have assumed that income in rural Latin America is so low—one-fifth of urban income—that sufficient capital accumulation could hardly be obtained through incentive mechanisms for rural savings. Moreover, private banks are loath to set up operations in rural areas because of the specialized knowledge agricultural production entails and the uncontrollable natural factors to which it is subjected, such as weather, diseases and insect pests. In general, private banks have limited their agricultural credit operations to certain large farmers and exporters, or for short-term investments.

The governments' answer was to transfer resources from the central government, the banking system, and multilateral institutions, and



disburse it through agricultural development banks under a policy of promotional credit with subsidized interest rates. The resource transfers would achieve three major goals:

▶ Make up for a shortage of medium- and long-term investment financing.

▶ Compensate farmers for adverse macroeconomic policies, for example, price ceilings on agricultural products, export taxes, overvalued exchange rates, etc.

Rural savings can provide at least part of the resources needed for rural development.

▶ Serve a social function by helping to raise rural incomes and bring about a more equitable distribution of wealth.

Although the importance of the agricultural development banks has varied greatly from country to coun-

Farmers line up for loans at a branch office of Colombia's agricultural development bank.

for crops included in price support programs, for crops with assured marketing programs, and for export crops.

Such credit was intended to promote investment and raise production in the agricultural sector. But this goal has not generally been achieved. For example, Peru's Agricultural Bank directs some 90 to 95 percent of its funds to finance short-term operations in crop production and to a much lesser extent marketing. Only 5 to 10 percent is for investment financing.

Although low interest rates may increase aggregate investment for the economy as a whole, subsi-

Subsidized interest rates do not necessarily induce farmers to invest in new technologies.

dized interest rates for agriculture will not necessarily induce farmers to invest in or adopt new technologies. Nor will it influence a farmer to produce a nonprofitable crop. Instead, the farmer will invest these fungible resources where the expected financial return is greatest, which is oftentimes outside of the agricultural sector. It is very difficult and costly for the government lender to trace substitutions among own and borrowed resources. Likewise, restricting the loans to inputs in kind, such as fertilizer or seed, does not resolve the problem. Farmers can allocate these inputs to other crops or sell or barter them.

Encouraging farmers to adopt high-yielding capital-intensive technology by providing credit for this purpose may run counter to the farmers' legitimate reasons for not adopting this technology in the first place. For example, the new technology may not be appropriate given existing market conditions, such as widespread labor unemployment. Promoting these technologies

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try, and even among areas within countries, similarities in their performance have been striking.

The dominant feature of the agricultural development banks throughout Latin America and the Caribbean has been their use of subsidized credit.

Determining interest rates by regulation rather than by market conditions has had a number of negative effects. For one thing, it has given rise to distortions in the pricing mechanism of financial markets. Interest rates have been denied their key economic role of providing a measure of the cost of money and their function of "clearing the market." Moreover, these regulated low interest rates have discouraged private financial institutions from serving rural markets by subjecting them to what amounts to unfair competition. The few private banks that were operating in the rural communities were forced to retreat to urban areas to remain profitable. For the rural communities, this loss was not necessarily compensated by the agricultural development banks.

Another effect of setting interest rates below the market equilibrium has been to generate an excess demand for credit, which could only be resolved through some form of nonmarket rationing procedure. Credit, therefore, has been made available on the basis of such criteria as a borrower's minimum annual wage, outstanding debt balance, size of farm, net agricultural assets, gross agricultural assets, annual family income, total assets, net annual income, per capita income, total net assets, fixed assets, etc. In addition, there was often a loan ceiling for each crop (in many cases equal to some percentage of the total costs of production) per hectare cultivated. Depending on the risk perceived in the production of a crop, the percentage loaned could also change: the higher the risk (as in the case of small-farmer subsistence crops), the lower the percentage financed. In general, the percentage was higher

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through subsidized credit only leads to further inefficient allocation of resources.

Finally, farmers are reluctant to adopt technologies dependent on imported inputs or unreliable domestic supply. In these cases, apparent hesitancy in adopting "advanced" technologies simply reflects their reluctance to increase production risks. Providing subsidized credit will not remove these problems or decrease the risks. It will simply divert the attention of policymakers from the real problems.

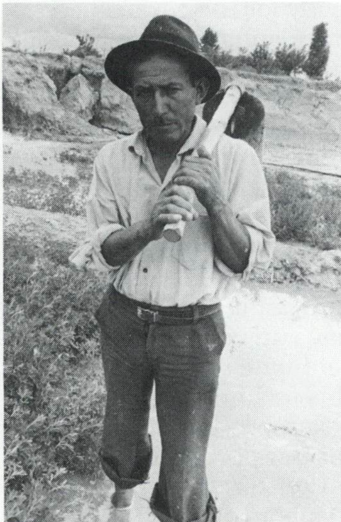
Subsidized interest has also failed to provide significant social benefits. While agricultural development banks are by far the most visible financial institutions in rural areas, their impact on the rural sector has been highly selective. The credit they extend benefits only 7 to 15 percent of agricultural producers, according to IDB estimates. The majority of farmers must continue to depend on informal markets.

Providing subsidized credit to such a small segment of the farming population cannot compensate for the adverse consequences of macroeconomic policies such as price ceilings on foodcrops and appreciated currencies. Moreover, the larger the interest rate subsidy, the greater the benefits accruing to the larger borrowers, and the smaller the volume of credit and subsidies provided to the small farmers. Large farmers use their extensive assets as a guarantee to obtain large loans, and therefore large subsidies. In Colombia, for example, resources mobilized by the Agricultural Financing Fund and the Agricultural Bank have been directed toward cash crops, such as rice, cotton, soybeans and sorghum, which are grown by large farmers, and away from peasant crops. In this way, rather than improve the distribution of income, the policy of subsidized credit has exacerbated the inequitable distribution of wealth. Moreover, payment of interest is only a part of the cost of obtaining a loan. Other costs such as paperwork, travel time to and from the lending institution and bribes can be equally important and particularly burdensome for the small farmer.

The larger the interest rate subsidy, the greater the benefits for large-scale farmers.

Low interest rates also have had a devastating effect on the ability of the development banks to mobilize resources. The low interest rates they must offer to rural depositors amount to a form of taxation and results in a disincentive to save. As a result, the publicly-supported credit agencies have had to adjust their lending to the limited supply of outside loans and transfers. In many cases operating losses have forced the agencies to rely on a flow of subsidies to stay alive.

Even worse, when nominal interest rates fall below the inflation rate, financial institutions may be unable to cover their transaction costs. This can jeopardize their very survival, particularly since publicly supported credit agencies have higher costs due to the wide spectrum of business endeavors and geographic areas covered, the small size of each farm loan, the required technical supervision, and the risky nature of agricultural production.



Irrigating alfalfa in Cochabamba, Bolivia.

BOLIVIA

Taking aim at interest rates

Bolivia's farmers will not be the only beneficiaries of a new IDB-funded agricultural credit program. The nation's financial system stands to gain as well.

Before 1985, government-run agricultural credit programs in Bolivia lent at subsidized interest rates. The result was limited benefits for small-scale farmers and support for projects whose internal rate of return was less than the opportunity cost of capital. In addition, subsidized credit undercut other financial institutions.

Since 1987, all IDB-financed lines of credit have been consistent with the cost of mobilizing long-term resources on the domestic financial markets. In the new program, the interest rate charged will be tied to the LIBOR rate of the day; the financial market therefore will reflect in part the actual cost of raising funds on international markets. Moreover, the interest rate cannot fall below the average interest rate on savings in Bolivian currency.

The result will be a unified financial market, in which the cost of external funds obtained by the government is tied to the cost of mobilizing resources in the domestic market. The program's funds will flow towards the most efficient firms and investments, which offer the greatest expected returns. Savers, for their part, will deposit their money with financial institutions that likewise offer the greatest expected return.

Agricultural development banks must respond to the financial needs of both savers and borrowers.

Despite this past record, the government does have a role to play in providing credit for rural development—if changes are made in policies and program operations. These changes would include the following:

▶ Probably most important, agricultural development banks should decentralize their decision making process. The banks' primary purpose in offering subsidized credit has been to finance the government agricultural development and production plans. Efficiency and long-term sustainability were only secondary goals. The banks must respond to a broader set of priorities, particularly, the financial needs of both savers and borrowers. In every case, commercial, not programmatic, considerations should be emphasized in lending decisions.

▶ Guarantee requirements for obtaining loans could be substituted by other requirements, such as a better knowledge of borrowers, or lending based on the farmers' capacity for repayment. This would give smaller, poorer farmers more access to the available credits.

▶ Banks should adjust their repayment schedules to the cycle of agricultural production and be more flexible if repayment delays are beyond the borrower's control. They should take into account the unpredictability of the weather, problems derived from insolvency of some government agencies at harvest time, etc.

▶ Research should be carried out to explore the potential of rural financial markets for handling resources from noninstitutional sources. For example, formal institutions could utilize informal lenders as rotating savings and credit associations as financial retailers at the grass-roots level. Or these same savings associations could establish their own banks.

▶ Rural financial markets should balance short- and long-term lending, and loan portfolios should be diversified among economic groups or regions. Institutions should strike a balance between savings and external resources, so that they will not be overburdened by the latter. Although development banks were designed to take advantage of large economies of specialization and scale, experience has shown that economies of scope are most important.

Another conclusion that can be drawn from the experience of rural credit programs is that efforts to reform rural financial markets can succeed only in the context of a suitable macroeconomic environment: policies that bring about a low and predictable rate of inflation while preventing major fluctuations in economic activity.

Furthermore, interest-rate and exchange-rate policies must be consistent with one another. Domestic interest rates should exceed interest rates abroad by the expected currency depreciation. Otherwise, savers will transfer their savings abroad, as has been happening since the early 1980s in the region as a whole.

The goal of reforming the rural financial markets is fully attainable and depends on the adoption of the same kinds of sound economic principles as those that are being used to address the region's broader economic problems. Doing so will unleash the creative and financial resources of rural people throughout Latin America and the Caribbean and bring about a renewed period of growth and social justice.

Growing beans in the Dominican Republic.

DOMINICAN REPUBLIC

Turning skeptics into believers

The agricultural development bank of the Dominican Republic, BAGRICOLA, has shown how fresh thinking and a new approach can be used to mobilize rural savings even despite unfavorable economic conditions.

During the 1970s, BAGRICOLA grew to rely on external funds for its lending resources. Then, with the start of the 1980s, the funds dried up.

So BAGRICOLA set itself on a new course: it would obtain its lending resources by mobilizing deposits in the rural areas. The plan was at first greeted with skepticism.

Nevertheless, by September 1985, all but two of the bank's 31 branches were accepting deposits.

The results of the deposit mobilization campaign disproved the idea that low income levels in rural areas must mean an insignificant demand for depository services.

By November 1987, 68,485 savings accounts had been established, about twice the number of loans BAGRICOLA had in its portfolio.

BAGRICOLA's remarkable growth did not take place at the expense of other banks. BAGRICOLA did not have competitors at most locations. Moreover, it offered its depositors interest rates comparable to those offered elsewhere. Finally, many of the bank's clients were first-time depositors in the financial system, making it very unlikely that any switching occurred from existing banks.

ADJUSTMENT

Paying the costs, reaping the benefits

Will Latin America turn it around?

by Margaret Daly Hayes

Although the events in Eastern Europe have grabbed the headlines, profound changes are also taking place in Latin America. The countries have achieved an important consensus on the roots of their economic problems and the measures needed to address them.

Continued pursuit of sound policies and adjustments could well bring about a new decade of prosperity: this was the conclusion of businessmen, bankers and policy makers gathered in London for the Third International Herald Tribune/ Inter-American Development Bank Conference on Latin America. The theme of the February 22-23 meeting was "Latin America in the 1990s—How New Administrations Will Meet the Challenges."

The Latin American participants—from Mexico, Argentina, Brazil, Uruguay and Bolivia—spoke with a united voice about the need to make fundamental changes in their economies.

"We no longer argue about whether to change or not, but what changes to undertake now," observed economist Guido di Tella, Argentina's ambassador to the United States. Similarly, Mexican Finance Minister Pedro Aspe noted that while structural reforms have short-term costs, they also have long-term benefits. "If you postpone the costs, you also postpone the benefits," he said.

Mexico is a good example of the benefits that flow from reforms. After five years of rigorous belt-tightening, stated Finance Minister Aspe, Mexico in 1989 posted a 3 percent increase in its GDP growth rate and a 9 percent decline in public spending. The inflation rate dropped from 160 percent in 1987 to less than 20 percent in 1989.

The country's success came as a result of a vigorous adjustment program consisting of moves to open up the economy, privatize state-held companies, reform the tax system, deregulate the private sector, liberalize the domestic market and renegotiate the debt.

Four years ago, Mexico was largely a closed economy. Ninety-two percent of the country's trade was regulated, tariffs averaged 47 percent, with a maximum tariff of 300 percent. Today, noted Mr. Aspe, the average tariff is 9 percent and the maximum is 20 percent. Import permits and licenses are no longer required. The private sector bore the burden of these adjustment measures, and "they've been pretty good about it," said Mr. Aspe. While imports did rise following deregulation, they are now leveling off. On the other hand, non-oil exports showed a 300 percent increase in five years, and 70 percent of Mexico's exports today are non-petroleum products.

'We no longer argue about whether to change, but what changes to undertake now'

In the area of privatization, the Mexican government so far has sold 273 firms, among them the national airline Aeroméxico. Since the sale, Aeroméxico has grown 15 percent per year and turned a profit for the first time in 27 years.

Mexico's goal in tax reform is to generate revenue by broadening the tax base. In the past, Mexico had high individual and corporate tax rates, but low revenues. Now its tax rates are lower, but many more companies and individuals are on the tax roles. Tax forms have been simplified, audits are being taken seriously, and tax havens that once permitted 16.8 percent of the national product to escape taxes have been eliminated.

Mexico is courting foreign investment through a broad-based liberalization of rules. Two-thirds of Mexico's non-banking activities are now open to foreign investment. Deregulation also has made the domestic economy more efficient and cost effective. For example, the average trucking rates dropped 28 percent in the week after deregulating the industry, said Mr. Aspe.

On the matter of the debt, Mr. Aspe said succinctly: "we got our deal." The recent agreement's $7 billion in enhancements and $15 billion in debt reduction will mean a 4 percent drop—from 6 percent to 2 percent—in net transfers in the 1990s and a decline in the debt to GDP ratio from 60 percent to 40 percent. Without the debt package, noted Mr. Aspe, some of the reforms that Mexico has undertaken could not have been carried out. Adequate offers for Mexicana de Aviación came only after the debt agreement, as did 87 percent of the $2.7 billion in capital repatriations and $2.6 billion in foreign direct investment.

The debt package was a welcome development for investors and bankers. The Mexican government recently returned to the international capital markets, and Mexican corporations are going to the market to finance their own operations.

Adjustment measures are also turning the tide for Uruguay. Moreover, stated Finance Minister Ricardo Zerbino, adjustment and growth policies need not be contra-

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Mexico's GDP grew at 3 percent last year while its public spending dropped 9 percent.

dictory; they can just as well be complementary.

Over the past five years, Uruguay's GDP has grown 15 percent, with real growth occurring each year according to Mr. Zerbino. Exports, encouraged by a competitive exchange rate, expanded by 80 percent from 1986 to 1989. Private sector investment has increased, unemployment fell from 14 percent in 1984 to 8.5 percent in 1989, and real wages rose by 30 percent over the five-year period.

The country's total debt, while still a constraint on the economy, has fallen as a proportion of both GDP and exports. Uruguay began to negotiate a Brady Plan package with its creditors in early 1989 and in August returned to the international financial markets with a private placement in the Japanese bond market.

In 1985 it seemed that only a miracle could save Bolivia from the ravages of hyperinflation. The country's remarkable turnaround since then, according to Planning Minister Enrique García Rodríguez, came as the result of cooperation between political parties, the private sector, labor unions, the church, the military and, above all, the country's citizens. Inflation dropped from a high of 28,000 percent in 1985 to less than 16 percent in 1989. GDP has begun to expand, although per capita GDP remains well below 1980 levels. In 1990 Bolivia will try to complete the repurchase of its commercial bank debt.

"The Bolivian experience suggests that successful adjustment and stabilization involve taking very difficult decisions," Mr. García Rodríguez told the conference participants. It means "maintaining discipline and consistency in economic policy management, and having the appropriate political backing as well as the support and tolerance of broad segments of society. It also involves severe suffering and hardships that must be ameliorated in the short term and rewarded in the medium term."

Like the Latin American ministers, the banking community representatives were in agreement on their future relations with the region. Commercial banks, they said, will be involved in Latin America—but differently. The 1980s gave the banks a sobering lesson on the limits of their proper role in sovereign lending. "Balance of payments support and deficit financing are not appropriate roles for commercial banks," conceded Anthony Loehnis, vice chairman of Britain's S. G. Warburg & Co. Ltd. Martin Murtfeld, Deutsche Bank senior vice president, argued that commercial banks in the near future will limit their Latin American operations mainly to trade and project financing, co-financing with members of the World Bank and IDB groups, and lending to the private sector.

As to the question of continued donor country support for Latin America, Japanese Finance Ministry special advisor Toyoo Gyoten summarized their position as follows:

"A politically stable and economically prosperous Latin America is crucial. . . regardless of other events," he said in a veiled reference to the emergence of Eastern Europe. In Japan, he continued, Latin America is becoming an increasingly important element in government policy.

Despite the disappointing outcome of the 1980s, Latin America can well take pride in its long-term economic performance. OECD Development Centre President Louis Emmerij reminded the conference participants that "GDP growth in Latin America averaged 3.8 percent per annum during the first nine decades of the 20th century against less than 3 percent for the OECD countries, 3.3 percent for the USSR and 3.2 percent for Asia."

But the long view also reveals key weaknesses in the areas of weakness in the region's past economic management. Among the most difficult economic decisions a country must take, stated Mr. Emmerij, involves the crucial issue of timing: when to shift its economic development strategy and when to start the process of adjustment. Most of the conference participants agreed with Mr. Emmerij's verdict that "part of Latin America's economic problems stems from errors of judgment in these two issues." Latin American leaders failed to heed signs of the need to change in the post-1973 oil crisis period. As Mexico's Aspe rued, "We thought that high oil prices and low inflation were a permanent state of affairs. But it turned out that the opposite was true."

In his summary of the meeting, IDB President Enrique V. Iglesias found broad agreement on the part of Latin American participants that the cause and nature of the region's economic problem are known and there is agreement on what to do.

Latin America will compete favorably with Eastern Europe for future investment resources.

The European participants agreed on a number of points: that the international community must play a role in the debt problem; that the public sector remains committed to Latin America; that private sector investment is crucial and commercial banks will work through the private sector to stay involved in the region; and that a successful outcome of the Uruguay round of trade talks is crucial.

Finally, while Eastern Europe is today's "big news," the profound changes taking place in Latin America deserve equal recognition, according to Mr. Iglesias. Overseas investors take note: Latin America can compete favorably with Eastern Europe for future investment resources.

A man with an answer: students at the Central American Institute of Business Administration decide how a failed firm can regain its health. The school set up a business economics program with the help of an IDB loan.

1989

A year of transition

Springboard to the 1990s

The IDB sharply boosted its loan approvals last year while laying the financial, policy and organizational groundwork for a stronger institution, according to the Bank's 1989 Annual Report.

The Bank approved 36 loans during 1989 totaling $2,618 million. This was the highest amount since the $3 billion approved in 1986.

The largest share of the Bank's lending—28 percent—was extended for energy projects. About 22 percent will help increase agricultural production, 19 percent will finance social infrastructure investments, 13 percent will finance transportation and communications infrastructure, and 15 percent is earmarked for industry and tourism projects.

Other 1989 highlights were the following:

▶ $61 million in technical cooperation approved, including both grant and contingent recovery operations. The figure was the highest in the Bank's history.

▶ $8.1 million approved for 19 projects in the Bank's Small Projects Program.

▶ $1,222 million in loan repayments.

▶ The equivalent of $1,983.6 million in 11 individual borrowings in the world's capital markets. This was more than double the previous year's borrowings.

The Bank's Annual Report is being reviewed by the institution's Board of Governors at its 31st annual meeting in Montreal, Canada.

A new Bank. The 1989 Annual Report also summarizes the major steps the Bank took last year to increase its resources and adjust its policies and organization to meet the region's needs in the present decade.

These measures, which have been reported in previous issues of *The IDB*, include the following:

▶ An agreement on a $26.5 billion increase in Bank resources, which went into effect on January 17 of this year. The increase will enable the Bank to lend $22.5 billion in the period 1990-93.

▶ A new thrust for Bank programs under the resource increase, including the introduction of sector lending; strengthening Bank activities in the fields of environmental protection, support for women, and microentrepreneurs

▶ Increasing the maximum percentage of foreign exchange that the Bank can lend for a given project.

▶ A termination program designed to reduce staff, increase staff mobility, and open the way for the recruitment of new talent.

▶ Changes in the IDB's organizational structure. Included were moves to strengthen the Plans and Programs Department's ability to program the Bank's operations and to conduct policy dialogue with its member countries in macro and sector analysis. A strengthened Finance Department will enable the Bank to operate effectively in the world capital markets at the much higher levels contemplated under the new resource increase. New units created in the Bank include a Sector Lending and Policy Division, a Division of Environmental Protection, a Microenterprises Division and a Cofinancing and Export Promotion Division.

Low-income benefits. An analysis of the distributive impact of the Bank's 1989 lending shows that low-income people will obtain 49 percent of the benefits of last year's lending, according to the report.

A basic policy adopted by the Bank's Board of Governors mandates that about half of the resources the IDB lends in each four-year replenishment period must directly benefit low-income people. The methodology the Bank devised to determine the distributive impact determines how many benefits, and what proportion of each benefit, accrue to low-income groups. A low-income level benchmark is defined in cooperation with each borrowing country.

The Annual Report also noted the Board of Director's approval last December of a new methodology for calculating the Bank's lending rate on its ordinary capital loans. The new Pool Based Variable Lending Methodology uniformly adjusts interest changes applicable to the outstanding balance on all loans made under it, not solely to disbursements, as was previously the case. As a result, all borrowers share equally the costs and benefits of changes in the lending rate.

Reciprocal benefits. The Annual Report also presented figures on the amount suppliers benefited from providing goods and services for Bank-financed projects in 1989. A total of 607 contracts amounting to $614.7 million were awarded for firms in 33 member countries in 1989. Disbursements in convertible currencies for purchases of goods and services totaled $2.3 billion last year, of which borrowing member countries received $1.3 billion and non-borrowing countries received the remaining $949 million.

These disbursement figures reflect only the initial round of procurement. They do not measure amounts received by subcontractors or the secondary and tertiary impact of the Bank loans.

1989

Support for the private sector

Operations for $14.85 million

The Inter-American Investment Corporation last year approved $14.85 million in loan and investment operations to help finance projects worth $51.6 million, according to its 1989 Annual Report.

The projects, which were the first approved by the Corporation after becoming operational last October, are being carried out by private firms in Argentina, Brazil, the Dominican Republic, Mexico and Uruguay.

Loan for Argentina: Signing are Alberto José Mangiaterra, of Argentina's Terminal 6 S.A., and Corporation General Manager Gunther Muller.

In addition, the Corporation had nine other operations under consideration at the end of the year. These represent possible loan and capital investment commitments totaling $33.9 million.

The Corporation, which is the merchant banking affiliate of the IDB, grants medium- and long-term loans and makes capital investments in private enterprises in Latin America and the Caribbean.

The Corporation's Board of Governors will review the Annual Report at its Fifth Annual Meeting, which is being held in Montreal, Canada, April 1-4.

Also in 1989, the Corporation laid the groundwork for an ambitious program of future activities. By year's end it had established contacts with private sector groups in all of its member countries, evaluated markets for its services, and identified approximately 200 projects for discussion and analysis.

The Corporation also has carried out discussions with government officials from various Latin American countries on possible collaboration in the privatization of public enterprises. Opportunities were also identified for restructuring private companies and for advising on ways to stimulate new flows of external investments into the region.

Other activities included studies and arrangements to participate in external debt conversion operations that will tie private sector transactions to reductions in the public debt, particularly intra-Latin American debt.

In the area of fund mobilization, the Corporation obtained a commitment in principle from the Dutch ABN Bank to cofinance a project presently under way in Brazil.

The right moment. Last year was a propitious time for the Corporation to begin activities, noted the Annual Report. The deepening economic crisis and other factors led many Latin American governments to adopt economic policies anchored in free markets and openness to the external world. The region also has begun to revaluate the role of small- and medium-scale enterprise—including those in the informal sector—in creating jobs, providing goods and services, and decentralizing economies.

"The private sector gained widespread public support as well as support from Latin American officials with widely varying social objectives and ideologies," stated the Corporation report.

PEOPLE

More changes in Bank staff

Appointments to fill key positions throughout the Bank were announced recently.

Sebastião Marcos Vital has been named Deputy Manager of the Policies Subdepartment.

Sebastião Marcos Vital

A citizen of Brazil, Mr. Vital was most recently an economist and professor at the Getulio Vargas Foundation in Rio de Janeiro. He has also served as president of the Development Bank of Rio de Janeiro, superintendent of the Planning Institute of the Ministry of Planning, vice president of the Development Bank of Minas Gerais and his government's vice minister of finance.

Mr. Vital has an economics degree from the University of Minas Gerais, a master's degree in economics from the Getulio Vargas Foundation and an advanced certificate in finance from New York University.

Ronald Brousseau has been appointed to the position of deputy controller.

Ronald Brousseau

A citizen of the United States, Mr. Brousseau has had a long career in the IDB, having served as a deputy manager in the Operations Department, a special advisor to the operations manager and an operations officer, and an economist in the Economic and Social Development Department. He served as a Peace Corps volunteer in Guatemala.

Mr. Brousseau has a degree in foreign affairs from Assumption College in Massachusetts and a master's degree in economics from the University of Wisconsin, in Madison.

Helio Tollini

Helio Tollini has been named chief of the Agriculture Division.

A citizen of Brazil, Mr. Tollini previously served with the International Fund for Agricultural Development in Rome, Italy, as director of the Planning and Economic Analysis Division. He has also held senior positions in Brazil's Ministry of Agriculture, among them national secretary for food supply and coordinator of the Economics Advisory Group.

Mr. Tollini has a degree in agronomy and a master's degree in agricultural economics, both from the Federal University of Viscosa, and a doctorate in economics from North Carolina State University.

Juan J. Santa Cruz has been appointed to the position of external relations deputy advisor.

Juan J. Santa Cruz

A citizen of Chile, Mr. Santa Cruz has held a number of senior positions at the Bank, most recently chief of the Division of Administrative Services. He previously served in the Finance Department as deputy associate treasurer, and was an operations officer.

Mr. Santa Cruz has a law degree from the University of Chile.

Washington to the Caribbean: IDB President Enrique V. Iglesias welcomes Uruguayan President-elect Luis Alberto Lacalle (right) to Bank headquarters. In Jamaica, the Bank president meets with Jamaican Prime Minister Michael Manley (right) and Central Bank Governor G. Arthur Brown (left) during a January visit to that country. While in the Caribbean, Mr. Iglesias also visited Haiti to meet with government officials and view projects.