

LOAN COMMITTEE

LC/M/86-34
November 5, 1986

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Minutes of the Loan Committee Meeting to consider
GUATEMALA - Proposed Export Development Project
held on October 28, 1986, in Conference Room E-1208

A. Present

Committee:

Chairman: Messrs. Stern
Finance: Hittmair
Legal: Scott
ERS: Baneth
OPS: Husain
RVP: Knox

Other:

Messrs/Mmes. Steckhan
Picciotto
Dubey
Wessels
Elson
Schultz
Collell
Clements
Donovan
El Maaroufi
El Serafy
Gonella
Guerard
Hallberg
Jaspersen
Moritz
Pinell-Siles
Roger

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COMMITTEE

Senior Vice President, Operations (Chairman)
Senior Vice President, Finance
Vice President & General Counsel
Vice President, Operations Policy
Regional Vice President concerned*
Vice President, Energy & Industry (for lending
in these sectors and SALs)
Vice President, Economics and Research (for non-
project lending)

OTHERS

Standard (see OMS 9.25 page 7)

*Copy to all other Regional Vice Presidents

B. Issues

1. The meeting was called to discuss the proposals in Mr. Knox's memorandum of October 16, 1986, for an Export Development Project in Guatemala. The discussion focussed on issues which were raised by the Chairman and by the Country Policy Department's memorandum of October 24, 1986.

C. Discussion

2. Macroeconomic Framework: The Chairman inquired about the progress made by the Government in establishing an appropriate policy framework for economic stabilization and adjustment. Regional staff explained that in June 1986, the new civilian Government had introduced a first set of stabilization measures designed to reduce inflationary pressures and strengthen the country's external position. Over the past few months, the Bank and the Fund have been pressing the Government for a consolidation of the stabilization process in 1987 through a number of measures, including a further reduction of the combined Central Bank/public sector deficit, a reduction of external arrears, and a further substantial increase in interest rates. A Fund mission is scheduled to visit Guatemala in November to discuss these issues further and prepare a draft letter of intent for a possible stand-by early next year. The Bank has also stressed the importance of putting in place a medium-term economic development strategy and has been discussing with the Government the main ingredients of such a strategy, namely production and export diversification, greater resource mobilization and more efficient use of resources, improved basic services, and better public enterprise management. Discussions of the CEM next month will provide an opportunity to advance our dialogue with the Government even further. The Government has been receptive to Bank and Fund advice and is in substantial agreement with the objectives sought, but has yet to define specific targets, instruments and timetables. The Committee noted that the Bank and Fund were in broad agreement on the approach to Guatemala's problems. The Committee further noted that, prior to inviting negotiations for the proposed project, the Region will submit for the Loan Committee's review a DCB including an assessment of the country's creditworthiness and a proposed Bank lending strategy.

3. Project Concept: The Region clarified that the proposed operation consisted of two major components: (i) a quick-disbursing component in support of the policy reforms necessary to provide an appropriate environment for the development of Guatemala's exports, and (ii) a credit facility to finance imports required by non-traditional exporters to non-CACM countries. The trade policy reforms included under the proposed project are substantially neutral as regards specific commodities and sectors. The specific orientation of the credit facility to non-traditional exporters is justified, since such exports have far greater unsatisfied needs for financing and better demand prospects and potential

for expansion (with the possible exception of meat). Both traditional and non-traditional exports will benefit from the proposed acceleration of the phase-out period of the windfall export tax. Such phasing-out, however, has to be gradual, because of the time required for the introduction of appropriate alternative tax measures. For instance, introduction of a land tax may raise controversial issues in the country, and involve serious complications. The Committee agreed that a tax on coffee exports could be maintained, provided its rates continue to vary in accordance with changes in world prices.

4. Hybrid Nature of the Proposed Loan: The question was raised as to the rationale for not making this operation only a credit facility with similar conditions. The Region explained that the policy changes to be introduced under the project are essential to provide an appropriate environment for the development of exports and the use of the proposed credit facility and that it was questionable whether they would be put in place in a timely fashion without the leverage that a quick-disbursing component would provide.

5. Common Approach to the CACM Tariff: The Region confirmed that Guatemala will be requested to take all the actions on tariff reductions that Costa Rica has agreed to take.

6. The Committee also agreed that: (i) caution is required in the possible replacement of SGS by national staff, since only SGS can effectively carry out certain functions (e.g., audit and spot checks at ports); (ii) a sufficiently detailed Export Development Policy Statement before Board presentation should make the preparation of a National Export Development Strategy unnecessary; (iii) the proposal of an Export Credit Guarantee and Insurance is acceptable, because of the need to compete with other countries with similar facilities; and (iv) Free Trade Zone policies will focus on improving the operation of existing facilities.

D. Conclusion

7. Subject to the modifications noted above, the Committee approved the Regional proposal to proceed with appraisal of the proposed Export Development Project along the lines set out in the Initiating Memorandum.