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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

REPORT AND RECOMMENDATIONS

of the

PRESIDENT

to the

EXECUTIVE DIRECTORS

on the

PROPOSED LOAN

to

CENTRAL HIDROELECTRICA DEL RIO ANCHICAYA, LIMITADA

guaranteed by the

REPUBLIC OF COLOMBIA

October 30, 1950

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

REPORT AND RECOMMENDATIONS OF THE PRESIDENT TO
THE EXECUTIVE DIRECTORS CONCERNING THE PROPOSED LOAN
TO CENTRAL HIDROELECTRICA DEL RIO ANCHICAYA, LIMITADA

1. I submit the following report and recommendations with regard to the proposed loan of \$3,530,000 to the Central Hidroelectrica del Rio Anchicaya, Limitada (CHIDRAL), of Cali, Colombia.

PART I - HISTORICAL

2. On July 20, 1948, a Colombian Financial Mission to the United States presented to the Bank an informal loan application for various development projects.

3. A Bank mission visited Colombia in July and August 1948 to assess the financial and economic situation of the country and to report on the projects submitted. The mission recommended a list of projects of high priority for the Bank's consideration which included three hydroelectric projects, (Anchicaya, La Insula and Lebrija) and a project for agricultural mechanization. A loan of \$5 million for the agricultural mechanization project was made by the Bank on August 19, 1949.

4. A technical mission from the Bank visited Colombia in December 1948 and January 1949 to make an examination of the technical and financial aspects of the three hydroelectric projects. At that time the technical features of the Anchicaya project were in the process of being redesigned by an American firm of consulting engineers. Its report was submitted to the Bank in July 1949.

5. Shortly thereafter, the Bank's representatives visited Cali and had technical discussions with the CHIDRAL officials on details of the stream-flow of the Anchicaya river, the design of the dam and plant, the market for power, the cost of the project and the sources for local currency financing.

6. The Bank informed CHIDRAL on February 16, 1950, that it was prepared to enter into negotiations for a loan for the Anchicaya hydroelectric project, subject to certain conditions, and formal loan negotiations started on July 13, 1950, with Dr. Zuleta-Angel, Colombian Ambassador in Washington, acting on behalf of the Guarantor as well as of the Borrower.

7. CHIDRAL formally applied for a loan on October 27, 1950. The Colombian Ambassador to the United States has been authorized to execute the Loan Agreement on behalf of CHIDRAL and the Guarantee Agreement on behalf of the Colombian Government.

PART II -- DESCRIPTION OF THE PROPOSED LOAN

Borrower

8. The borrower would be the Central Hidroelectrica del Rio Anchicaya, Limitada, a company organized and established in 1944 under Colombian law as a commercial company of limited liability. Its stock is owned by the Government of Colombia, the Department of Valle del Cauca and the Municipality of Cali, the participation of the three shareholders being 51%, 23% and 26%, respectively.

Guarantor

9. The guarantor would be the Republic of Colombia, a member of the Bank.

Amount

10. The loan would be in the amount of \$3,530,000 or its equivalent in other currencies.

Purpose

11. The proceeds of the loan would be used to provide the Borrower with the greater part of the foreign exchange required for a hydroelectric plant on the Rio Anchicaya together with the necessary transmission lines and substations. The installed capacity of the plant would be 24,000 kw of electric power, which would be supplied to the City of Cali.

12. CHIDRAL will be the only supplier of power to the City of Cali. In addition to the new generating and transmission facilities of the Anchicaya system, it will own and operate the existing generating facilities which it proposes to purchase from the Municipality (about 10,000 kw). The Municipality will continue to own the distribution system, and will purchase the power from CHIDRAL at agreed rates satisfactory to the Bank.

13. The total cost of the Anchicaya project is estimated at the equivalent of \$13,296,000, broken down as follows:

<u>Sources of Financing</u>	<u>Foreign Exchange Expenditure</u>	<u>Local Currency Expenditure</u>
	(In U.S. Dollars)	
CHIDRAL	1,265,000	8,501,000
IBRD	3,530,000	+
	<u>4,795,000</u>	<u>8,501,000</u>

Terms

14. The loan would bear interest at the rate of 4% per annum including the statutory commission of 1%.

15. The commitment charge would be at the customary rate applied by the International Bank and would accrue from the effective date of the loan or from February 1, 1951, whichever is the earlier.

16. The loan would be amortized by approximately equal semi-annual principal and interest payments of about \$144,000 commencing May 1, 1954, and ending November 1, 1970. These payments would retire the loan by maturity on November 1, 1970.

17. I consider that the proposed schedule for the repayment of principal and the rate of interest and other charges in connection with the proposed loan are reasonable and appropriate.

Legal Instruments and Legal Authority

18. Appendix I contains drafts of the following legal instruments to be executed to give effect to the proposed loan:

- (a) A Loan Agreement between the Bank and CHIDRAL;
- (b) A Guarantee Agreement between the Bank and the Republic of Colombia.

It will be observed that the Loan Agreement would not become effective until after certain specific conditions had been fulfilled, including:

- (i) the curing of certain legal defects in the corporate structure of the Borrower;
- (ii) the conclusion of agreements, satisfactory to the Bank, concerning the acquisition of the power generating plants and installations of the Municipality of Cali, and concerning the sale of power by the Borrower to the Municipality (see paragraph 12 above);
- (iii) the conclusion by the Borrower of arrangements, satisfactory to the Bank, for the provision of the additional capital funds needed to carry out and complete the project (see paragraph 40 below).

19. Law 90 of December 16, 1948 of the Republic of Colombia authorizes the Colombian Government to sign the proposed Guarantee Agreement.

PART III - APPRAISAL OF THE PROPOSED LOAN

20. A draft of the report of the Currie Mission was made available to the Executive Directors on July 11, 1950, and was distributed in its final form on October 24, 1950. This report contains an analysis of the Colombian economy and sets forth a suggested program for the economic development of Colombia.

21. A technical and financial appraisal of the project to be financed by the Bank loan is attached as Appendix II (Loan 107).

Justification for the Loan

22. The construction of the Anchicaya hydroelectric plant was decided upon primarily in order to satisfy the demand for power in Cali, a city of about 165,000 inhabitants. Cali is one of the four major industrial centers of Colombia. It is located in the Cauca Valley, a region with considerable agricultural and industrial potentialities and it has the fastest growing population of the country.

23. During the last ten years, Cali has suffered from a shortage of power. It has been impossible to meet even the residential demand and many potential customers have been denied connection to an already overloaded system. Because of the power shortage, many of Cali's industrial establishments have been forced to install their own individual power plants. The high cost of establishing and operating such plants has been a deterrent factor in the growth of the city's industries.

24. Considerable industrial expansion is now planned in Cali, and there is good reason to believe that the creation of an ample source of power at this time would act as a spur to this development, to which the favorable geographical location, natural resources and transportation facilities have already given the initial impulse. The Currie Report specifically mentions the Cali area and states that it should be assigned high priority in the development of new power projects.

25. In the opinion of the Bank's engineering staff, the Anchicaya hydroelectric project is technically sound. Completion of this project would provide the City of Cali with sufficient electric power and an effective distribution system.

The Economic Situation in Colombia

26. A report on recent developments in the economy of Colombia has been prepared by the Economic Department and is attached (Appendix III).

27. Industrial and agricultural production is increasing steadily. Receipts from the export of coffee, which accounted for 75% of total exports in 1949, are at an all-time high, and oil exports also ran high in 1949, contributing 18% to total exports.

28. The volume of coffee production and exports declined during the 1949-50 season as a result of political disturbances as well as heavy rainfall, but export receipts did not suffer owing to the considerable increase in coffee prices at the end of 1949. It is expected that the former export volumes will be resumed, and prospects for coffee prices, at least over the next 3 years, are good.

29. The prospects of oil exports are greatly dependent on Government petroleum policies, particularly with respect to foreign equity investment in the petroleum industry. Recent legislation in this field has discouraged the foreign oil companies operating in Colombia. Further exports of oil

will tend to decrease as rising demand for oil within the country necessitates an increasing proportion of output to be retained for domestic consumption.

30. Colombia's balance of trade has been very favorable lately, leaving a net balance of \$51 million in 1949 and of \$31 million in the first four months of 1950. This development was mainly due to a drastic reduction of imports through the imposition of strict import control regulations, and to a considerable increase in the domestic production of consumer goods.

31. Including the undisbursed balance of several Eximbank credits and after allowing for other proposed, but not yet effective, borrowing, the total outstanding external debt of Colombia amounts to approximately \$190 million (mostly in U.S. currency), and will require an annual debt service of about \$20 - 22 million in the next five years, or 6 - 7% of expected receipts on current account.

32. Colombia's gold and foreign exchange holdings stood at \$111 million in December 1949, reached \$128 million in February 1950, and fell back to \$108 million on June 30, 1950. It is believed that in the short run Colombia will be able to maintain its reserves without much difficulty.

33. Government budgets have never been high, compared with the level of national income, and the Government deficit and debt are relatively small. Fiscal policies in general have been conservative in the past, but the new Government seems to be ready to engage in large development expenditures.

34. A resurgence of inflationary tendencies has developed since the beginning of 1950, due to legislative wage increases and an increase of bank credits, and caused a rise of 18% in the cost of living index between January and May 1950.

35. By and large, the main trends in the Colombian economy are favorable. Development has been and is proceeding, particularly since the war. Capital formation is at a relatively high level, private investment providing some three-quarters of the total. As a result, there has already been a notable expansion of production; the Currie Report estimates that the volume of industrial production increased 143% from 1939 to 1948.

36. This expansion of production is in the direction of diversification of the economy, enabling Colombia to utilize more of her own resources to meet her own consumption requirements. She remains, however, heavily dependent upon the export of a single commodity, coffee, and, although the immediate prospect is very favorable, this entails obvious long-run dangers. Those dangers are diminished by the diversification and widening of domestic production that is occurring, since it will become easier to forego imports without real hardship. Nevertheless, prospects for long-run stability would be improved by expansion of other exports to the full extent possible.

37. The development process has generated and could continue to generate import pressures arising from requirements for imported equipment, and from monetary expansion due partly to domestic financing of investment. Colombia seems ready to face this and other development problems squarely. Not only did she invite the assistance of the Bank in a form which resulted in the Currie Report, but she is moving towards thorough study and implementation of that Report by creating agencies whose center is the Committee on Economic Development.

38. The prospects for sound future development, for which Colombia has substantial resources, therefore appear good. Even though foreseeable export diversification can only be limited, development should ease real pressures for non-dispensable imports, permitting greater freedom in allocation of exchange receipts.

The Political Situation

39. While the political situation has been unsettled ever since the disturbances of April 1948, I do not believe that this need prevent the Bank from making the proposed loan.

Prospects of Fulfillment of Obligations

40. CHIDRAL's present resources, including the proposed loan, will fall short of the presently estimated amount required to complete the project and to provide adequate working capital. An increase of the subscribed capital of CHIDRAL will be necessary. CHIDRAL will have to make satisfactory arrangements for such increase as a condition precedent to the proposed loan becoming effective. In order to allow for further price rises and as an assurance that construction of the project will not be unduly delayed by lack of peso funds, the proposed Guarantee Agreement provides that the Government of Colombia will, in case of need, make available such additional funds as may be needed to complete the project.

41. The Anchicaya station is a high cost installation, the investment amounting to about \$560 per installed kw. However, about 73% of the cost of the plant will be met with share capital, so that interest and amortization service is required on only 27% of the investment. On the basis of the power rate agreed upon between CHIDRAL and the Municipality, and after deducting all operating expenses including depreciation, it appears that this project will earn ample income to enable the Borrower to meet its obligations towards the Bank.

42. In the opinion of Bank observers who have visited Colombia, the management of CHIDRAL is competent and capable of satisfactory execution of the project and its operation after completion.

43. As provided in Article III, Section 4(i) of the Articles of Agreement, the Republic of Colombia will guarantee the repayment of the Bank loan. In addition, it will guarantee the performance of all other obligations undertaken by CHIDRAL under the Loan Agreement.

44. In the light of the above considerations, it is my opinion that CHIDRAL and the Guarantor will be in a position to meet their obligations under the proposed loan, and that in making this loan, the Bank will be acting prudently in the interest of the Republic of Colombia and of the members of the Bank as a whole.

45. Appendix IV contains a recommendation of the proposed loan by the Statutory Loan Committee provided for in Article III, Section 4, Paragraph (iii) of the Articles of Agreement.

PART IV - COMPLIANCE WITH ARTICLES OF AGREEMENT

46. I am satisfied that the proposed loan would comply with the requirements of the Articles of Agreement of the Bank.

47. I am also satisfied that, in the prevailing market circumstances, CHIDRAL would be unable to obtain elsewhere a loan of the amount required on reasonable terms.

PART V - RECOMMENDATIONS

48. I recommend that the Bank at this time make to Central Hidroelectrica del Rio Anchicaya a loan of \$3,530,000 for a term of 20 years with interest (including commission) and commitment charge at such rates and on such other terms as are specified in the draft Loan and Guarantee Agreements attached as Appendix I.

Eugene R. Black
President

October 30, 1950