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COLOMBIA

SMALL PROJECTS FINANCING PROGRAM

PROPOSAL FOR FINANCING AND TECHNICAL COOPERATION FOR:

CORPORACIÓN EL MINUTO DE DIOS

**PROJECT TO PROVIDE
FINANCIAL SERVICES TO MICROENTERPRISES IN CHOCÓ**

(SP/98-03-36-4-CO)

This document was prepared by the project team consisting of: This document was prepared by the project team consisting of: Fernando Palacio (COF/COL); Miguel Coronado (LEG/OPR); Leyda Fajardo (LEG/OPR); Alexandra Santillana (SDS/MIC); and Miguel Taborga (SDS/MIC); Project Team Leader.

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ABBREVIATIONS

CESI	Committee on Environment and Social Impact
CMD	Corporación Minuto de Dios
FSO	Fund for Special Operations
PCTGO	CONTIGO program

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EXECUTIVE SUMMARY

AMOUNT AND SOURCE: IDB: Financing: US\$300,000
Technical cooperation: US\$250,000 nonreimb.
Corporación Minuto de Dios: US\$150,000
Total: US\$700,000

The funds for the financing and the technical cooperation operation will come from the net income of the Fund for Special Operations (FSO) in local currency.

FINANCIAL Amortization period: 15 years
TERMS AND Grace period: 4 years
CONDITIONS: (on the principal)
Disbursement period: 4 years
Interest rate: 18% (in local currency)

The interest rate to be charged on the loan will be adjusted half-yearly on January 1 and July 1, solely downward, on the basis of the Consumer Price Index determined by the Banco de la República in Colombia.

OBJECTIVES: The general objective of the project is to improve the socioeconomic situation of microentrepreneurs in the department of Chocó, especially in the city of Quibdó. The specific objectives are to: (i) strengthen the CONTIGO program (PCTGO) so as to enable it to provide efficient and institutionally sustainable financial services to microenterprises; (ii) establish an appropriate program of financial services for microenterprises in Quibdó; and (iii) analyze the feasibility of making the PCTGO independent of the organizational structure of the Corporación El Minuto de Dios (CMD) and support the process of institutional change.

DESCRIPTION: The loan funds will be used to address the credit needs of approximately 300 microentrepreneurs who operate in the city of Quibdó and the surrounding areas, by financing fixed assets and working capital. In addition, the nonreimbursable technical-cooperation funding will be used to finance the following two phases:

Institutional strengthening of the CONTIGO program, in which the following activities will be financed: (i) assistance to the CMD/PCTGO in conducting a technical analysis of the costs and benefits of making the PCTGO independent of the CMD; (ii) institutional strengthening of the PCTGO, to equip it to administer its current portfolio and, in particular, the portfolio of the project to be set up in Quibdó; (iii) development of a business plan for the PCTGO and the credit program in Quibdó; and (iv) assistance to the PCTGO in future efforts to obtain additional funds from other donors and/or sources of financing, essentially for the credit program in Quibdó.

Operational implementation of the credit program in Quibdó, in which the following activities will be financed: (i) development of credit regulations, and implementation of an appropriate credit methodology; (ii) development and implementation of an accounting and management information system (including procurement of computer equipment and software); and (iii) basic and specialized training of loan officers. The products resulting from this phase will be applicable both to the credit program in Quibdó and to the PCTGO. In addition, the funds will finance two evaluations, which will determine future disbursements for this operation.

**ENVIRONMENTAL
CLASSIFICATION:**

At its meeting of July 6, 1998, the Committee on Environment and Social Impact (CESI) reviewed this operation and made recommendations on providing training, simplifying the microentrepreneurs' access to the credit program, and including evaluation indicators broken down by gender and ethnicity. These recommendations were taken into account by the project team in the design of the present operation.

BENEFICIARIES:

Approximately 300 microentrepreneurs, of whom it is estimated at least 50% will be women.

RISKS:

The main risk of this operation is connected with the fact that recovery of loans granted with project funds may prove very difficult. This risk derives from the cultural and socioeconomic characteristics and traditional practices and circumstances prevailing in Quibdó (state paternalism, dependence on the government budget and municipal programs, limited economic opportunities, limited demand for products and services, etc.). Accordingly, an appropriate credit methodology and prudent management of the loan portfolio will be required. To this end, using technical cooperation funds, the program aims

to develop a suitable credit technology, through which it will also be necessary to provide the microentrepreneurs with solid training in areas related to the formation of "solidarity circles" (in which each person in the group is jointly and severally responsible for loan repayment) and credit management.

**THE BANK'S COUNTRY
STRATEGY:**

The country paper for Colombia (CP-1568, version of August 3, 1998) notes that part of the Bank's strategy in Colombia is aimed at reducing poverty and inequality through formation of human and social capital and the expansion of financial services and improvement of the supply of nonfinancial services for microenterprises.

**SPECIAL
CONTRACTUAL
CONDITIONS:**

It is recommended that, in addition to the general contractual conditions, the financing and technical cooperation agreement include the following special conditions:

The following are conditions precedent to the first disbursement of the loan: (i) the CMD and the PCTGO will submit the business plan referred to in paragraph 2.4 of this document; (ii) credit regulations agreed on with the Bank will be in effect; and (iii) the performance standards for the CONTIGO program agreed on by the Bank and the CMD will have been met (see paragraph 4.8).

A condition precedent to the first disbursement from the technical cooperation funds is that the CMD will have agreed with the Bank on the terms of reference for and the selection of the consultants to be responsible for the institutional strengthening of the PCTGO and the operational implementation of the credit program in Quibdó (see paragraph 4.10).

The CONTIGO program will be subject to two evaluations. The first will be performed at the CMD's request, prior to the first disbursement for the credit program. The second will be made once 25% of the credit program's funds have been committed (see paragraph 4.14).

For disbursements in excess of 33% of the credit program, evidence will have to be submitted, to the Bank's satisfaction, that the PCTGO has implemented the corrective measures agreed on with the Bank on the basis of the findings of the program's second evaluation, and that the most appropriate legal status for the PCTGO has been agreed on with the Bank (see paragraph 4.12).

The CONTIGO program will be required to maintain the real value of its assets by means of an adjustment to take account of inflation, and shall verify that the level of prices for the services to be provided with project funds is sufficient to cover the costs of such services, plus all the direct financial and operating costs. If ever this condition is not being met, the Bank may suspend disbursements (see paragraph 4.5).

By its nature, the program requires immediate availability of the technical cooperation funds. Accordingly, and at the CMD's request, the Bank may set up a revolving fund of up to 20% of the total amount of the technical cooperation funding (see paragraph 4.11).

I. FRAME OF REFERENCE

A. Macroeconomic context and the level of poverty in Chocó

- 1.1 Over the past 40 years the Colombian economy has posted average growth of 4.7%. However, there are major disparities in income levels and access to basic services for socioeconomic groups which constitute significant concentrations of poverty. ^{1/} The country is currently experiencing difficult socioeconomic circumstances, as evidenced by a high fiscal deficit, a pronounced economic slowdown and a high level of unemployment, which reached 15.8% in the past quarter.
- 1.2 The department of Chocó is considered to be the region with the lowest quality of life in the entire country. For the first half of 1998, the unemployment rate was 56%. It is estimated that the basic needs of 79% of the population are unmet, while 39% are living in absolute poverty. In addition, this region has been suffering the effects of the highest levels of violence and has become a zone of conflict between guerrilla and paramilitary groups. Afro-Colombians account for 90% of the population, while the remaining 10% consists of indigenous peoples and settlers who have moved in from other regions.

B. The microenterprise sector and the demand for services in Chocó

- 1.3 In Colombia the microenterprise sector is one of the main sources of employment, accounting for approximately 51% of all employment in the country. There are an estimated 1,200,000 microenterprises in Colombia's 10 main cities. About 80% of these microenterprises are concentrated in four major capitals, 40% of them in Bogota. Of the sector's employees, 57% are men and 43%, women.
- 1.4 The department of Chocó, located on Colombia's Pacific coast, has a population of about 430,000. The department's main urban center is its capital, Quibdó; the municipality of Quibdó occupies 13% of the department's area and has 32% of its population (138,000 people), of whom 53% are women. The unemployment rate in Quibdó is estimated at 38% and the number of microenterprises located there is around 5,000. The main difficulties these microenterprises have to contend with include lack of working capital and of access to credit. The Corporación El Minuto de Dios (CMD), through its CONTIGO credit program (PCTGO), has identified 812 microenterprises in Quibdó, of which 32% are engaged in productive activities, 40% in commerce and 28% in services. These microenterprises have shown

^{1/} It is estimated that one fourth of urban households and half of the country's rural households live in poverty. Source: Country paper, version of August 3, 1998.

interest in utilizing the PCTGO's services and represent a potential credit demand of close to US\$400,000.

C. Supply of financial services for microenterprises

- 1.5 There are no institutions in Quibdó that are providing efficient and sustainable financial services to microenterprises. Since 1993, and during recent years, the sole exception was the nongovernmental organization ACTUAR Caldas Famiempresas por Chocó, which is expected to shut down due to bankruptcy by the end of 1998. This institution found the going difficult, which is evidenced by the fact that 57% of its portfolio is in default. The reasons for this experiment's failure can be summarized as follows: (i) application of a deficient and inadequate credit methodology, in both the granting and recovery of loans; (ii) the institution's lack of identification with the local situation and no sense of ownership; (iii) weak program supervision; and (iv) lack of suitable human resources and of effective training. As a result, it is expected that the main competitor of the PCTGO will be the local moneylender, who normally charges considerably higher interest rates than those that will be applied under this project.

D. Background

1. The request

- 1.6 In May 1997 the Bank, through the Country Office, received the CMD's request for a loan under the Small Projects Financing Program for the purpose of setting up a program of financial services for microenterprises in Chocó.

2. Statement of nonobjection

- 1.7 Through letters dated September 2, 1997, and of October 14, 1998, the Colombian government, through the National Planning Department (DNP), stated that it had no objection to the Bank's participation in the financing of the program requested by the CMD.

3. Strategy of the government

- 1.8 The Colombian authorities are committed to improving the population's standard of living, in particular that of the lowest-income segments, by promoting actions in various sectors of social significance. In the productive sphere, since 1984 Colombia's National Planning Department has been implementing a national microenterprise development plan, the objectives of which are to increase microenterprise productivity and profitability and to create new jobs. To accomplish this, the plan has been offering training, administrative advisory services, credit services and assistance with marketing.

- 1.9 As a result of the execution of the plan, it is estimated that over 100 executing agencies (NGOs, financial institutions, cooperatives, etc.) participated, which provided training to 130,000 microenterprises and made loans totaling some US\$70 million. Notwithstanding the important results achieved, the coverage of the services remains low, especially in the secondary zones, which means that the population in greatest need has limited access to credit.

4. The Bank's strategy and experience in the country

- 1.10 This project responds to the special emphasis placed on microenterprise development in the report on the Bank's Eighth Replenishment, and represents a contribution to the mission set forth in the microenterprise development strategy in that it provides access to financial services for disadvantaged and low-income microentrepreneurs and promotes the development of sound and sustainable institutions able to offer them high-quality services. Moreover, the August 3, 1998, version of the country paper for Colombia (CP-1568) notes that part of the Bank's strategy will be to focus on reduction of poverty and inequality through the formation of human and social capital coupled with expansion of financial services and improvement of the supply of nonfinancial services for Colombian microenterprises. In this connection, as part of the strategy proposed in the country paper, the operation requested by the CMD is listed among the projects selected for fiscal 1998.
- 1.11 This operation also complements the activities envisaged in the Sustainable Development Program for the Pacific Coast (Pacific Plan) financed by the Bank under Loan 926/SF-CO of July 1994, an operation in an amount of US\$50 million targeting the health, education, basic sanitation and production sectors. As of August 30, 1998, 23% of the funds of this project had been disbursed and as part of the productive component agreements had been concluded with various NGOs that are currently providing training services for microenterprises. One challenge to be met by the Pacific Plan is ensuring that specialized institutions provide credit services to microenterprises. The fact is that although the Pacific Plan has funds for financing training and the studies that support the marketing of the microentrepreneurs' products, it does not have resources for financing credit.
- 1.12 In addition, over the past ten years the Bank has successfully financed three global credit operations for microenterprises. However, given the lack of formal and nonformal financial institutions with capacity to channel these in the Chocó region, it has not proven possible to funnel credit funds to the region. Another important factor in the nonutilization of these resources has to do with their high cost, which is determined on the basis of the interest rate on 90-day fixed-term deposits plus 3.5%, which would currently be equivalent to 39% per year. These terms are

considered excessively hard for undertaking credit activities in areas considered to be difficult access and high risk, such as Chocó Department. At the present time, the Bank is working on a fourth global microcredit operation, which could be launched in 1999. By strengthening the PCTGO office located in Quibdó in the provision of efficient and sustainable financial services, it is hoped that in the future it will be possible to obtain funds from the global line in order to increase the program's support for the least privileged sectors.

II. THE PROGRAM

A. Objectives

- 2.1 The general objective of the project is to improve the socioeconomic situation of the microentrepreneurs in Chocó Department, and especially that of those in the city of Quibdó. The specific objectives are to: (i) strengthen the CONTIGO program (PCTGO) so as to enable it to provide efficient financial services for microenterprises under conditions of institutional sustainability; (ii) establish in Quibdó an appropriate program of financial services for microenterprises; and (iii) analyze the feasibility of making the PCTGO independent of the CMD's organizational structure and support the institutional conversion process.

B. Description

- 2.2 The project will consist of: (i) financing of the CMD (PCTGO) for the granting of loans to microentrepreneurs in Quibdó, and (ii) nonreimbursable technical cooperation for the institutional strengthening of the PCTGO and the commencement of credit services in the Quibdó office.
- 2.3 The US\$300,000 financing will be used to finance the credit needs of microentrepreneurs located in the city of Quibdó and its environs. These funds will be used to cover their working capital needs (raw materials, inputs, small tools, etc.) and for procurement of fixed assets (large tools, equipment, machinery, etc.). Two types of loans will be granted: (i) joint loans for groups of four to six microentrepreneurs who will assume joint and several responsibility for repayment, and (ii) individual loans. It is estimated that at least 50% of the clients will be women microentrepreneurs.
- 2.4 The institutional strengthening will be designed to help the CMD develop a coherent, efficient and self-sustainable credit program. This component will be divided into two phases: (i) institutional strengthening of the PCTGO, and (ii) operational implementation of

the credit program in Quibdó. In the first phase the following activities will be financed: (i) assistance to the CMD/PCTGO for preparing a technical analysis of the costs and benefits connected with making the PCTGO independent of the CMD; (ii) institutional strengthening of the PCTGO for ensuring that it has the capacity to administer its present portfolio plus, in particular, the project portfolio to be created in Quibdó; (iii) development of a business plan for the PCTGO and the credit program in Quibdó; and (iv) assistance to the PCTGO in future efforts to obtain additional funds from other donors and/or sources of financing, basically for the Quibdó credit program. During the second phase the following activities will be financed: (i) drafting of a set of credit regulations and implementation of an appropriate credit methodology; (ii) development and implementation of a system of accounts and management information (including procurement of computer equipment and software); and (iii) basic and specialized training of loan officers. The products resulting from this phase will be applicable to both the credit program in Quibdó and to the PCTGO. In addition, these funds will be used to finance two evaluations, which will be made as specified in Chapter IV, Section F of this document.

C. Cost and financing

- 2.5 The total cost of the program is estimated at US\$700,000 equivalent, of which the Bank will contribute US\$300,000 for the financing of lending operations and US\$250,000 for financing the nonreimbursable technical cooperation. The CMD will contribute the remaining US\$150,000 to finance the administration and supervision of the credit program in Quibdó, together with the training services that will focus primarily on the training and operation of the microentrepreneur groups and developing awareness of the need for proper administration of the credit granted and how to set about this. The funds for financing the lending operation will be turned over to the CMD with the following conditions attached: repayable in local currency, with an amortization period of 15 years, including four grace years (for the principal only), and at an interest rate that will start at 18% and will be adjusted halfyearly on January 1 and July 1 of each year, downward only, in accordance with the movement of the Consumer Price Index determined by the Banco de la República in Colombia, which information will be provided by the Country Office in Colombia. The US\$250,000 for the technical cooperation on the other hand, will be nonreimbursable and will be disbursed in local currency.

III. THE INTERMEDIARY AGENCY

A. Identity, origin and objectives

- 3.1 The Corporación El Minuto de Dios (CMD) is a private nonprofit organization founded in 1958 by the late Father Rafael García-Herreros, a leading figure in social work in Colombia. Since then, the CMD's chief objective has been to promote the integral development of the poor and of poor communities through community support projects designed to generate employment, provide training, construct low-cost housing and furnish social support. Recently, starting in 1994, the CMD set up a microcredit program called the CONTIGO program, which represents a new sphere of action for the CMD. The PCTGO is run as an independent cost center by an executive director and has 19 full-time employees out of the CMD's total staff of 213.

B. Activities carried out

- 3.2 Its over 42 years experience working with poor communities in Colombia has enabled the CMD to develop varied types of programs, which include housing, health, education, care for vulnerable groups, and others. By way of background, in 1983 and as a result of an earthquake that caused considerable destruction in the city of Popayán, the Bank granted the CMD a financing of US\$500,000 equivalent (SP/TF-83-17-CO) under the Program for Financing Small Projects for the purpose of facilitating provision of housing for low-income families affected by the earthquake. The execution of this program was highly successful.

C. The CONTIGO program

- 3.3 Right from the start, the PCTGO has followed an integral approach, through which it promotes the creation and strengthening of microenterprises, socioadministrative training, and joint and individual loans, products which are granted in five of the CMD's 14 regional offices. 2/ This program has been implemented conservatively, and to date 4,991 microentrepreneurs (75% of them women) from the poorest strata have been assisted with training services and loans representing a total of approximately US\$1.3 million.
- 3.4 Financially, the PCTGO is designed to be sustainable and operates as an independent cost center. Although its loan portfolio is so far still small (US\$894,000 equivalent), the income derived from its activities covers approximately 87% of the costs. The PCTGO

2/ The CONTIGO Program only offers its services in the low-income areas of Bogota, Cucuta and Medellin.

offers individual and joint loans to microentrepreneurs and currently has a portfolio made up of 473 clients. Delinquency in this portfolio (calculated on the basis of overdue installments) stands at 7.32% for individual loans and 6.56% for joint loans. As of this time, only 4% of the loans have been granted under the joint responsibility methodology. The operating efficiency indicator for 1996 and 1997 was 15%. 3/

- 3.5 The interest rate the CMD charges on the loans is one half a point less than the commercial lending rate in the Colombian financial market; i.e. approximately 4.2% per month. The PCTGO's operating results as of December 1997 and June 1998 show losses equivalent to US\$41,524 and US\$10,281, respectively, which can be reversed by growth of the loan portfolio, application of a more efficient and better-suited credit methodology, and changes in the interest policy.
- 3.6 A year ago, the PCTGO started operations in a CMD office located in the center of Quibdó which is staffed with six employees (manager, trainer, accountant, architect and two assistants). For the moment this office only provides training services, and has to date assisted 812 microentrepreneurs (59% women), 40% of whom are engaged in commerce, 32% in productive activities and 28% in services. The experience gained has been most valuable and has enabled the office to familiarize itself with the community's customs, gain a better understanding of the market and identify potential clients for the loan program to be executed with this operation.

D. Financial position of the CMD

- 3.7 As of June 30, 1998, the CMD has total assets equivalent to US\$16.5 million, the majority of them in the form of investments (long and short term) and structures and fixed assets (including buildings, machinery and equipment), connected mainly with its housing programs. Because of its relatively recent establishment compared with the other programs, only a figure close to 5.4% of the total assets has been invested in the PCTGO portfolio. The CMD's net worth stood at US\$5.8 million equivalent and its liabilities were US\$10.8 million (see Annex II, Financial Statements 1996 - June 1998). The drop in assets from US\$22.3 million to US\$16.5 million is accounted for by three factors: (i) the effects of the depreciation of the Colombian peso; (ii) the reduction in accounts connected with housing programs (construction in progress, and other debtors) that were included; and (iii) the book losses posted at the end of December 1997 and of June 1998.

3/ Operating costs/average portfolio during the period.

- 3.8 Historically, the CMD has obtained its financing from donations from the general public, individuals, public and private institutions, and international cooperation agencies. As of June 30, 1998, the CMD's liabilities stood at US\$10.8 million equivalent, being made up as follows: advances received, basically for purchase of homes (38%); debts to financial institutions (26%); current liabilities (17%); and other liabilities (19%).
- 3.9 The CMD's Statement of Income shows that the institution posted surpluses of US\$337,000 and US\$222,000 for the 1995 and 1996 fiscal years, and losses of US\$882,000 and US\$891,000 for the periods to December 1997 and June 1998 (see Annex II). The current financial deficits are due fundamentally to the following factors: (i) the effects of the economic crisis besetting the country, which is reflected in high inflation rates and depreciation of the currency; (ii) the high financial costs assumed by the CMD in connection with its housing construction programs; and (iii) the reduction in income from donations and grants from NGOs and international agencies.

E. Institutional evaluation

- 3.10 The CMD has a good reputation and is known as one of the NGOs that is most efficient and committed in the development of Colombia's most impoverished population groups. Its long involvement in development activities and the experience it has gained through the PCTGO and its office in Quibdó provide assurance that the CMD possesses the institutional base for working toward and accomplishing the objectives proposed in this operation.
- 3.11 The following can be identified as weaknesses of the CMD: (i) low volume of operations at the level of the CONTIGO program; (ii) its Quibdó office's lack of experience in credit management; (iii) the mixing of financial and nonfinancial services; (iv) information systems and accounting and financial practices that are unsuited for administration of a credit program; (v) lack of an entrepreneurial approach in the administration of the loan portfolio; and (vi) low efficiency of the credit methodology employed.
- 3.12 In this connection, in order to ensure efficient execution of the project it will be necessary to strengthen the PCTGO, and at the same time to examine the possibility of separating it from the CMD's institutional structure so that it can develop operating autonomy and modernize its management capacity. It will also be necessary to train the PCTGO's personnel in the formulation, management and understanding of a business plan, in the application of an appropriate credit methodology, and in the use and maintenance of information systems.

IV. EXECUTION OF THE PROGRAM

A. Responsibility for execution

- 4.1 The CMD will be responsible for the execution of the credit program and of the technical cooperation, through its CONTIGO program and its office located in Quibdó.

B. The credit program

- 4.2 The credit program will be started after the technical cooperation, once the PCTGO has reached certain performance standards and is in a position to operate the credit program in Quibdó. The credit regulations will be drawn up by the CMD/PCTGO with the assistance of the consultants hired with the technical cooperation funds. The credit regulations, which will govern the execution of the program, will have to be consistent with the Bank's rules and policies and also with current Colombian legal requirements and banking and financial practices. The basic points to be covered by the credit regulations will be the terms and conditions detailed below.
- 4.3 Terms: The amortization periods will be set by the PCTGO in accordance with the characteristics of each project, taking into account the type of investment, the cash flow of the productive unit concerned and the client's ability to pay. In no case will loans for working capital be for terms longer than twelve months. The maximum term for loans for fixed assets will be 18 months. Grace periods will not be allowed for either type of loan.
- 4.4 Interest rates, charges and commissions: The interest rate charged by the PCTGO on loans granted with program funds will be positive in real terms and will be set freely by the PCTGO. The calculation to determine the rate must take into account the average inflation rate, the opportunity cost of the money, the intermediation costs (both financial and operating), the establishment of a conservative reserve for bad debts, the maintenance of the real value of the corporate capital and of the funds provided by the Bank within the framework of the financing component, and generation of a surplus to enable the capitalization of the institution.
- 4.5 Maintenance of the value of the CONTIGO program's assets: The PCTGO shall maintain the real value of its assets by means of an adjustment to take account of inflation, and ensure that the prices charged for the services to be provided with project funds are sufficient to cover these costs, plus all the direct financial and operating costs. Should it become apparent that this condition is not being met, the Bank reserves the right to suspend disbursements.

- 4.6 Amounts and limits: The debt ceiling for each beneficiary or group of beneficiaries shall take into account the total of all operations for which the beneficiary or group is responsible, and may not exceed the equivalent of US\$6,000 in Colombian currency.
- 4.7 Environmental conservation: The PCTGO shall take special care to ensure that the projects financed with program funds do not cause any deterioration of the environment, to which end the PCTGO shall take into account the Bank's preliminary guidelines for improving and environmental quality of lending operations for microenterprises.
- 4.8 Conditions precedent to the first disbursement from the financing will be: (i) that the CMD and the PCTGO submit the business plan referred to in paragraph 2.4 of this document; (ii) that the credit regulations approved by the Bank have been put into effect; and (iii) that the PCTGO has met the following performance requirements: (a) delinquent portfolio (calculated on the basis of portfolio at risk) more than 30 days overdue/gross portfolio equal to or less than 10%; and (b) administration costs/average portfolio equal to or less than 25%; and (c) number of clients per loan officer equal to or in excess of 200.

C. Technical cooperation

- 4.9 The project technical cooperation will serve to ensure responsible and efficient administration of the PCTGO and of the credit program in Quibdó. The plan of operations giving a detailed description of the components of the technical cooperation is presented in Annex I to this document. The CMD will be responsible for selecting and hiring the consultancy services required for the technical cooperation. The manager of the PCTGO, in conjunction with the manager of the Quibdó office, will be responsible for directing and coordinating the consultants' work, which shall be done in such a way that these tasks are performed in a manner that is optimal for the institution.
- 4.10 It will be a condition precedent to the first disbursement from the technical cooperation funds that the CMD shall have agreed with the Bank on the terms of reference for and selection of the consultants to carry out the institutional strengthening of the PCTGO and the operational implementation of the credit program in Quibdó.

D. Disbursements

- 4.11 The funds from the financing will be disbursed within a 48-month period counting from the effective date of the agreement. By its nature, the program requires that the technical cooperation funds be immediately available. Accordingly, and at the CMD's request, the Bank may establish a revolving fund of up to 20% of the total amount of the technical cooperation funds.

- 4.12 For disbursements in excess of 33% of the credit program, a requirement will be submission of evidence satisfactory to the Bank that the PCTGO has implemented any corrective measures agreed on with the Bank on the basis of the findings of the second evaluation of the program as referred to in chapter IV, Section E of this document, and that the most appropriate legal status for the PCTGO has been agreed on, i.e. whether it should remain attached to the CMD or whether steps should be taken to make it independent so that it can function as a separate entity.
- 4.13 During the execution of the program, the PCTGO shall take such actions as may be appropriate to ensure that the delinquency level of its loan portfolio (calculated on the basis of portfolio at risk more than 30 days overdue) connected with the program is kept below 5% of the total program. On the event of failure to comply with this requirement the Bank may suspend disbursements, though always taking due account of the occurrence of circumstances that would cause a temporary rise in the delinquency index. To this end, throughout the execution of the program the PCTGO will submit to the Bank, quarterly, information on the status of its loan portfolio, which will be reviewed in the second evaluation referred to in Chapter IV, Section E of this document.

E. Evaluations

- 4.14 The CONTIGO program will be subject to two evaluations. The first will be made at the CMD's request, prior to the first disbursement for the credit program. The second will be conducted once 25% of the credit program funds have been committed.
- 4.15 The evaluations will measure the operating and administrative efficiency of the PCTGO and of the Quibdó project, together with their solvency, the quality of their portfolios, and their results. The reports to be submitted by the CMD and the PCTGO will serve as inputs for these evaluations, which will be made by consultants to be financed with the technical cooperation funds. The findings of these evaluations will determine future disbursements for this operation.
- 4.16 The first evaluation will consider the following: (i) the institutional strengthening of the PCTGO; (ii) the preparation and relevance of the business plan; (iii) the application of the credit regulations by the PCTGO; and (iv) the meeting of the performance standards referred to in paragraph 4.8. For its part, the second evaluation will consider the following: (i) the feasibility of making the PCTGO independent of the CMD's organizational structure; (ii) the institutional strengthening of the PCTGO; (iii) the functioning of the operation in Quibdó and the degree of adherence to the business plan; (iv) the solvency and liquidity of the PCTGO; (v) the delinquency level of the PCTGO and of the project in Quibdó; (vi) the financial sustainability of the PCTGO and of the project in Quibdó; (vii) the effectiveness of the technical

cooperation; (viii) the implementation and use of a good credit methodology both for the PCTGO and for the Quibdó office; (ix) the accounting and management information system; (x) the training of the loan officers, particularly for the Quibdó office; (xi) the prospects and achievements as regards the securing of additional funds from other donors and/or sources of financing; (xii) the type of microenterprises served, and their sphere or sector of activity (including breakdowns by gender and ethnicity); (xiii) the quality of the services offered; and (xiv) the level of satisfaction of the microentrepreneur clientele.

F. Use of the recoveries and of the net surpluses

- 4.17 The recoveries from the credit activities financed with program funds will be paid back by the PCTGO into its revolving credit fund established in the city of Quibdó. During the validity of the financing agreement, the recoveries from the loans granted with program funds may only be used by the PCTGO for the granting of new loans in the Chocó zone that are consistent with the rules laid down in the financing agreement and in the program credit regulations.
- 4.18 Throughout the validity of the financing agreement, the net surpluses generated by the investments and provisions of services by the PCTGO shall be used to cover the operating costs of such activities, expand the provision of the credit services, or capitalize the new institution. Any other use of the recoveries and net surpluses shall require the prior written approval of the Bank.

G. Reports

- 4.19 Throughout the execution of the program and within 30 days of the close of each calendar year, the CMD and the PCTGO shall submit to the Bank's satisfaction a report on the progress of the program, which shall include, among other things, the financial statements of the two institutions, and detailed information on the status of the loan portfolio and the maintenance of the value of the PCTGO's assets and of the operations in Quibdó. The last of these reports shall constitute the final report and shall contain a summary of the accomplishments posted in terms of the program objectives.

H. Outside audit

- 4.20 For a period of five years, starting with the year in which the disbursements are begun and within 120 days of the close of each calendar year, the CMD and the PCTGO shall submit to the Bank their financial statements and those of the program, duly audited by an independent auditor or a firm of independent public accountants acceptable to the Bank.

V. FEASIBILITY, JUSTIFICATION AND RISKS

A. Socioeconomic feasibility

- 5.1 The execution of the program will make it possible to consolidate the microenterprise support operation conducted by the CONTIGO program and the Quibdó office. The program will contribute to the improvement of the living standards of approximately 300 households, which means that some 1,500 low-income persons will be directly benefited. A further approximately 500 persons in other regions will be benefited indirectly by the improvement in the quality and sustainability of the financial services offered by the PCTGO.
- 5.2 Moreover, the efforts to develop the financial sustainability of the project in itself will help to guarantee permanent access to these services for the target group, in a context of attractive conditions and good quality. Consequently, the success of the project will contribute to the socioeconomic progress of microentrepreneurs in Quibdó.

B. Institutional feasibility

- 5.3 The CMD has an adequate legal base and a solid organizational structure that will enable it to manage this operation. The institutional strengthening received will contribute with the development of an autonomous (possibly fully independent) management and will help to resolve at least three of the weaknesses identified: (i) the mixture of financial and other nonfinancial services; (ii) the lack of an entrepreneurial approach in the administration of the loan portfolio; and (iii) the use of information systems and accounting and financial practices that are unsuited for the administration of a credit program.
- 5.4 However, the weaknesses in financial and credit administration mentioned in paragraph 3.11 will have to be corrected if the PCTGO is to be able to execute the project efficiently and on a sustainable basis, and also to perform a more important role in the formulation and execution of similar programs in the future. It has accordingly been deemed necessary to proceed with institutional strengthening of both the PCTGO and the Quibdó office. The parallel nonreimbursable technical cooperation will provide for the contracting of specialized consultants who will work on the spot and in close coordination with the personnel of the PCTGO and of the Quibdó office with the aim of creating bases that will foster the feasibility of the operation. On the basis of the results of this operation, the PCTGO will be able to develop a track record that will enable it to secure new financings in the future, that will help both the PCTGO and the Quibdó office to develop the

economies of scale necessary for maintaining financial self-sufficiency.

C. Financial feasibility

- 5.5 The products of the technical cooperation will be fundamental instruments for bringing the PCTGO and the Quibdó office into financial feasibility. The business plan in itself, combined with the application of real and positive interest rates, should illustrate the project's financial feasibility. Application of the credit regulations and of an appropriate credit methodology will ensure a portfolio of good quality loans, a factor that will also contribute to the financial feasibility of the operation. Finally, a sound accounting and information system will enable the PCTGO to make better decisions, and this will in turn have a favorable impact on its results and those of the project in Quibdó.

D. Risks of the operation

- 5.6 The main risk of this operation is connected with the fact it is thought that recovery of loans granted with project funds may prove to be very difficult. This assessment is based on the cultural and socioeconomic characteristics of the people, coupled with the traditional practices and circumstances prevailing in Quibdó (state paternalism, dependence of the population on the government budget and municipal programs, limited economic opportunities and limited demand for products and services, etc.), which will require application of an appropriate credit methodology together with prudent management of the loan portfolio. To minimize this risk, through use of the technical cooperation funds the program proposes to develop a credit methodology suited to the local circumstances, to which end it will also be necessary to provide the microentrepreneurs with sound training in topics connected with formation of groups to be jointly responsible for loans taken out and credit management.

VI. JUSTIFICATION AND RECOMMENDATIONS

- 6.1 The operation is consistent with the policy guidelines for the Small Projects Financing Program, in that it meets the criteria laid down in documents GP-75-7 and GN-1238-2, and with the Bank's operating policy on women in development as set forth in document GP-114-3, and will directly benefit low-income groups that currently have no access to conventional sources of credit (it is estimated that at least 50% of the loan beneficiaries will be women). The project will generate employment opportunities and foster the application of appropriate technologies.

- 6.2 On the basis of the above analysis it can be concluded that execution of the proposed project is feasible. The Bank's management accordingly recommends to the Executive Directors that the respective financing be approved, for which purpose it submits the pertinent Proposed Resolution on Financing and Technical Cooperation for their consideration.

PLAN OF OPERATIONS

TECHNICAL COOPERATION CORPORACIÓN EL MINUTO DE DIOS (CMD) COLOMBIA (SP/98-03-36-4-CO)

I. BACKGROUND

- 1.1 In addition to the request for financing, the CMD submitted a request for nonreimbursable technical cooperation in support of the execution of the proposed project.
- 1.2 During the analysis of the operation, the need was detected to make independent and strengthen the CONTIGO program (PCTGO), and especially the office located in Quibdó, so that the project will be able to operate on a financially and institutionally sustainable basis.

II. OBJECTIVES

- 2.1 The objective of the technical cooperation is to help the CMD to develop a coherent, efficient and self-sustainable credit program. This component will be divided into two phases: (i) institutional strengthening of the PCTGO, and (ii) operational implementation of the credit program in Quibdó.

During the first phase the following activities will be financed: (i) assistance to the CMD/PCTGO for making a technical analysis of the costs and benefits connected with making the PCTGO independent of the CMD; (ii) institutional strengthening of the PCTGO, to give it the capacity to administer its present portfolio and, in particular, the portfolio of the project to be set up in Quibdó; (iii) development of a business plan for the PCTGO and the credit program in Quibdó; and (iv) assistance to the PCTGO in future efforts to obtain additional funds from other donors and/or sources of financing, basically for the credit program in Quibdó.

During the second phase the following activities will be financed: (i) drafting of credit regulations and implementation of a suitable credit methodology; (ii) development and implementation of an accounting and a management information system (including procurement of computer equipment and software); and (iii) basic and specialized training for loan officers. This technical assistance will be provided with a view to ensuring that, in the medium and long term, the PCTGO and the Quibdó office attain

financial self-sufficiency. The products resulting from this phase will be applicable both to the credit program in Quibdó and to the PCTGO.

- 2.2 To achieve these objectives, the CMD will contract with the Bank's go-ahead the following consultancy services:
 - a. Consultancy services in management, development of business plans for microfinancing programs and institutions, and institutional and financial policies.
 - b. Consultancy services in development and implementation of credit methodology for microenterprise credit programs.
 - c. Consultancy services in design and implementation of computerized accounting and management information systems for microfinance institutions.
- 2.3 The manager of the CONTIGO program and the manager of the Quibdó office will be jointly responsible for directing and coordinating the work of the consultants who will be hired with technical cooperation funds, so as to ensure that the work is done in an optimal manner for the project and the institution. Moreover, depending on whether it is deemed desirable for the project, the CMD and the PCTGO will have the option to hire individual consultants or a specialized consulting firm with the capacity to provide the support required for this operation.
- 2.4 Finally, the Bank will hire specialized consultancy services for performing the evaluations referred to in Chapter IV, Section E of the document.

III. TERMS OF REFERENCE OF THE CONSULTANTS

A. Institutional strengthening of the CONTIGO program

- 3.1 A specialist will be hired for a period of ten to twelve months to strengthen the PCTGO's management capacity and make the technical analysis of the costs and benefits connected with making the PCTGO independent of the CMD. This consultant will also be responsible for designing and collaborating in the implementation of a business plan setting objectives, goals, strategies and appropriate policies that will enable the PCTGO and the Quibdó office to achieve, over the medium and long term, efficient administration of the income and costs of the project such that the desired financial sustainability will be attained. Among other things, the consultant shall perform the following tasks:

- a. Study the feasibility and desirability of separating the PCTGO from the CMD and, if necessary, collaborate in the separation process. To this end, the consultant shall make a diagnostic study of the management and operating capacity of the PCTGO, and of the Quibdó office in particular, together with an evaluation of its management autonomy. The outcome of the study must reflect a clear recommendation, based on sound arguments, regarding the most appropriate legal form for the PCTGO. In other words, the consultant must be able to defend a position concerning whether the PCTGO should remain attached to the CMD or whether steps should be taken to make it independent and enable it to function as an entity separate from the CMD.
- b. Recommend the ideal organizational and operating structure for the PCTGO and the Quibdó office, that will enable efficient administration of the assets, liabilities and capital of the PCTGO and of the Quibdó office, together with the human resources connected with the operation.
- c. Develop, jointly with the executive team of the PCTGO and the Quibdó office, a business plan for the PCTGO and the Quibdó office, which will include the following, among other things:
(i) a clear vision of the mission and objectives of the PCTGO;
(ii) a projection of the financial statements of the PCTGO and of the Quibdó office (balance sheets and profit and loss statements) and of the potential sources of resources that clearly illustrates the potential of the new institution and of the credit program in Quibdó for achieving financial sustainability over the medium and long term. These projections will have to take into account macroeconomic and general operating assumptions such as inflation, growth rate, liquidity, average loan amount credit personnel productivity in terms of number of clients per officer, delinquency, average terms, interest rates, dropout rates, etc. The plan must include an appropriate marketing strategy that will make it possible to identify and select microentrepreneurs showing promise of economic viability, and shall be entirely drawn up on a joint basis and in total agreement with the executives of the CMD, the PCTGO and the Quibdó office.
- d. Prepare, jointly with the PCTGO team and the Quibdó office, a statement of general policies that will serve as basis for the administration of the PCTGO and of the Quibdó credit program. All the policies to be applied by the PCTGO in the administration of all its assets, especially those connected with the operations in Quibdó, must be set down in this document. Among others, the policies to be defined are:
(i) personnel policies; (ii) financial policy; (iii) policy on securing funds; (iv) lending policy (based on the work to be done with the consultant referred to in 2.2(b)); (v) training policies, and such other policies as are considered necessary.

These policies will serve to ensure that during the execution of the project appropriate business, management and administrative practices are adopted, and will also provide guidance in decision-making by the executive staff of the PCTGO and the Quibdó office.

- e. Prepare a plan for securing funds from other institutions, which will be designed to support the PCTGO in obtaining new resources, from both local and international financial institutions. The plan will have to be primarily aimed at securing funds for the expansion of the credit program in Quibdó, and will have to identify potential sources that are prepared to contribute to the project. The consultant will be required to propose a set of specific activities to be carried out by the PCTGO for the obtaining of funding. The consultant will also be expected to prepare a presentation document on the new institution and the program in Quibdó for use in launching future negotiations.
- f. Train the executive team and other personnel of the PCTGO and of the office in Quibdó in understanding and using the strategic planning instruments. The intention will be to organize various meetings and/or workshops with the personnel at which training will be given on organizational aspects, application of the institutional policies, administration and use of the business plan, and the execution of the plan for securing funds.

B. Development of credit technology

- 3.2 A specialist in microcredit will be hired for a period of ten to twelve months for the purpose of developing an appropriate credit technology for both the PCTGO and the credit operation in Quibdó. The methodology to be developed shall take into account the characteristics of the target population and shall seek to optimize operating efficiency, a step which should help to produce a portfolio of high quality that will be reflected in a low level of delinquency. Among other things, the consultant shall perform the following tasks:
 - a. Review and perfect the credit technology for lending to the target group. This entails designing the system for preparing client dossiers, reducing the time required for the granting of the loans to a minimum, aspects connected with the organization and precredit training of the clients, entering of the information into the computerized information system, application of the credit policies, guarantee management, etc.
 - b. Develop flexible and effective mechanisms for loan recovery.

- c. Train the loan officers, and other relevant personnel of the PCTGO and the Quibdó office, in the use of an appropriate methodology in order to maintain the loan portfolio at a high quality level. The aim will be for this consultant to work jointly and in close coordination with the other two consultants.

C. Accounting and management information systems

- 3.3 A specialist will be hired for a period of ten to twelve months to develop and implement an accounting and management information system that will enable the PCTGO and the Quibdó office to keep track of operations in general, and of credit operations in particular, providing them with timely and high-quality information for making the management decisions necessary for ensuring the sound functioning of the project. Among other things, the consultant shall perform the following tasks:
- a. Make a diagnostic study and an evaluation of the accounting and management information system used by the PCTGO and the Quibdó office.
 - b. Design the ideal solution for handling the accounting and management information requirements for the PCTGO and the Quibdó office, in such a way that it will be possible to periodically monitor the quality of the assets and of the sustainability indexes of the project.
 - c. Depending on the outcomes of (a) and (b), improve, adapt or recommend the procurement of such software and hardware as may be needed for proper and efficient administration of the PCTGO's resources and of the credit program in Quibdó.
 - d. Collaborate with the CMD and the PCTGO in the process of procuring the most suitable software and computer equipment. This procurement will have to be done in accordance with the procedures specified by the Bank.
 - e. Develop the accounting system for the generation of reports that are relevant for the new institution's decision-making.
 - f. Train the officer responsible for the systems of the PCTGO and of the office in Quibdó, and the specific users of the system, in the use and maintenance of same, taking into account the tie-in with a specialized company that will guarantee timely and adequate service of the computer systems, including those for the Quibdó office.
 - g. Prepare a manual of procedures on the management systems that are set up.

D. Evaluations

- 3.4 The CONTIGO program will be subject to two evaluations. The first will be made at the CMD's request, prior to the first disbursement from the credit program. The second will be made after 25% of the credit program funds has been committed. The evaluations will measure the operating and administrative efficiency of the PCTGO and of the project in Quibdó. Their solvency, portfolio quality and results will also be evaluated. The reports to be submitted by the CMD and the PCTGO will serve as inputs for these evaluations, which will be made by consultants to be financed with the technical cooperation funds. The findings of these evaluations will determine future disbursements for this operation.
- 3.5 The first evaluation will consider the following: (i) the institutional strengthening of the PCTGO; (ii) the preparation and relevance of the business plan; (iii) the application of the credit regulations by the PCTGO; and (iv) the meeting of the performance standards referred to in paragraph 4.8. The second evaluation, for its part, will consider the following: (i) the feasibility of making the PCTGO independent of the organizational structure of the CMD; (ii) the institutional strengthening of the PCTGO; (iii) the functioning of the operation in Quibdó and the degree of adherence to the business plan; (iv) the solvency and liquidity of the PCTGO; (v) the delinquency rate of the PCTGO and of the program in Quibdó; (vi) the financial sustainability of the PCTGO and of the project in Quibdó; (vii) the effectiveness of the technical cooperation; (viii) the implementation and use of a good credit methodology, for both the PCTGO and for the Quibdó office; (ix) the accounting and management information system; (x) the training of the loan officers, especially for those working out of the Quibdó office; (xi) the prospects and achievements connected with the securing of additional funds from other donors and/or sources of financing; (xii) the type of microentrepreneurs served, and their sphere or sector of activity (including breakdowns by gender and ethnicity); (xiii) the quality of the services offered; and (xiv) the level of satisfaction of the microentrepreneur clientele.

IV. COST AND FINANCING

- 4.1 After completion of the relevant analysis, it is estimated that the total cost of the technical cooperation will be of the order of US\$250,000 equivalent, broken down as follows:

CATEGORIES	IDB FINANCING (US\$ equivalent)
2. Technical cooperation subprogram	
2.1 Institutional strengthening of the CONTIGO program	
2.1.1 Consultant's fees	70,000
2.2 Development of credit technology	
2.2.1 Consultant's fees	65,000
2.3 Accounting and management information system	
2.3.1 Consultant's fees	50,000
2.4 Equipment	
2.4.1 Procurement of computer equipment and software	40,000
8.2 Evaluations	20,000
9.8 Contingency allowance	5,000
Total technical cooperation subprogram	250,000

- 4.2 The technical cooperation will be financed in local currency from the net income of the Fund for Special Operations (FSO), and will be furnished to the CMD on a nonreimbursable basis. The CMD and the PCTGO will provide all the logistic support necessary as regards services, office space, stationery, telecommunications services, light, etc.

V. EXECUTION OF THE PROGRAM

- 5.1 With the exception of the consultants who will make the evaluations, who will be hired by the Bank, all other consultancy services will be contracted by the CMD following the Bank's rules. The terms of reference for all the consultants and their selection shall be subject to prior express approval by the Bank.

VI. REPORTS

- 6.1 The CMD and/or the PCTGO shall provide the Bank with the following reports: (i) within 30 days of receipt of the final reports submitted by the consultants, an evaluation of same, including an opinion on the work done by the consultants, and (ii) within 120 days of the close of the calendar year in which the final disbursement is made, a financial report audited by independent auditors which sets forth how the Bank's contribution was used.

Corporación El Minuto de Dios
FINANCIAL STATEMENTS 1/
(1996-June 1998; in US\$ thousands)

BALANCE SHEET <u>1/</u>	1996	1997	June 1998
Assets	22,356	17,443	16,596
Cash, banks, temp. inv.	3,300	2,234	1,650
CONTIGO program portfolio	282	848	894
Other debtors <u>2/</u>	5,308	4,962	3,233
Construction in progress	5,730	1,459	3,034
Permanent investments	794	917	1,144
Fixed assets	6,439	6,595	6,191
Other assets	503	428	450
Liabilities	15,126	10,664	10,809
Current liabilities	2,277	1,448	1,838
Accounts w/ affiliated institutions	2,223	2,633	467
Advances received	5,002	2,436	4,119
Long-term debts to financial institutions	2,412	2,956	2,835
Other liabilities	3,212	1,191	1,550
Capital	7,230	6,779	5,787

PROFITS AND LOSSES	1996	1997	June 1998
Income from construction	1,420	2,243	367
Income from services <u>3/</u>	1,317	1,137	396
Income from rentals	423	391	207
Income from education services	406	329	147
Donations and grants	733	283	82
Total income	4,299	4,383	1,199
Management cost	1,983	3,134	568
Operating surplus (deficit)	2,316	1,249	631
Admin. and sales expenses	4,925	5,068	1,342
Other income/expenditures	2,829	2,936	-180
Total surplus (deficit)	220	-883	-891

1/ The peso/U.S. dollar exchange rates used for 1996, 1997 and to June 1998 were Col\$1,002, 1,294 and 1,363 = US\$1, respectively.

2/ Represent loans to clients for housing construction, accounts with affiliated institutions and advances to suppliers.

3/ The financial income of the CONTIGO program is posted in this item.

PROPOSED RESOLUTION

COLOMBIA. FINANCING TO THE CORPORACION EL MINUTO DE DIOS
WITHIN THE PROGRAM FOR FINANCING SMALL PROJECTS

The Board of Executive Directors

RESOLVES:

1. That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such agreement or agreements as may be necessary with the Corporación el Minuto de Dios, of the República de Colombia, to grant it, within the Program for Financing Small Projects, approved by Resolutions DE-85/78 and DE-147/79: (a) reimbursable financing for the execution of the program referred to in Document PR-____ ; and (b) nonreimbursable technical cooperation for the execution of the program, in accordance with Annex I of said document.

2. That up to the equivalent of US\$300,000, in pesos colombianos, is authorized for the purposes indicated in paragraph 1(a), and up to the equivalent of US\$250,000, in pesos colombianos, for the purposes indicated in paragraph 1(b), both chargeable to the net income of the Fund for Special Operations.