Draft
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6/1/68

Notes On Program and Project Lending in Brazil

1. The preconditions and performance standards that can be applied to project aid are more clear-cut and therefore reasonable than those that can be applied to program aid. They are more justifiable, moreover, in terms of the lending country's weight ("leverage") in the project involved: with about a 50% share in the financing of a project which, in turn, is only a certain share of gross investment and future income in the recipient-country economy, the donor is in a strong position to impose conditions about the way the project or recipient enterprise should function (rate-raising, etc.). In program lending, on the other hand, the donor country imposes conditions on the economic policy of the country with about a 10% financing of total imports, and a minuscule contribution to GNP. At the same time the seriousness of the conditions relative to the significance of the financing is much greater in the case of program lending than in the case of projects. Conditions are therefore likely to be considered unreasonable---and resisted, or sabotaged---in program lending more than in project lending.

For a project, one asks that certain changes be made, e.g., in the enterprises's rate structure, that certain complementary investments be made, that certain accounting practices be adopted. It is relatively easy to verify that such a condition has been met, and there is not much chance that forces outside the recipient enterprise's control will interfere with its compliance. With program lending, the situation is the opposite. Standards of performance---or rather, performance itself---is more of a qualitative than quantitative nature; if quantitative, the standards or goals are better drawn up as ranges of values rather than as a single absolute-value target---nevertheless, such conditions are usually expressed in the latter form. In addition, there is more room in program lending for forces outside the policymaker's control to interfere with performance. Since qualitative standards are hard to verify or to enforce, the donor country ends up resorting to quantitative standards in a situation where they really don't work. Thus the application of sanctions when standards aren't met is highly resented because the recipient-country policymakers believe they are victim of events due to forces beyond their control, and/or of the application of unrealistic measures or performance.

This point is particularly relevant to the case where recipient-country policymakers are already in agreement with the fiscal and monetary philosophy of the donor country. This case can be just as counterproductive as its opposite; that is, you, the recipient country, are vulnerable to even more A.I.D. "meddling" than the wayward country because the donor-country officials think you are "one of the boys," and therefore that you are willing to accept a highly detailed friendship involving gratuitous "technical advice" on how to reform your tax structure, how to liberalize your tariffs, etc. Moreover, because of your agreement on general principles---and because of the unworkability of the performance standards---the donor country ends up being highly demanding about small details, and more and more concerned with the "personality" aspects of the relationship ("does Delfim keep his word?", "does Campos consult us as much as he should?"). The possible problems of this harmonious relationship are illustrated by one of Delfim's exasperated comments at an A.I.D.-Finance Ministry meeting where A.I.D. officials conveyed their concern over how Delfim's stabilization program was going (it was soon after Delfim came to power). "What makes you think," he asked, "that I'm not three times as worried about the possibility of an inflationary resurgence as you are?!" In sum, the recipient country's reward for being and thinking "right" is perhaps more interference than occurs in the less well-behaved, ~~cognitive-dissonance~~ countries.)

2. The donor country is in any case likely to treat the recipient country as a banker treats his client, whether on the project or program side. I think this is more workable for a project than for a country's monetary and fiscal policy. In the latter case, there is less of a body of technical "banker's" information to rely upon for drawing up the loan preconditions and for judging performance, and there is more of a danger in erring by simply transferring developed country techniques to underdeveloped countries.

3. It is less politically costly to be involved with the "Americans" on a project loan than on a program loan. Projects already take place in the world of "deals," so that you are in a situation where the native supplier who loses may be easily

"bought off:" he can be promised the contract for another, non-foreign-financed project. In program lending, there is no way to compensate the opposition---not only because it would undermine the program which is a precondition of the lending, but because there is no way of buying the loser off outside the policy complex which buys the financing (in contrast to project lending, where the disgruntled local supplier can be bought off with the contract for another, unrelated project).

The following points have to do with unfavorable aspects of project lending, or areas in which program lending comes off better than project lending.

1. Project lending is not necessarily less "irritating" than program lending. The difference is that between alienating one top-level policymaker, or alienating ten third-level policy makers. Project lending contributes to a kind of democratization of resentment against American assistance; it reinforces the vague distrust against American assistance with many concrete experiences undergone by many persons.

Project lending is more vulnerable than program lending to manipulation by outside commercial interests (because there are many more opportunities for these outside interests to gain in project lending): for example, the type of dam recommended by an American consulting firm may have less to do with the existing local resource supply than with the alternative most agreeable to the American company that will be able to supply heavy construction equipment. Project lending, therefore, lends itself to a more strictly Marxist interpretation of American development assistance than does program lending. Whereas program lending is disliked by the recipient because of the "stupidity" or "conservatism" or "meddling" of the lending country officials, project lending, in contrast, is disliked as representing the insidious hand of the imperialist economy---and, what's worse, it appears in the guise of the helping hand.

Any outright interference in Brazilian decisions by American firms occurs through project, not program, lending. Program lending could be labeled "political" interference---- but it is the masked American-company interference that arouses the most virulent protest in the recipient country. (The Alianca para o Progresso has been dubbed the "Alianca para Negocios" by Brazilians.) There seems to be much more awareness of, and inveighing against, evidence of economic influence by American firms in the Brazilian economy, in contrast to political influence, or program-loan pressure. Perhaps because the project influence is more visible than the latter: it occurs at lower levels and probably on more frequent occasions than political or program-loan interference, and it comes to the surface in the unhideable deals that accompany the details of project lending.

Project lending, in sum, is more manipulable by, and more interesting to, outside financial interests than program lending---thereby confirming recipient-country distrust about the motives of donor-country assistance. Moreover, it is more difficult for reform-minded donor-country officials to attack this "nefarious" influence in projects than in program lending: in the former, the influence does not appear in a clear-cut policy decision, but is the way hundreds of small technical and microeconomic decisions happen to fall. Any attempts at changing the way things fall involve not changing a certain policy, but involve turning against a certain company (Brazilian or American) on a certain decision. This leads into the next point.

2. It is more difficult to prevent unwise and costly economic decisions in project lending than in program lending because in the former case, decisions are made on both sides by officials <u>not</u> involved in and not concerned with macroeconomic policy questions. At the same time that program lending involvement is demanding that the recipient country make commitments about, among other things, using more efficiently the existing productive capacity, and attacking the unemployment problem, project lending is encouraging the importation of equipment already fabricated in the country, is encouraging the undertaking of highly capital-intensive projects. Project lending, in short, tends to reinforce the underdeveloped country "extravagance" and "irrationality" that program lending is supposed to help wipe out. It undermines the "sanity" that program lending is supposed to introduce.

Project lending brings to the surface in the most graphic way some of the serious economic problems of the country---unemployment due partially to a capital-intensive industrialization, excess capacity in the capital goods industry, scarcity of domestic financing in relation to international financing---but before the eyes of those who are <u>least</u> concerned with economic repercussions. That is, project officials on both donor and recipient sides of the loan are entrepreneurial and banker types, not economists or economic policymakers, the adverse economic aspects of a particular project's structure do not have a repercussion in their financial analysis. It is not that project officials are behaving wrongly; as entrepreneurs, they cannot be expected to act like policy-making economists. It is, rather, that the project-lending process falls into the hands of the financial, rather than the economic, analyst. The result is that important opportunities to witness the form in which economic problems appear, and to attack them---thereby providing a truly valuable technical assistance---are being lost. Serious misallocations of resources therefore take place through project lending, simply because those who are concerned with such problems, who have the training to deal with them, and who have the power to impose decisions, are not involved in the project-making process. They are too high up.

Program lending officials---though perhaps misguided---are more susceptible to economic reasoning, because that is the business of their type of "project." Indeed, when the structure of a proposed project implies serious economic costs, it is easier to reach the ear of the uninvolved program-lending people than of those directly involved with the project. If the project is financially sound, then the project people are impervious to suggestions of change on economic grounds; the program people, on the other hand, can be aroused with the argument that the physiognomy of the project is bound to <u>undermine</u> the performance demanded of the recipient country under the program loan (this is not as exaggerated a possibility as it may seem, because most dollar project lending goes to large capital projects that have a significant repercussion in the recipient-country's economy).

This point perhaps comes closer to being a reformer's guide to strategy within an aid-giving organization, rather than a substantive difference between project and program aid. But it does demonstrate the fact that program lending, in theory, requires more "lofty" considerations than project aid. If program aid fails, it is due to misguided interference and general ignorance, as well as the cumbersomeness of the aid-giving mechanism; if project aid fails, it is due to the unavoidable accessibility of private interests to the aid-giving process. The former failure is due in great part to the mediocrity of the donor-country administrators; the latter failure is due to the <u>structure</u> of the aid-giving process, which is too "pedestrian" and microeconomic to include the development economist or economic policymaker.