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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

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REPORT AND RECOMMENDATIONS OF THE PRESIDENT  
TO THE EXECUTIVE DIRECTORS  
CONCERNING A PROPOSED LOAN FOR  
SOUTHERN ITALY DEVELOPMENT PROJECTS

February 18, 1958

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

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1. I submit the following report and recommendations with regard to a proposed loan in an amount in various currencies equivalent to \$75 million to the Cassa per Opere Straordinarie di Pubblico Interesse nell'Italia Meridionale (Cassa per il Mezzogiorno) for the purpose of financing ten Southern Italy development projects.

PART I - HISTORICAL

2. The program for the development of Southern Italy was drawn up in 1950. Originally a 10-year program, it has been extended, first to 12 years and more recently to 15 years, i.e., to 1965. Over the 15 years about \$3.2 billion will be invested in the effort to raise the standard of living in that part of Italy lying south of Rome and including the islands of Sicily, Sardinia and Elba. The governmental agency charged with carrying out this program is the Cassa per il Mezzogiorno.

3. The Bank has already made loans aggregating \$164.6 million to the Cassa per il Mezzogiorno. Their status on January 31, 1958, is given below (in millions of dollars):

| <u>Year</u> | <u>Amount</u>              | <u>Repayments</u> | <u>Outstanding</u>      |                       |
|-------------|----------------------------|-------------------|-------------------------|-----------------------|
|             |                            |                   | <u>Held by the Bank</u> | <u>Held by Others</u> |
| 1951        | 10.00                      | .46               | 9.44                    | .10                   |
| 1953        | 10.00                      | -                 | 10.00                   | -                     |
| 1955        | 68.40 <sup>1/</sup>        | -                 | 62.40                   | 6.00                  |
| 1956        | 74.63 <sup>2/</sup>        | -                 | 73.63                   | 1.00                  |
|             | <u>163.03<sup>1/</sup></u> | <u>.46</u>        | <u>155.47</u>           | <u>7.10</u>           |

4. Members of the staff visited Italy in the fall of 1957 to bring the Bank's evaluation of the economic position up to date, to assess the impact of the Cassa program on the economy of the South, and to study on the spot projects which could serve as the basis for a loan. Negotiations were completed in Washington in February 1958. The proposed loan would complete the series of loans to the Cassa inaugurated in 1955 as a result of the request of the Italian Government for a loan of about \$200 million.

PART II - DESCRIPTION OF THE PROPOSED LOAN

5. The purpose of the loan would be to aid the development of Southern Italy by providing financing for a selected group of industrial, power and irrigation projects. All the industrial projects are privately sponsored. One power project will be carried out by a publicly controlled and the other by a privately owned power company, and the irrigation projects will be carried out directly by the Cassa.

<sup>1/</sup> Allowing for \$1.60 million cancelled.

<sup>2/</sup> Including \$900,000 not yet effective.

6. The main characteristics of the loan would be as follows:

|                           |  |
|---------------------------|--|
| <u>Borrower:</u>          | Cassa per Opere Straordinarie di Pubblico Interesse nell'Italia Meridionale (Cassa per il Mezzogiorno) |
| <u>Guarantor:</u>         | Republic of Italy  |
| <u>Amount:</u>            | The equivalent in various currencies of \$75 million   |
| <u>Amortization:</u>      | In 35 semi-annual installments, commencing on February 15, 1961, and terminating on February 15, 1978  |
| <u>Interest rate:</u>     | 5-1/2%, including 1% commission  |
| <u>Commitment charge:</u> | 3/4 of 1% per annum  |
| <u>Disbursement:</u>      | Related to expenditure on the projects after September 1957  |

PART III - LEGAL INSTRUMENTS AND AUTHORITY

7. The loan documents consist of the following:

- (a) Loan Agreement (No. 1);
- (b) Guarantee Agreement (No. 2); and
- (c) two Project Agreements (Nos. 3 and 4).

8. The loan set-up and the Loan Documents are similar to those of the last loan (150 IT) and, similarly, reflect the differences from the typical single project loan made directly to the enterprise which is to operate the project. These differences include:

- (a) Ten projects are described in Schedule 2 to the Loan Agreement. The specific amounts of the loan allocated to each project are listed in Schedule 4 to the Loan Agreement. Section 3.01(b) provides that these Schedules may be changed by agreement between the Bank and the Borrower.
- (b) The Loan and Guarantee Agreements may become effective and may be cancelled, and withdrawals from the Loan Account may be suspended, separately with respect to each project and the amount of the loan allocated thereto. Separate Closing Dates with respect to the various projects may also be agreed upon between the Bank and the Borrower.

- (c) The documents provide for the proceeds of the loan in the power and industrial sectors to be relent (under arrangements satisfactory to the Bank) to the enterprises which will be the ultimate beneficiaries.
- (d) For each power project there will be a Project Agreement with the beneficiary enterprise. These are Societa Meridionale di Elettricit  and Societa Generale Elettrica Della Sicilia. Societa Finanziaria Elettrica Nazionale per Azioni ("Finelettrica") and Societa Italiana per le Strade Ferrate Meridionali ("Bastogi") will be additional parties to each Project Agreement, guaranteeing performance of the Agreement and agreeing to become sureties for the performance of all obligations (including financial) of the power company to the Borrower.
- (e) In Section 2.02 of the Guarantee Agreement the Guarantor agrees to cause the Irrigation Projects to be completed and properly operated and to take such action as shall be required to assure that no use, other than for potable purposes, will reduce the amounts of water available for irrigation purposes on the Irrigation Projects below the amounts needed therefor.

#### PART IV - APPRAISAL OF PROPOSED LOAN

9. A study of the projects is contained in the "Appraisal of Italian Industrial, Power and Irrigation Projects" (TO 162)(No. 9). This study may be summarized as follows:

##### The Projects:

- 10. Industry: The \$29,360,000 provided for the industrial projects would finance 43% of the cost of six plants. Three of them, which account for more than 85% of the amount proposed, would be in Sicily; the other three are on the mainland. Two of the Sicilian projects and part of the third one will exploit extensive deposits of potash newly discovered on that island. They will add extensively to Italy's industrial potash fertilizers and basic chemicals. The three smaller projects on the mainland include a new plant for the production of ready made clothing and additions to existing plants which will produce electrical appliances and electrolytic tin plate.
- 11. Power: The \$29,200,000 to be provided for power would finance about 60% of the cost of a 300,000 kw plant to be built at Naples and a hydroelectric pumping plant in Sicily with a generating capacity of 60,000 kw. These, when completed, will add 14% to the then existing generating capacity in the Cassa area.
- 12. Irrigation: The \$16,440,000 provided for irrigation would be divided between two irrigation projects on the southern mainland: \$10 million would provide about 17% of the cost of the Fortore project on the north side of the Tavoliere Plain on the east coast of Italy; \$6,440,000 would provide about 27% of the cost required to complete the Volturno project on the west coast of Italy between Rome and Naples. These projects

will result in the irrigation of 66,000 hectares of land in the Tavoliere plains and 43,000 hectares on both sides of the lower Volturno river.

Procurement:

13. For the industrial projects, various methods of procurement have been employed. Much of the equipment will be bought on the basis of competitive bids. In some cases, machinery and equipment have been obtained under licensing arrangements; in others, branch plants are being built by northern Italian firms which have long established arrangements with suppliers. For the SME project, orders were placed on the basis of international bidding. Gibbs and Hill, a New York consulting firm, will assist in the design and layout of the plant. For the SGES project bids have been received from both Italian and foreign manufacturers for major pieces of equipment. Orders have not yet been placed. For the irrigation projects only local labor and materials will be used, and bids are let on a negotiated basis under Cassa supervision.

Disbursement:

14. As in loans 117 IT and 150 IT, the proposed loan will be disbursed against evidence of expenditure in lire on individual projects. This expenditure will be mainly for locally produced goods and services and it was therefore not possible to tie disbursement to specific imports. The loan will thus provide foreign exchange to meet the cost of imports arising indirectly out of the Cassa program. The Bank will decide the particular currencies to be disbursed in the light of the currencies available to the Bank at the time of disbursement.

Justification of the Loan:

15. The Bank has now followed the growth and development of the Cassa and its program for a period of seven years. The attached report (No. 7) "Cassa per il Mezzogiorno and the Economic Development of Southern Italy" (EA 80) records the solid accomplishments of this period. By Italian legislation in 1957, new resources have been provided for the Cassa, its life has been extended to 1965, and by a shift in emphasis toward industrialization new goals have been set for it. Its impact on the economic life of Southern Italy, and indeed that of all Italy, has been remarkable.

16. Already 57,000 hectares have been provided with irrigation facilities out of a total program of 352,000 hectares, although the large irrigation projects for which the Bank has lent money are still under construction. Two thousand eight hundred km of rural roads have been built and 10,600 km of provincial roads improved. Twenty three thousand farm homes have been built and 621 new agricultural processing plants have been established. New aqueducts bring potable water to 2.7 million people in 572 villages. These and related investments have cost \$1 billion. An additional \$350 million of Cassa funds has directly or indirectly supported new industrial investment, increasing industrial employment in the Cassa area by 12% and value added by manufacturing by about 26%. In human terms, these figures mean the creation of 20,000 full time jobs in industry and 35,000 in agriculture.

17. Since 1950, a general improvement in the economy has taken place throughout Italy. In the North the existence of an established industrial complex with idle capacity, a pool of skilled labor and markets near at hand all favored economic expansion. That a comparable improvement has taken place in the South is attributable to the investments made directly and indirectly through the Cassa. In fact, the growth of agricultural production in the South has exceeded the national average and industrial growth has kept pace with it, and the results from current investment have still to appear. Cement production, with help from the Bank, has grown at double the national rate. Housing construction, power consumption, use of fertilizers and tractors, all indices directly related to the Cassa's program, have grown faster than in the North. During the life of the Cassa, income in the South grew by 71% as compared with 64% for the North, and this is reflected in higher consumption and savings.

18. This loan would complete the assistance to the Cassa program requested by the Government of Italy in 1954. Although domestic resources available in Italy for investment continue to grow, I believe that maintenance of the present level of investment in a non-inflationary manner requires external assistance.

Prospects of Fulfillment of Obligations:

19. The report on "Current Economic Position and Prospects of Italy" (EA 81) (No. 8) shows that real national income has continued its post 1950 rise of 5% per annum through the past two years. This growth has permitted simultaneous increases in consumption, savings and investment with a concomitant fall in unemployment. Agriculture suffered from the effects of bad weather during the past two years, but manufacturing, construction and service industries have all expanded rapidly. In 1957, for the first time, more people were employed in manufacturing than in agriculture. Public finances are sound and price stability has been maintained.

20. Exports have increased and so have earnings from invisibles. But imports have increased faster, in large part due to heavy imports of capital goods, and increased needs of industry for imported fuel and raw materials. United States aid and capital inflow have more than offset current account deficits and foreign exchange reserves have therefore increased. They now stand at \$1,300 million, higher than ever before.

21. Italy's debt record is good. Service charges on her external debt are relatively small. Annual debt service in 1956 was less than 4% of global foreign exchange earnings and this percentage will diminish rapidly after 1963. Italy is a good risk for the proposed loan of \$75 million.

PART V - COMPLIANCE WITH ARTICLES OF AGREEMENT

22. I am satisfied that the proposed loan complies with the requirements of the Articles of Agreement of the Bank. A report of the Committee provided for in Article III, Section 4, paragraph (iii) of the Articles of Agreement of the Bank is attached (No. 5).

PART VI - RECOMMENDATIONS

23. I recommend that the Bank at this time lend to the Cassa per Opere Straordinarie di Pubblico Interesse nell'Italia Meridionale an amount in various currencies equivalent to \$75,000,000 for a term of 20 years with interest, commission and commitment charges and on such other terms as are specified in the attached draft Loan and Guarantee Agreements, and that the Executive Directors adopt a resolution to that effect in the form attached (No. 6).

Eugene R. Black

Washington D. C.  
February 18, 1958