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Operations Evaluation Group

OEG *Findings*

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Evaluation of the Mekong Project Development Facility (June 4, 2002)

Nexus Associates, a consulting firm based in Belmont, Massachusetts, conducted this 2002 study for the Operations Evaluation Group of the International Finance Corporation (IFC)) and on behalf of the donors funding MPDF. This is one of four evaluations of individual SME facilities that are part of an overall study of IFC's facilities. IFC's Operations Evaluation Group (OEG), an independent unit that reports to IFC's Board of Directors, is responsible for the post-evaluation function within IFC. OEG's work aims to: (i) help provide accountability for achievement of IFC's objectives; (ii) identify lessons from past experience for improving IFC's operational performance; and (iii) help reinforce corporate objectives and values among staff.

Small and medium sized businesses in Cambodia, Laos and Vietnam have potential for growth. But their momentum has been slowed in part by the difficulty of accessing long-term capital, inadequate business planning, and limited management skills. On the one side, businesses seeking capital often cannot document their prospects and risks in a way that instills confidence. On the other side, lending institutions face collateral requirements, interest rate ceilings, intolerance towards risk and their own shortage of capital. Informal networks of private investors--sometimes relatives--remain a primary source of needed capital.

The International Finance Corporation (IFC) and other donors established the Mekong Project Development Facility in 1996 to tackle these problems. They provided more than $18 million in funding for MPDF during the 1996-2002 period. The MPDF has two fundamental missions, classified as "Part A" and "Part B." Part A programs, company advisory services, help small and medium businesses prepare business plans that can be presented to financiers and helps them in approaching financiers. MPDF also provides their clients with advisory services on how to better operate their businesses. Part B of MPDF, development of business support services, seeks broader changes as it aims to build the capacity of organizations to provide services for small and medium businesses. It focuses on intermediary organizations such as lending institutions and universities or other training organizations. Its vision is that these organizations will be able to deliver these services on a sustainable basis.

Some MPDF activities under Part B include:

- Producing a series of workbooks on how to manage a business.
- Developing a management training curriculum.
- Training banks in loan analysis.
- Establishing a venture capital fund, the Mekong Enterprise Fund.
- Developing papers on promoting private sector development in Vietnam, Cambodia, and Laos.

The IFC and donor organizations are currently considering future support for MPDF. They requested the independent evaluation that is described here in brief. This summary highlights the evaluation findings. The full 107-page report, based on program records, 60 in-depth interviews and 170 completed client surveys, is available with appendices at www.ifc.org/oeg.

Part A

Part A activities are based on the premise that financial institutions in Vietnam, Cambodia and Laos are more likely to provide long-term financing for companies when given reliable information about them. MPDF assists businesses in properly and rigorously compiling that information so as to provide answers to the classic questions of any potential investor: What exactly does the business do? What is its market? Where does it fit within its market? What is its record of past performance? What are its financial projections? What is its strategy going forward? What's the risk? All of this is addressed in a prospectus MPDF helps managers to prepare with the help of outside consultants. Once it's completed, MPDF officers often participate in meetings with bank officials to review the documents and discuss the loan application.

In the course of working with the businesses, MPDF officers have learned a great deal about their general management needs. They leverage this knowledge by providing advisory services not directly tied to raising capital. Some clients just receive these advisory services as stand alone services. So far, these services have focused on marketing, business operations, management information systems and certification for management system standards (ISO 9000.)

Well Ahead of Projections

MPDF's level of activity is well ahead of the projections contained in the 1996 IFC Board report. As of December 31, 2001, MPDF had completed 96 financial advisory projects and 13 technical assistance projects, with completion defined (in the case of investment-related services) as the signal from a financial institution that it intends on providing financing to the MPDF client. MPDF had helped raise $40.2 million in financing commitments for 96 projects. Study findings indicate companies subsequently secured approximately 70 percent or $28 million. Another $18 million had been raised for the Mekong Enterprise Fund, established at MPDF initiative and described below.

MPDF clients are primarily private, locally-owned and run, small and medium-sized enterprises (SMEs), concentrated in manufacturing. More than 90% of the clients had annual sales of $5 million or less when they started working with MPDF. Appropriately, most were rapidly growing companies planning expansions to meet expanding demand for their products.

Satisfied Clients

The evaluation team's survey of Part A companies indicated that the vast majority were interested in obtaining financing rapidly and on more favorable terms. About two-thirds said that they came to MPDF, at least in part, because they needed help in preparing financial projections, in structuring project financing, and/or in preparing the application to the bank. The vast majority (82%) said they were satisfied or very satisfied with the assistance they received. The survey suggested that some of those less satisfied often came to the process with unrealistically high expectations about the terms of the financing they might get. MPDF needs to better manage client expectations.

The evaluation team examined some of the financing documents prepared with MPDF's help and found that some were still not sufficient for lenders to make well informed decisions. Some also made only passing reference to potential risks in their documents.

A Genuine Need

Could these companies have raised money as easily and rapidly on their own? Two-thirds thought not. They said that MPDF helped them obtain financing that they would not have been able to obtain on their own under any circumstances, or enabled them to obtain financing fast and/or under more favorable terms and conditions. Indeed, the survey conducted for the evaluation showed that many had sought financing unsuccessfully for the same projects before approaching MPDF. It was not only the improved documentation that helped the companies. The very participation of MPDF appeared to serve as an imprimatur. One bank official in Vietnam said that MPDF assistance made credit committees feel more "assured that the loans make sense." An official in Laos thought that MPDF involvement was reassuring. The "bank trusts MPDF and IFC and believes the projects must be good," he said.

However, one-third of the companies believed that MPDF made no difference to the financing that they were able to secure for the project. They explained that they were already bank customers with established relationships. And two-thirds of respondents said they would have gone ahead with the project even if they had not been able to obtain bank financing. Most of these said that they could have gotten the money from relatives or equity investors but, they acknowledged, only in a way that would have delayed their projects, reduced its scope or increased the costs of obtaining the financing.

How much difference did MPDF technical assistance make to these companies? Quite a lot. Most reported that the technical assistance provided by MPDF prompted them to develop or improve products and services, and/or institute new practices. But the true test is whether these changes actually improve performance. Sixty eight percent thought that MPDF helped them improve their performance in terms of planning, quality management, human resource management, and/or environmental management. And, over half attributed increases in their net profits or annual sales to changes they made in their businesses as a result of MPDF services.

The experience of one Vietnamese manufacturer is illustrative. This manufacturer needed financing to expand production facilities as well as help in revamping operations and identifying new markets. MPDF arranged for three consultants to advise the company. The assistance enabled the company to take advantage of increased demand, particularly in Europe, and significantly increase its sales from exports.

MPDF Finances

MPDF was not intended to be financially self-sustaining. But it does try to cover some of its costs, which include salaries and benefits for a staff of 52. For financial advisory services, clients are asked to pay a nominal fee of $100 at the outset and, upon obtaining financing, a "success fee" of 1.5 percent of the financing arranged by MPDF. MPDF, however, has been charging less than the1.5percent. MPDF is collecting roughly 4.8% of the total cost of services, well below the original projection, which envisioned that MPDF would generate roughly 10% of total costs. (MPDF's accounting does not allow MPDF to determine the costs of providing services to individual clients. This should be corrected.)

Part B

As Part A tries to make businesses better borrowers, Part B tries to help other organizations develop or strengthen services that serve small and medium-sized businesses. Its aim is to help develop the infrastructure needed for a vibrant private sector. The evaluation focused on five Part B programs on which either considerable resources were expended and/or that MPDF management believed had the most significant development impacts.

Working to Improve Banks

One such program works with banks, primarily through training, to make them better lenders. As of December 31, 2001, 27 courses had been offered with 826 participants from 55 banks. MPDF's initial foray in bank training was not as successful as it would wish. At MPDF's request, Planters Development Bank of the Philippines conducted an independent assessment in 1999 of MPDF's Loan Analysis Training package. The quality of the courses was high, it concluded, but there was "too much emphasis given to financial appraisals…inappropriate to the real situation obtaining in Vietnam, given the absence or inadequacy of financial records." MPDF shifted gears in 2000 to broaden its course offerings to include other subjects deemed important by bank officials. And in 2001, it helped establish the Bank Training Center—a limited liability company with ten joint stock banks as shareholders. This also has led to significant growth in training courses in customer service, human resources, and management.

Spreading Management Knowledge

MPDF has developed a management training curriculum aimed at managers of small and medium-sized companies. While the curriculum covers many subjects also addressed by other training programs, it is unique to the region because of its strong basis in participatory learning using case studies drawn from Vietnam. As of December 31, 2001, 128 courses had been taught at 16 institutions serving over 3000 participants from 1000 companies. A survey conducted as part of the evaluation, found companies employing students were highly satisfied with these courses. Responding companies reported that the training produced better trained, more highly motivated employees. These managers brought about change and improved profitability directly as a result of their training, companies reported. Other, non-partner institutions are now using the MPDF curriculum and/or training approach. There is some doubt about the sustainability of the specific training programs being offered by the partner institutions given increased competition in the market, including competition among institutions using the MPDF curriculum and other organizations that offer free courses fully subsidized by international donors.

Best-selling Workbooks

To further expand the reach of management training, the MPDF commissioned a series of workbooks in 1999 called "Teach Yourself Business Management." Twelve titles have been published since May 2001 and the local language versions are good sellers in Vietnam, with a total of 37,114 sold as of Mid-February 2002, and in Cambodia, with 7,000 sold. Some are being used in classroom training in Vietnam and Cambodia. Total revenues from sales are about $59,000. The evaluation did not obtain more specific information on impact of the workbooks.

Mekong Enterprise Fund

Institutional risk capital is uncommon in the region and the level of investment remains fairly low. To address this issue, MPDF has helped establish a new fund, the Mekong Enterprise Fund, to provide risk capital to small and medium-sized businesses. As of April 2002, the MEF had secured $18 million, from the Asian Development Bank (the lead investor), the Nordic Development fund, the State Secretariat for Economic Affairs of Switzerland, the Finnish Fund for Industrial Cooperation Ltd. and private investors. MPDF will serve as "investment advisor," receiving a fee of 0.5% of committed capital per year. The average investment is expected to be about $500,000 in 25 to 35 firms, but no investments had yet been made at the time of this evaluation so it is too early to judge the likelihood of success. The fund manager plans on working closely with portfolio companies to strengthen their management capabilities and improve their chances for success.

Spreading the Word

Over the past five years, MPDF issued 12 reports on private sector development in Vietnam, Laos, and Cambodia. Evaluation findings indicate that the reports have been well-regarded by those who read them, particularly those that are based on company surveys. Users report that the series contributed to the policy debate within the World Bank Group and government bodies.

Overall Conclusions and Recommendations

Overall, the evaluation found that MPDF was filling an important gap, serving and serving well the needs of the class of enterprises it was established to assist. The level of activity has surpassed expectations. Clients are satisfied and boast concrete results from involvement with MPDF. The advice provided through the program has prompted businesses to make what they consider positive changes. The rationale for the program remains valid.

There are a number of areas needing improvement.

Clarify the Target Population

With the help of its donors, MPDF should clarify its target population, especially for Part A services. The bulk of the firms in the region (about 70,000) have annual sales of less than $5 million and assets greater than $100,000. MPDF cannot serve them all. Who should receive its subsidized support? MPDF should consider not merely the size of potential clients but also need. That is, it should be asking whether a potential customer is able to secure needed capital on its own.

Know the Customers

MPDF should develop its capacity to conduct full needs assessments of individual companies. This information should guide MPDF's business with the individual firms and also help it determine what new programs are needed that it might foster.

Reconsider Pricing

MPDF should reconsider its pricing policy. Prices charged for services should be based on the principle of full cost recovery unless there is a clear rationale for subsidization. It should consider developing a sliding fee schedule based on the ability of companies to pay. Also, donors should set a target for the percentage of total expenses that MPDF should be expected to get from client fees; MPDF then needs to develop a business plan for how it intends to achieve the target.

Integrate Services

While MPDF has taken steps in this direction, more should be done to integrate company advisory services (Part A) and business support services (Part B.) In addition to making cross-referrals, MPDF should use the work that it does with companies under Part A to inform and support activities undertaken under Part B, and use Part B to build capacities to deliver services to individual companies under Part A. For example, the companies assisted in Part A might make excellent case studies for the training programs of Part B. And training institutions could be involved in the delivery of services directly to Part A clients.

Coordinate Activities

MPDF should identify opportunities to participate in efforts coordinated across donors to address specific country needs, especially for strengthening local banks and training institutions. For example, in order to address institutional weaknesses in the banking sectors of Vietnam, Cambodia and Laos, MPDF should coordinate the Bank Training Center with efforts of the Asian Development Bank, the World Bank Group and others.

Increase advocacy

Working closely with its donors and the World Bank, as well as IFC, MPDF should consider a broader role in seeking to improve the business environment in Vietnam, Laos, and Cambodia.

Strengthen Reporting

The evaluation revealed a number of weaknesses in the collection and reporting of data by MPDF. MPDF needs to address deficiencies in systems used to track staff time, establish and maintain unified information systems, address deficiencies of cost accounting systems, and provide annual audited financial statements. It should also establish explicit definitions for performance measures..