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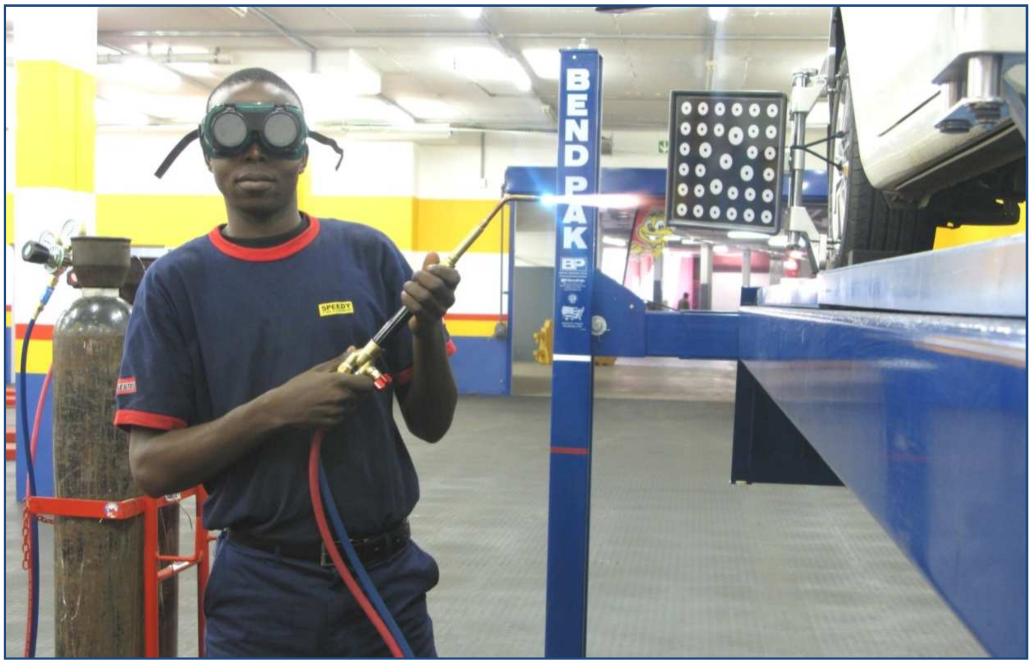

FINANCIAL SECTOR PROGRAM

ANNUAL WORKPLAN OCTOBER 2010 – SEPTEMBER 2011

October 2010

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ANNUAL WORKPLAN OCTOBER 2010 – SEPTEMBER 2011

Contract No. 674-M-00-08-00043-00

CONTENTS

ACRONYMS

AIPSA	Association of Insolvency Practitioners of South Africa
BA	Banking Association
BDS	Business Development Services
BDSP	Business Development Services Provider
BEE	Black Economic Empowerment
BSO	Business Support Organization
BSSA	Business Skills for South Africa Foundation
BUSA	Business Unity South Africa
CCRD	Consumer and Corporate Regulation Division of dti
CIPRO	Companies and Intellectual Property Registration Office
DCA	Development Credit Authority
DCA ODC	Development Credit Authority Office of Development Credit
DFI	Development Financial Institutions
DOJ	Department of Justice
dti	Department of Trade and Industry
EDC	Enterprise Development Centre of ABSA bank
FABCOS	Foundation for African Business and Consumer Services
FI	Financial Intermediary
FNB	First National Bank
FSP	Financial Sector Program
GSA	Government of South Africa
HDE	Historically Disadvantaged Enterprise
IBA	Institute of Business Advisors
ICSB	International Council for Small Business
IDF	Identity Development Fund
IFC	International Finance Corporation
IIB	Institute for Independent Business
INSOL	International Association of Restructuring, Insolvency & Bankruptcy Professionals
IPPC	Intellectual Property Protection Committee
IRBA	Independent Regulatory Board for Auditors
JEF	Johannesburg Equity Fund
KM	Knowledge Management
LOI	Letter of Intent
MOE	Ministry of Economics
MOF	Ministry of finance
NCA	National Credit Act
NCR	National Credit Regulator
NRCA	National Register of Credit Agreements
NBSC	National Small Business Chamber
NSBAC	National Small Business Advisory Council
OCIPE	Office of Companies and Intellectual Property Enforcement
OMM	Old Mutual Masisizane
POF	Purchase Order Financing
RGA	Raizcorp Guiding Academy
RFF	Royal Fields Finance
SAIBL	USAID South African International Business Linkages project
SAICA	South African Institute of Chartered Accountants
SAIPA	South African Institute of Professional Accountants
SEDA	Small Enterprise Development Agency
SOW	Scope of Work

SME	Small Medium Enterprise
TIGF	Thembani International Guarantee Fund
USAID	United States Agency for International Development
USG	United States Government

EXECUTIVE SUMMARY

The Financial Sector Program (FSP) seeks to expand access to financial services and lower financing costs for small and medium enterprises[1] (SMEs) through reforming the legal and regulatory framework affecting the financial sector and business environment and improving the commercial viability of lending to historically disadvantaged SMEs in South Africa, thereby expanding SME access to a range of high quality and affordable financial services. The contract was awarded to the Chemonics consortium on May 22, 2008.

This third annual work plan covers the period of October 1, 2010 through September 30, 2011 and details planned activities to support the four project components – SME finance, SME bankability, business enabling environment and knowledge management.

Building on its progress with partner financial intermediaries[2] (FIs) thus far, FSP will continue to expand and deepen its assistance to FIs to diversify and expand their **SME finance** portfolios. Given the tumult in the South African financial sector due to the global financial crisis, many banks were in a period of retrenchment – consolidating their portfolios and tightening their approaches to risk management thereby diminishing their interest in exploring new market segments. This led FSP to initially pursue specialized lending partners and pilot new products in anticipation of ramping up these demonstration efforts in Year 3. With the economy slowly emerging into a recovery mode, FSP is well-poised to assist larger financial institutions expand their SME lending efforts armed with targeted financial products, such as purchase order finance, invoice clearing, equipment term loans, and leasing; streamlined credit delivery processes; and loan guarantee schemes such as USAID's Development Credit Authority facilities to mitigate the risk of entering new SME lending sectors. With FSP assistance, ABSA bank is already piloting new SME-focused purchase order finance and invoice clearing products which will be fully rolled out in Year 3. Through new product launches, FSP is demonstrating to the industry that SME finance is not only viable, but profitable and worthy of significant investment by a growing pool of SME-friendly sources of financial services. In fact, a competitive process is underway to develop similar products with new FIs this year. FSP's second year saw the award of DCA portable guarantee facilities to three South African FIs – Mettle, Spartan, and True Group -- targeting specific SME subsectors. In Year 3 FSP will support these FIs to utilize their guarantees to expand their SME portfolios. Project staff will help to build partner capacity to develop better credit evaluation mechanisms and streamline procedures to reach a wider pool of SMEs and increase the additionality of the guarantee to the extent possible. Finally, FSP will explore new DCA LPG opportunities with FIs interested in penetrating the SME market.

While the SME finance component addresses the supply side constraints of the FIs another supports the demand side of finance by improving **SME bankability**. Banks and other FIs often complain about the financial literacy and financial management expertise of their SME clients and cite it as a significant hindrance to expanding their SME portfolios. In an effort to make SMEs more creditworthy, FSP will build the capacity of business development services provider (BDSPs) to improve the quality of finance-related business development services (BDS). Building on a major initiative designed in Year 2, FSP will pilot a BDSP industry

[1] For the purpose of this program, an SME is defined broadly as a business engaged in activities generating annual turnover between R200,000 and R25,000,000. This definition was based on the pending Financial Sector Charter definition proposed and agreed to by the Banking Association and its members.
[2] Financial Intermediary is defined herein as any organization engaged in the provision of financial services, be it a bank, non-bank credit provider or a private financing fund.

standards program through a private sector partner, Raizcorp. Raizcorp will grade BDSPs to ensure SMEs are receiving high quality finance–related business development services from qualified providers leading to a better return on their investment. Where BDSP skill and financial literacy deficits exist, FSP through its partners will provide mechanisms for BDSP capacity building, including the roll out of an innovative web-based resource called *finfind*[3] with a local host institution. *finfind* is designed to promote the understanding and knowledge of SME finance providers and help link SME clients to appropriate financial products offered by specific FIs. It will link the BDS provision directly with the FIs' product delivery, helping SMEs understand the inherent value in BDS and gain practical financial management advice and secure appropriate financial products that ensure sustainable business growth. This process will also see that FIs receive finance applications that are well supported and more easily bankable. Additionally FSP will institutionalize its SME cash flow management courses with other partner business development service organizations (BSOs) and FIs making SMEs more attractive clients for FIs.

An **enabling policy environment** that fosters cost effective delivery of financial services, as well as well-functioning enterprises is essential for economic growth. FSP supports public and private sector partners in the policy reform process to develop solutions to identified obstacles. Assistance can be provided at any stage of the process – from preliminary policy analysis and public –private dialogue facilitation to legislative drafting assistance and capacity building during policy implementation. FSP's applied research agenda mirrors key policy issues affecting the business and financial sector operating environment. In Year 3, this will include building on Year 2's analysis of the financial sector policy framework to foster options for stimulating reforms, completing a comprehensive review of the insolvency policy framework and its impacts on businesses and FIs, proposing a roadmap for revamping the system of SME statistical monitoring, analyzing South Africa's competition policy and its progress toward creating a "level playing field," and reviewing the National Credit Act to evaluate its impact since it came into force. FSP will also contribute to select institutional reforms within the Department of Trade and Industry (dti) and National Credit Regulator (NCR). Previously, FSP supported the drafting of the new Companies and Intellectual Property Commission (the Commission) business case, and in Year 3 the project will continue assistance to the dti's team to produce the associated Companies Act Regulations and complementary fee structure for the Commission. Following up on the insolvency framework, FSP will recommend actions to harmonize the new Companies Act's rescue provisions with the National Credit Act and Insolvency Act. Finally in a continuing effort to promote evidence –based policy making, FSP will support the government's efforts lead by the National Treasury to introduce a Regulatory Impact Assessment (RIA) methodology to analyze costs and benefits of policy actions both before and after implementation.

FSP's final component is a cross-cutting intervention to improve the **knowledge management** of SME finance data, finance opportunities, successful approaches to SME development, donor and government programs, and tools for FIs and BDSPs to use in SME capacity building efforts. The goal is to develop a "community of practice" linking SME finance practitioners and clients and introducing best practices from around the world. The Financial Sector Blog (www.fsp.org.za/blog) forms a key conduit for information exchange on shared experiences and lessons learned. Each year FSP expands its pool of collaborating partners and in Year 3, anticipates significant increase in information exchange via the blog and numerous partner events and forums through the year.

[3] FSP is in the process of registering the *finfind* name as a trademark

SECTION I: INTRODUCTION TO THE FINANCIAL SECTOR PROGRAM

A. Contract Background

The Financial Sector Program (FSP) is a USAID/Southern Africa-financed program awarded to Chemonics International on May 22, 2008 under the GSA Contract GS-23F-0127P and USAID Blanket Purchasing Agreement EEM-E-00-05-00006-00; provided for under USAID task order 674-M-00-08-00043-00. This award had a base period (30 months) with an option period (30 months), which was exercised on June 22, 2010. This project will now conclude May 21, 2013. The total cost of the contract was originally $14,297,997 however in 2009, a modification was finalized increasing the contract to $14,497,997 to support an additional technical element.

FSP was designed to support the accomplishment of the U.S. Government's Economic Growth Objective in South Africa. This program is one of three main vehicles to promote vibrant growth of historically-disadvantaged small and medium enterprises (SMEs) and reduce unemployment and poverty — generating rapid, sustained and broad-based economic growth in South Africa.

Chemonics Consortium

Prime:
- Chemonics International Inc.

Subcontractors:
- Crimson Capital
- Shorebank Advisory Services
- Khulisa Management Services

The objective of FSP is to expand access to financial services and lower financing costs for small and medium enterprises (SMEs), primarily those historically-disadvantaged, through reforming the legal and regulatory framework affecting the financial sector and business environment and improving the commercial viability of lending to SMEs in South Africa. The ultimate result is to mitigate market credit risk leading to increased SME access to a range of quality, affordable financial services.

This annual work plan builds on the partnerships established and successes seen in the first two years of the project and covers the period October 1, 2010 through September 30, 2011.

B. Operating Environment and Approach

South Africa is Africa's largest economy, with strong financial, legal, energy, communications, and manufacturing sectors, abundant natural resources, and a thriving tourism industry. Yet underneath South Africa's developed economy lies a "second economy," comprised mostly of poor, historically-disadvantaged communities. A legacy of Apartheid, this second economy can be seen in the townships and outskirts of South Africa's cities and in rural areas where large numbers of the population live in informal housing with little to no access to electricity, transport, or modern water or sewage systems.

FSP will actively engage in activities which will help to integrate this second economy of historically-disadvantaged groups into South Africa's larger economy and specifically assist SMEs fulfill their critical roles as drivers of the economy. Activities under FSP will focus on improving and expanding financial services and products; managing and mitigating financial risk and transaction costs; improving bankability of SMEs and business services by linking financial services with business service activities that can build SME capacity, productivity and competitiveness, as well as improve the capacity of financial advisory services to serve SMEs; support the emergence of an efficient credit industry regulator that promotes an enabling environment for financial intermediation and risk management, and boosts the private sector's role and participation in the provision of financial services to SMEs; promote reforms to commercial laws, regulations, and administrative practices affecting the private sector and SME development; and, improve knowledge management through an accessible repository of information and analysis about SMEs and finance in South Africa.

As any project progresses, its operating environment – economic, and political, regulatory realities – continuously evolves often impacting planned activities and proposed partnerships. For FSP, each of these realities presents challenges, but also opens up new opportunities. Unfortunately, at a point to coincide with the launch of FSP in June 2008, the money supply, credit approvals and business confidence level began a free fall. The business confidence survey results illustrated below reflects the deteriorating levels of optimism that people who run companies had about the performance of the economy and how they felt about their organizations' prospects over the last five years. Following relatively consistent high faith in economic conditions, South African businesses, as in most countries, lost significant business confidence as the global financial crisis unfolded in late 2007. Following a slight recovery in September 2009 probably related to the anticipated gain from the 2010 World Cup, the trend unfortunately reversed itself again in May of 2010 and has continued to decline.

The challenges to launching an SME access to credit program and expecting immediate results in such an environment are obvious. Program assumptions and delivery mechanisms needed to be swiftly adapted to turn market challenges and obstacles into development opportunities.

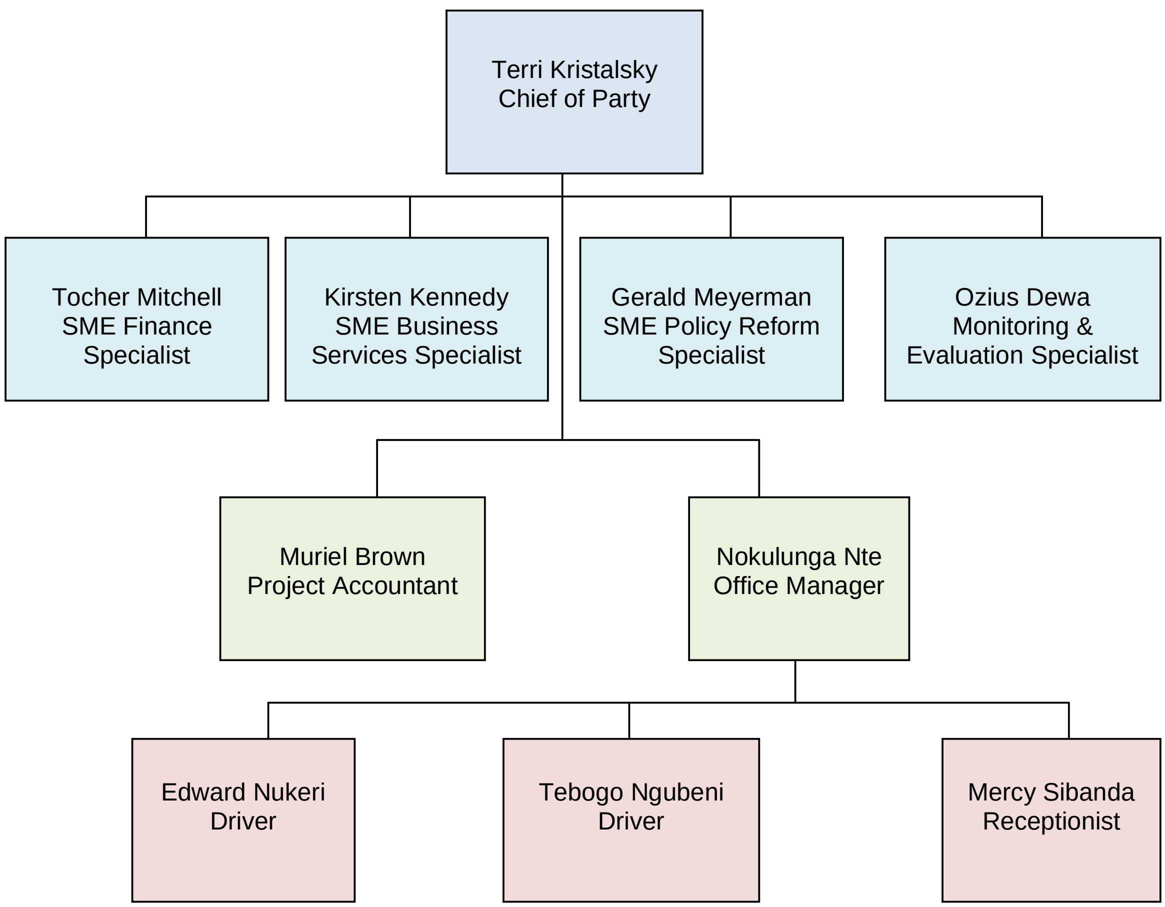
Since the beginning of FSP our major focus and point of contact with the Government of South Africa (GoSA) has been the *dti*. This Ministry is responsible for the drafting of most business laws, including the Companies Act and Regulations, the Close Corporations Act, Real Estate legislation as well as the National Credit Act and oversight of the NCR. The Economic Development Department (EDD) now oversees both macro-economic and micro-economic policies. More than ten areas have been identified, ranging from industrial policy, competitiveness, and access to and the cost of capital for businesses. It has also taken over direction and management of three economic regulatory bodies, the Competition

Commission, the Competition Tribunal and the International Trade Administration Commission; and three development finance institutions namely Khula Enterprise Finance Limited; the South African Micro-Finance Apex Fund and the Industrial Development Corporation. This will require that FSP establish new relationships with the EDD staff in areas of its mandate offering a new opportunity to forge productive relationships.

Within this operating environment, FSP is undertaking a four-pronged approach to increase SME access to a range of quality, affordable financial services to facilitate business growth and catalyze increased employment and incomes:

1) Improve financial intermediaries' capacity to serve SMEs in South Africa
2) Improve the "bankability" of SMEs
3) Reform the legal and regulatory framework affecting the financial sector and business environment stimulating SME growth
4) Strengthen the SME finance knowledge management system.

C. FSP Program Team -Exhibit 1



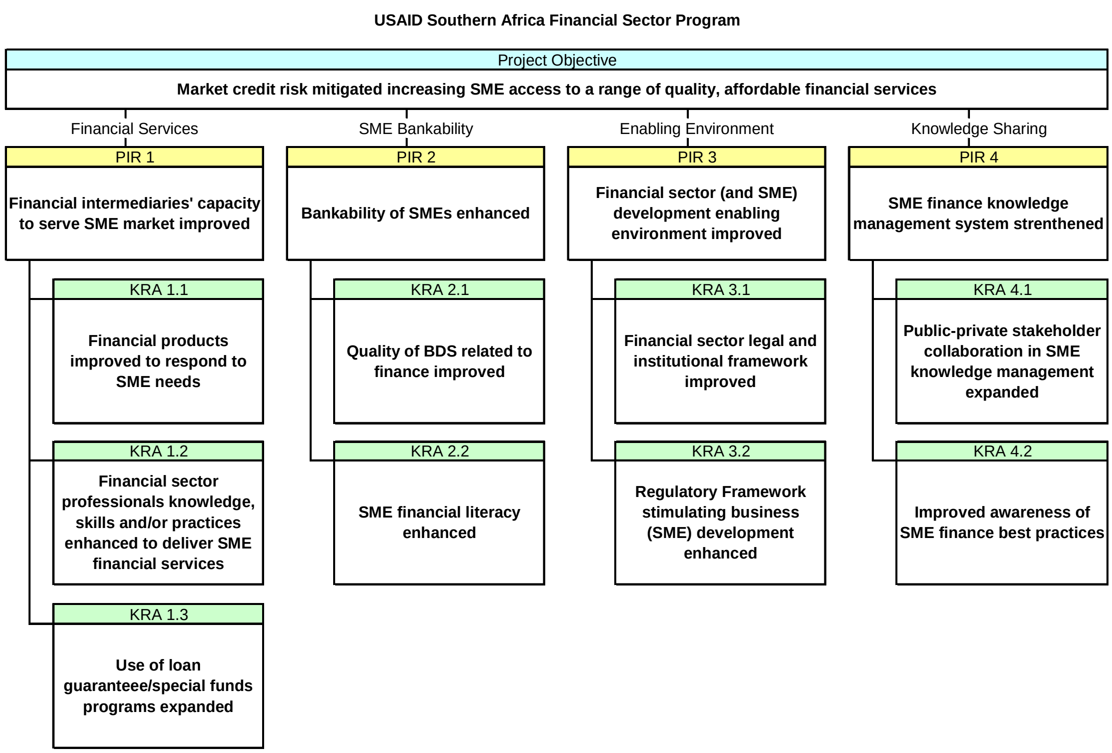
Staff change: During Year 2, FSP replaced the Monitoring and Evaluation Specialist. Ozius Dewa, joined the team in June 2010 and was presented with a new M&E monitoring and analysis tool that reduces the margin for errors in data input and generates detailed reports by indicator.

D. FSP Results Framework

FSP has been designed to support the achievement of the U.S. Government Economic Growth Objective in South Africa. This program contributes to the objective to help improve SME access to a range of quality, affordable financial services. Within the Economic Growth objective, FSP helps to mitigate market credit risk increasing SME access to a range of financial services (see Exhibit 2, Results Framework).

The results from each level of the framework support the achievement of the results on the level above – culminating in achieving the Mission Economic Growth objective of increased access to finance by SMEs. For each of the four Project Intermediate Results (PIRs), FSP has elaborated Key Result Areas (KRAs) that are representative of the overall strategies for achieving the intermediate results. These KRAs guide project staff in their activity planning and provide the basic structure for performance monitoring, evaluation and reporting. Each KRA has a technical leader, a set of activities, associated tasks, defined resources, and benchmarks for this interim work plan. These are detailed in the text in Section II and activity sheets and timelines in **Annex A**.

E. FSP Results Framework – Exhibit 2



SECTION II: WORKPLAN BY TECHNICAL COMPONENT

A. Project Intermediate Result (PIR) 1: Financial Intermediaries' Capacity to Serve SME Market Improved

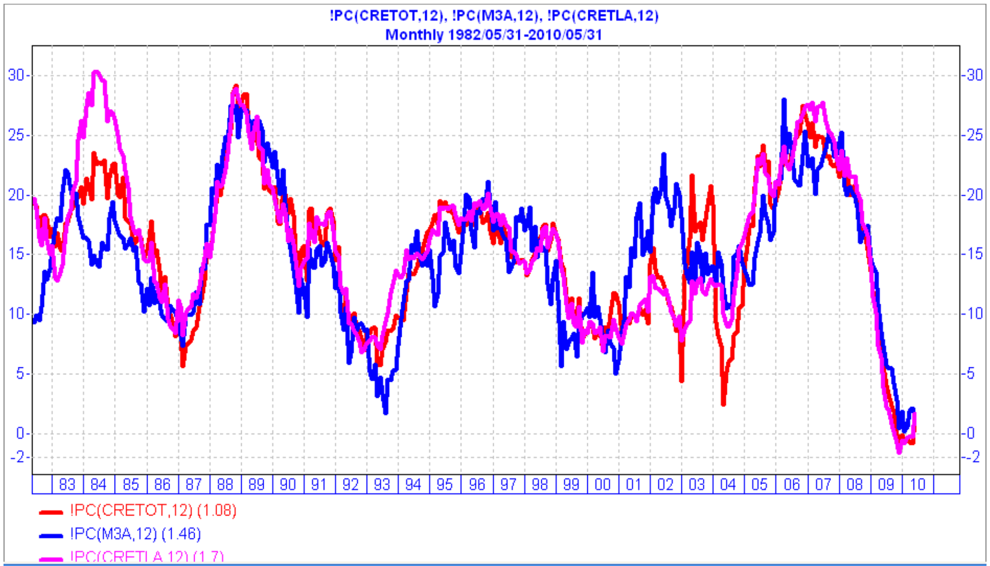
The primary objective of PIR 1 (SME finance component) is to increase the supply of SME finance and improve SME access to finance primarily by improving the capacity of South African financial intermediaries (FIs) to provide financial services to SMEs in an efficient, innovative and cost effective manner in response to market needs. South African FIs have traditionally addressed the finance needs of large corporate businesses and more recently micro-enterprises. However, there remains a significant gap in meeting the financing needs of SMEs, particularly those considered historically disadvantaged enterprises, now classified as such under the government's Black Economic Empowerment Program[4] (BEE). Although there is significant demand for finance from SMEs, few of these firms successfully access credit through the formal financial sector. Many SMEs lack traditional forms of collateral typically required by financiers. SMEs often appear less transparent, possess limited financial literacy and expertise, with many presenting poorly prepared loan applications and lacking credible/audited financial statements. Further, the line of demarcation between individual/personal assets and business assets can often be indistinguishable.

FIs are therefore challenged to develop assessment mechanisms, financial products and credit policies/procedures designed to address those perceived business inadequacies and heightened risks. By taking such actions, FIs can enjoy a large, often untapped potential for expanded intermediation. FSP's goal is to make the "business case" for SME lending, detailing the potential market and then assisting FIs with adapting their current systems, policies and procedures to accommodate these new clients.

When FSP began, it was envisaged that the finance component would work primarily through the country's Banking Association and with South Africa's "big four" banks: ABSA, Nedbank, FNB, and Standard Bank. However, FSP was launched as the global financial crisis was unfolding, so the environment for expanded lending, especially to the perceived riskier SME sector, faced resistance from those banks. During the initial years of FSP, the big banks concentrated primarily on protecting their balance sheet positions, resulting in postponement of their SME credit expansion plans. The only exception was ABSA bank, which worked with FSP in the development and cautious launch of new, contract-based loan products for SMEs.

According to Reserve Bank and Financial Services Board data, extension of credit in South Africa dropped sharply over the course of 2008 and 2009 (see chart below). It has barely begun to recover in 2010. The overall recession, significantly lower money supply, lower loan demands, tighter credit standards imposed by lenders (thereby reducing the supply of credit) and enactment of the National Credit Act, resulted in a much more highly regulated credit market and the exclusion of borrowers deemed to have reached their "credit ceiling," many of whom are SMEs.

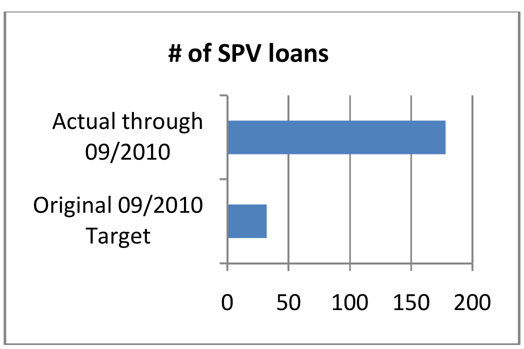
[4] A BEE enterprise is defined as an SME that has more than 25% unfettered black ownership or shareholding. Under the codes, 'black is defined as South African citizens with the following ethnicities: black Africans, coloreds, Indians and Chinese.

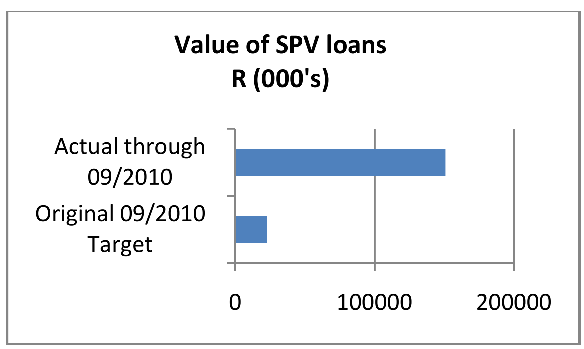


The blue line in the above graph represents the M3 money supply; red represents *total* credit in the South African economy; pink represents *total* loans and advances. The vertical scale shows growth rates. Data shown is through May 2010. Sources: Reserve Bank, FSB.

In the face of these obstacles, in Years 1 and 2, FSP pursued a dual approach: 1) continuing to make the business case for expanded SME lending to all financial institutions with limited breakthrough among the "big four" banks thus far succeeding with only ABSA while; 2) reaching out to smaller financial intermediaries, namely smaller banks (e.g., SASFIN, WIZZIT), finance companies (Blue Financial Services), and special purpose vehicle (SPV) private funds such as Royal Fields Finance (RFF) and those established by Old Mutual, Barloworld, and Pretoria Portland Cement. Given their development objectives, these SPV funds, RFF and Blue had not pulled back from SME lending and were receptive to FSP technical assistance. FSP therefore approached these FIs to demonstrate the SME finance opportunities available that would in turn ramp up their SME lending as the effects of the financial crisis eased.

By working with smaller but committed FI partners, despite the poor macro-economic conditions prevailing over the last two years, FSP dramatically exceeded its SPV loan targets (see charts below).





In addition to this, the proportion by number of all FSP FI partner loans going to black-owned businesses has been high, at 73%, supporting a key project objective to help mobile funding to historically disadvantaged entrepreneurs.

While the SPV lending has been an encouraging trend, going forward into Year 3 and beyond FSP has revised its SME finance component strategy to narrow its focus, using a tiering process reducing the total number of key FI partners to seven. Tier 1 partners provide for greater potential to scale up SME lending — a key impact indicator for project success. Tier 1 partners include two of South Africa's biggest banks[5] which, despite the country's sluggish economic recovery, at this point are deemed willing to venture into the SME new product markets in a structured manner with FSP's support. Royal Fields, the only SPV in Tier 1, is a specialized contract financier that exclusively targets black owned SMEs. They are a nimble, young and ambitious FI with tremendous potential in FSP's core target market and have shown consistent growth. FSP will also focus efforts on all four DCA Guarantee partners: Blue, Mettle, True Group and Spartan, who are all likely to generate substantial results and serve distinct and underserved market segments.

Assistance will be considered on a case by case basis to Tier 2 FIs, with whom FSP will maintain regular but less frequent contact. Support will be provided on an ad hoc basis and subject to performance improvements, these four FIs may be considered for additional technical support.

FSP has decided not to have further engagement or receive further reporting from four of the original fourteen partners after the current Letters of Intent expire in December 2010 either because their results and impact are minimal and/or because further engagement is not feasible.

FSP Finance Component Partner Tiers

Tier	Attributes	FI Partners	Level of Engagement
1	Large, national footprint Highly likely to generate good results and impact; Expressed interest in new product development, Focus on BEE SMEs	ABSA Standard Bank* Mettle Spartan True Group Blue Financial Services, Royal Fields Finance	Targeted technical assistance Monthly monitoring
2	Some potential for good results and impact Limited impact from previous technical support Good BEE SME profile	Grofin, Old Mutual Masisizane, Identity Development Fund, Thembani International Guarantee Fund	Ad hoc onsite assistance Quarterly monitoring
3	Not sufficiently receptive to SME finance technical assistance Negligible impact Movement away from SME credit	PPC Ntsika, Barloworld Siyakhula, Sasfin, WIZZIT	Suspended support

*potential partner

The key elements of PIR 1 strategy in Year 3 will be new loan product development and the facilitation and promotion of DCA guarantee facilities. FSP anticipates that these activities will generate significant results and have the biggest impact in improving SME access to finance. The degree of success will increase exponentially with improvements in economic and credit market conditions.

Three Key Results Areas (KRAs) support PIR 1:

KRA 1.1: Financial products improved to respond to SME needs

[5] FSP has had a working relationship with ABSA bank for the last two years. Standard Bank submitted an EOI to develop a new SME-focused loan product with FSP assistance.

KRA 1.2: Financial sector professionals' knowledge, skills and/or practices enhanced to deliver SME financial services

KRA 1.3: Use of loan guarantees/special funds programs expanded

Each of these KRAs is detailed in the following pages in terms of its overall strategy, key activities, implementation resources/partners and expected results/impact. Specific tasks and timings are indicated on the timelines that follow the text in Annex A.

KRA 1.1 Financial products improved to respond to SME needs

KRA Strategy:

Key to improving SME access to finance is to offer products that meet the needs of SMEs. This may seem obvious, but in fact for the most part, the South African banks have, up to now, offered the same loan products to SMEs as to large corporate clients, e.g. overdrafts and investment term loans (for equipment and vehicles) using the same process of evaluation. However, SMEs more often than not need financing tailored for specific transactions with an eye toward modifying the approval process to take into consideration the lower level of business sophistication and collateral available with most SMEs. Therefore, FSP's strategy for this KRA is to assist its FI partners to develop and implement loan products that will meet the specific financing needs of SMEs such as purchase order financing (POF), invoice clearing (IC), factoring, warehouse receipts, asset based finance, and leasing.

There is keen interest among South African banks in further developing these products, especially POF, as evidenced by the pilot effort underway with ABSA bank. Of course, development of a new product is ineffective without complementary technical assistance in creating appropriate risk analysis tools, risk management systems and proper marketing targeted to the new sector. Overall, development of more suitable financing products will broaden the SME finance market and increase access to finance.

PIR 1 Benchmarks

- ABSA POF and IC loan product review undertaken
- 4 new or refined loan products designed
- Mettle equipment term loan designed
- 1 new loan product opportunity identified
- 3 finance processes improved
- Financing for all 3 approved DCA portable guarantees achieved
- 1 completed DCA LPG concept paper

Activities:

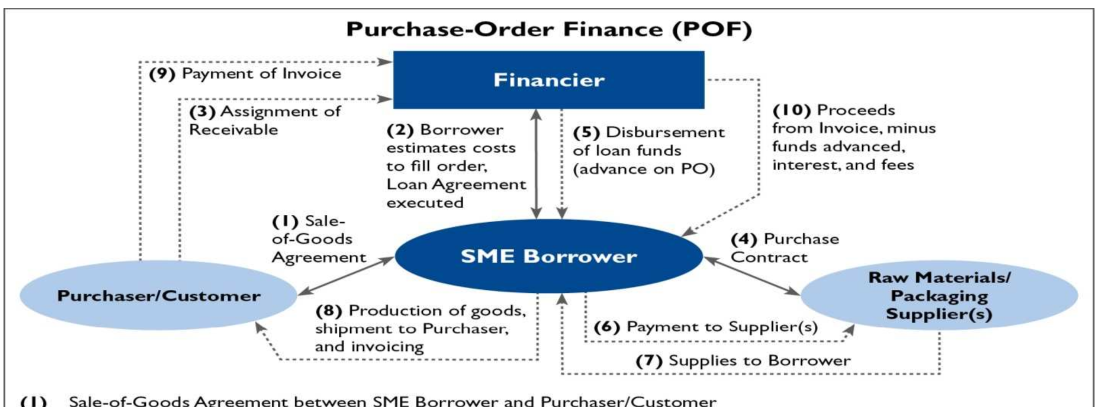
1.1.1 Improve ABSA's POF and IC loan products. FSP previously worked with ABSA to develop POF and IC loan products. ABSA launched the two loan products in September 2009, and volumes have grown slowly but steadily through 2010. ABSA now intends to introduce both loan products in the medium and large size business units of the bank in addition to the small business division with which FSP works. In Year 3 FSP will assist ABSA as it further refines the POF and IC loan products and will assist the bank to promote and disseminate information about the POF and IC products by facilitating linkages between them and BSOs at information sessions where ABSA, potential SME borrowers and BDSPs are present. ABSA's loan volume for these products has reached nearly 15 loans per month. By the end of the third year, FSP expects exponential growth in the number and value of these loans.

1.1.2 Develop POF and IC loan products with other FIs. South African FIs are now showing keen interest in developing POF and IC loan products. Given the demand, suitability and general unavailability of these products in South Africa, FSP places high priority on their development in Year 3. Consequently, at the end of Year 2 FSP began a competitive process to identify suitable POF partners. FSP's familiarity with South African FIs allowed firstly the compilation of a shortlist of ten FIs to whom Requests for Expressions of Interest (REOIs) would be sent. Near the end of September, FSP sent the REOIs to the ten FIs to assess their interest in receiving FSP technical assistance to develop the POF and/or IC loan products. Five FIs (Standard Bank, WIZZIT, Blue Financial, Mettle and Royal Fields Finance) indicated that they would submit detailed proposals for assistance by the end of October 2010.

Following proper evaluation, FSP will assess and select the best candidates with the greatest possibility for successful broad outreach and provide technical assistance to develop POF and IC loan products over the course of Year 3. Tasks will include helping the FIs to develop screening mechanisms for loan applications, drafting or making appropriate refinements to credit evaluation policies and procedures, developing tracking systems for these types of loans, designing the products, training loan and credit officers in their use, and facilitating

What is POF?

A "Purchase Order Finance" (POF) loan product is suitable for an SME that has an order in hand for a product or service. The tenor of a POF is tied to the SME's production and collection cycle (typically 30 – 270 days depending on sector, product/service cycle, and credit terms for the customer), which limits the SME borrower's interest expense. A traditional overdraft loan by contrast, not being related to the production cycle, could end up being open ended, unnecessarily increasing interest expenses. The lender advances loan proceeds directly to the SME's suppliers. The SME produces and ships the goods or delivers the service and issues the invoice to the customer. Under POF financing, arrangements are made for the SME's customer, once invoiced, to pay the bank directly. When the customer pays, the lender is repaid the advance plus interest and fees. These loans are self-liquidating and the SME only pays interest for the number of days it really needs the money. The POF cycle can be repeated over and over as the SME gets more orders. An "Invoice Clearing" (IC) loan also is possible, whereby the lender makes a loan to the SME only when an invoice is issued to the buyer/customer. When a bank makes an IC loan it removes the need for the SME borrower to wait for the duration of the credit terms it has provided to the customer.



(1) Sale-of-Goods Agreement between SME Borrower and Purchaser/Customer
(2) Borrower estimates costs of filling and shipping order. Loan Agreement is executed between Financier and SME Borrower for needed amounts (advance on PO)
(3) The PO/Receivable is assigned to the Financier to secure the loan
(4) Purchase Contract between SME Borrower and Supplier(s) of raw materials, packaging, and other goods/services needed to produce/ship order
(5) Financier disburses loan (advance on PO) to SME Borrower
(6) SME Borrower pays Supplier(s) (payment in advance is frequently required for SMEs and/or for discounts)
(7) Suppliers provide necessary goods and services to SME Borrower
(8) SME Borrower produces goods and ships to Purchaser/Customer; issues Invoice payable to Financier
(9) Purchaser/Customer pays Invoice to Financier
(10) Financier pays proceeds from paid Invoice to SME Borrower, minus the loan funds (advance), interest, and fees

information sessions and consultative processes for interested parties, e.g. potential SME borrowers, BSOs, BDSPs, regulators, corporate customers of SMEs and other stakeholders. Initial feedback from the FIs indicates there is potential to generate at least an incremental 100 POF and IC loans per month

1.1.3 Develop Equipment Term Loan Product for Mettle (DCA partner). Mettle is one of three FIs for which a DCA Portable Guarantee facility has been approved. Funding supported by USAID DCA guarantees will be used by Mettle for the financing of panel beaters (auto body shops). Initially the loan financing will be in the form of factoring of the panel beaters' accounts receivable due from auto insurance companies, financing in which Mettle has specialized since its founding.

The "additionality[6]" for this DCA facility includes the expansion and development of two new loan products; short term financing for vehicle spare parts (a form of POF), which Mettle already provides to a very limited extent, and up to three-year term loans to finance purchase of equipment (such as spray paint booths) for panel beaters. Mettle's factoring of receivables helps the panel beaters meet their short term working capital needs, while the provision of equipment term loans will take financing to another level. The acquisition of equipment enables the panel beaters to expand their operations and thereby increase their volumes and increase staffing.

After an initial period during which Mettle will utilize the DCA guaranteed loans for expanding factoring operations, FSP will help Mettle develop the equipment term loan product, train Mettle staff in how to conduct due diligence for this type of lending, and help promote the new product through consultative processes with BSOs, BDSPs, and potential SME clients. Mettle currently has approximately 600 registered factoring clients. Introduction of the equipment term loan product to this client base has the potential to provide a significant economic impact in terms of investment, sales growth and employment.

1.1.4 Develop or refine other finance products. In line with the strategy for this KRA, FSP will explore possibilities for development of other finance products that are more suited for the needs of SMEs. It is notable that even the "big four" banks concede that their approach to SME lending, including the loan products in their offerings, needs to be amended. During the joint FSP-Banking Association workshop held in May 2010, which was intended to identify initiatives to bridge the demand and supply gaps identified in surveys FSP conducted earlier, the General Manager of ABSA's Small Business division admitted that the traditional collateral which big banks demand (real estate and life insurance policies), and the whole approach they use for SME lending, was not working and needed to be re-examined. FSP will undertake evaluations to build a business case for alternative products better suited to SME finance as opportunities arise.

One possibility for an alternative financing product is leasing. Some SMEs might not be able to afford the down payment that outright purchase of equipment requires. The leasing alternative removes the need for a large down payment and the monthly lease payments can be tailored to better accommodate an SME's cash flow. Leasing is widely available in South Africa to finance the acquisition of vehicles, but not so much for other kinds of equipment. A key mechanism in increasing SME access to finance, in Year 3, FSP will assess the feasibility of such products in the South African market. FSP will assess the interest in these products

[6] Factoring is a type of financing whereby the financier purchases (at a discount) an account receivable and then collects it.

among FIs, determine current availability, and examine any legal, regulatory and infrastructure challenges. If the outcome of this research indicates there is a favorable environment, FSP will issue an REOI and conduct a competitive bidding process with interested FIs, as it has done in connection with development of the POF loan product. FSP will then commence developing the products with the selected FIs. Aside from leasing, warehouse receipt loans[7] and asset based financing are other possible types of products that might be investigated.

KRA 1.2 Financial sector professionals knowledge, skills and/or practices enhanced to deliver SME financial services

KRA Strategy:
While KRA 1.1 will promote new products, there are other opportunities for enhancing existing products by improving the policies and procedures governing their use. The activities in this KRA aim to streamline the FIs' loan approval processes and simultaneously improve the capacity of their staff, resulting in an increase in the number and amount of loans made without sacrificing portfolio quality.

Primarily, it is FSP Tier 2 FIs that need this kind of assistance, but even the loan and credit officers of the "big four" banks could benefit from refinements to their approach. They tend to treat SME loan applications as they would those of large corporate clients, when the approach to SME credit evaluation needs to be different. Aside from the need for special loan products, two reasons why a different approach is needed are that the standard of financial information provided by SMEs is much lower and the capabilities of the SME owner/manager are more crucial for the SME than for large companies. During regular visits to FI partners, FSP will discuss their current credit processes/practices and make recommendations for improvement.

Activities:
1.2.1 Improve SME finance approval processes of smaller FI partners. FSP will visit its Tier 2 partners on at least a quarterly basis to discuss their current performance, loan processing and loan monitoring challenges. Close monitoring of these partners is warranted as any deleterious practices that develop could have a more serious impact on their relatively small operations as well as the fact that they have a higher proportion of relatively inexperienced staff.

As appropriate, FSP will make recommendations on how to improve credit processes, including risk assessment techniques, best practices in cash flow lending, credit scoring, and will follow up during subsequent visits on their implementation.

Royal Fields Finance Financing Process Improved

RFF was intending to employ a risky payment method for its clients, using loan proceeds to pay cash in advance for the imported raw materials one of its clients needed to fulfill contracts. Upon learning of this intention during a monitoring visit, FSP recommended that instead RFF should employ the more structured, safer documentary drafts payment method, under which payments are effected through banks. The South African importer only pays for the shipped goods when the shipping documents, which confer title, are received by his bank from the exporter's overseas bank.

[7] Warehouse receipt loans enable financing against a commodity deposited in a bonded, secure warehouse. When the commodity is sold the proceeds are used to repay the loan.

Such improvements should lead to higher loan production while keeping loan portfolio quality within acceptable limits (see RFF example in textbox). FSP will continue to explore the possibilities of extending technical assistance for credit scoring, as this method can be an efficient, streamlined and yet prudent way of underwriting smaller, uncomplicated loan applications.

KRA 1.3 Use of loan guarantees/special funds programs expanded

KRA Strategy:
From its outset, FSP has sought to expand the role of loan guarantee schemes. Lenders throughout the world generally are interested in using these guarantee facilities as a risk mitigation tool when looking at penetrating a new credit niche (either in terms of loan products, industrial sectors or geographic areas). In view of tight credit market conditions that developed in South Africa because of the impact of the 2009 global recession and the ensuing sluggish economic recovery, guarantee schemes offer an attractive mechanism to entice lenders to extend their credit risk profiles.

In addition to FSP's mandate to expand the use of the USAID Development Credit Authority (DCA) guarantee schemes, FSP also engaged with two South African guarantee schemes; Thembani International Guarantee Fund (TIGF) and Khula Enterprise Finance, the state agency aimed at assisting SMEs. These indigenous schemes were hampered by a number of factors, such as the effect of the economic slowdown on their clients, and the requirement for significant restructuring/streamlining to their claim processes to make them more attractive to lenders. Even the relatively high guarantee percentages offered by Khula and TIGF did not provide enough incentive for the "big four" banks to extend their risk profiles for higher risk BEE borrowers. Overall, traditional lenders have not been eager to utilize a guarantee to expand their penetration into the SME market. Therefore, FSP will also embark upon a mindset modification approach to increase uptake of these opportunities.

In the meantime, promotion of the USAID DCA guarantee scheme has proved to be relatively attractive, primarily for non-bank intermediaries to access much needed on-lending capital. In Year 3 FSP will support three recently approved holders of DCA portable guarantees. The results and impact from these three facilities are expected to be substantial, but securing financing is still a work in progress and will be a priority for FSP to facilitate finalization of loan funding.

Moving forward however, FSP's preference will be on developing DCA loan portfolio guarantee (LPG) facilities, similar to the LPG facility approved for Blue Financial Services in 2009. So long as the beneficiaries of LPGs are creditworthy, processing of LPGs is simpler and faster and has the potential to build a multi-layered financial services relationship with the lender.

Activities:
1.3.1 Facilitate and Promote utilization of USAID DCA guarantee facilities. FSP will help facilitate arrangement of funding for the three portable loan guarantee facilities — for Mettle, True Group and Spartan — by participating in DCA information sessions with potential lenders. They are seeking funding of $20 million, $20 million and $25 million, respectively. To date however, the market has shown itself to be somewhat reluctant to engage in traditional direct lending even with the credit enhancement of a DCA guarantee. As a result, FSP will also explore innovative alternatives to traditional direct lending; specifically explore

the possibility of developing a bond scheme to support the capital needs of these and other SME lenders utilizing further DCA support to enhance this SME Bond issue.

Once the loans are closed and the three DCA portable guarantee partners begin making their loans or leases, FSP will assist in promoting and monitoring of the facilities. FSP will also work to increase the utilization of Blue's LPG facility, which has been slower than expected due to Blue's funding challenges. Thus far Blue has utilized around 40% of its $5 million LPG.

Over the last two years Mettle has made 1,200 – 1,800 advances per month in connection with its factoring operations. With increased funding made possible by the DCA guaranteed funding it should be able to at least double the value of its factoring during the life of the facility. Spartan's leases for information technology (IT) equipment funded by the DCA guaranteed loans are expected to number 20 to 50 per month. The total number of loans True Group is expected to make will only be around 60 over the life of its facility, but the type of financing it extends (long term, investment financing for start-up and early stage expansion SMEs) is unique and rarely available in South Africa. As noted earlier, there will be additional impact from FSP's assistance to Mettle in developing new financing products, equipment term loans and purchase order financing for auto parts.

1.3.2 Develop new DCA Loan Portfolio Guarantees (LPG). FSP plans to develop new DCA LPG facilities as they have a greater potential for overall financial sector deepening. FSP is currently discussing the preliminary concept for a $5 million LPG with ABSA Bank, under which the bank is envisioning making loans to SMEs in Northern Cape, South Africa's poorest province. Additional LPG facilities will be pursued with FNB and Nedbank. Once concept papers are finalized, FSP will help draft LPG Action Packages for submission to, and approval by, USAID Washington's Credit Review Board.

Financial vs Non-Financial BDS

Regular consultation with USAID SAIBL has shown how their activities complement those of FSP. Where SAIBL focuses on BDS which impact the ability of an SME to access corporate linkages, FSP focuses on those BDSPs which have a more direct bearing on access to finance. Where non-financial BDS are broader in scope, and remain essential to SME bankability, FSP has concentrated on the finances of an SME and what FI's consider as important factors in awarding finance.

During Year 3, FSP will continue to leverage this symbiotic relationship to gain greater market impact for many of its bankability interventions.

B. PIR 2: Bankability of SMEs Enhanced

Just as PIR 1 addresses the challenges faced on the supply side (FIs) of access to SME finance, PIR 2 seeks to help overcome deficits on the demand side of SME finance (SMEs) – to make SMEs more bankable. The main focus of PIR 2 is to build the capacity of business development service providers (BDSPs) — both organizations and individuals - so that SMEs are offered a more robust and effective service in helping them to access finance and thereby grow their business. Many SME owners do not meet even the most basic requirements that applications for finance require, and so in order for them to become bankable they must understand their financing needs and the cash flow of their business, project future earnings, and prepare the proper documentation to apply for credit. FSP focuses on improving the quality of finance-related business development services[8] they

[8] Hereinafter, any reference to "BDS" refers to finance related BDS.

receive from BDSPs as well as enhancing their financial literacy, namely their understanding of what financial services and products are available to them, who the market of finance providers are and how to approach them, as well as how to better manage their own finances.

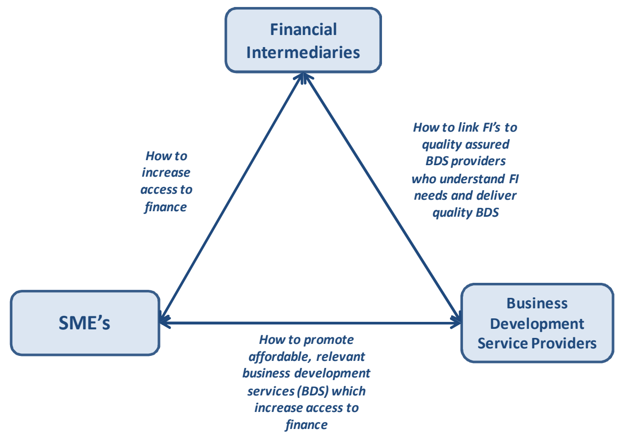


Figure 1: SME sector linkages

The figure to the right depicts the players with which FSP seeks to make a difference. In a March 2010 FSP survey identifying the hurdles FIs face in the provision of credit to SMEs, several external factors emerged as contributing to the failure of SMEs to access finance. These included lack of financial education and literacy on the part of SMEs, a lack of adequate pre-finance support for SMEs and a lack of qualified BDS providers advising the SMEs. FSP's 2008 research of SMEs' finance challenges indicates the lack of adequate information in the market about the types of finance products available to SMEs, SMEs' lack of adequate analysis of what type of finance they need, as well as the weak supply and demand for BDS based on the quality and type of BDS generally offered to SMEs. These findings confirm the fragmentation in the market between players, something which FSP is making a concerted effort to address.

FSP's approach to improving SME bankability is predicated on achieving a multiplier effect. FSP is targeting its interventions at BDSPs and FI's rather than providing services to SMEs directly as offering direct assistance to SMEs is not a cost effective nor sustainable approach. This approach required FSP to identify dynamic partners– primarily private, fee based organizations whose members provide BDS to SMEs. In most cases, these partners require capacity building of both institutions and individuals. Institutions need to improve their ability to offer a service more widely to BDSPs, and individuals need to build their skills and knowledge to better serve SMEs.

PIR 2 Benchmarks

- 15 new BDSPs graded
- 100 BDSPs trained in how to deliver cash flow management
- Strategy developed and accepted by BSO
- Web-based version of **finfind** completed and field tested
- **Finfind** host institution identified
- 100 SMEs trained in cash flow management
- 3 informal partnerships formed

In laying the ground work for future activities, FSP has identified partners with great outreach potential, analyzed their needs for capacity building and the most cost efficient delivery mechanism, catalogued the available SME financing products, and developed appropriate SME business skill development materials. In Year 3 FSP will focus on strengthening these partners' capacity to offer more effective services, and on refining and scaling up the delivery of finance-related BDS in the SME sector that can lead to access to finance. To improve the quality of BDS, FSP will focus on assessment and grading of BDSPs, equipping them to assist SME clients manage their finances (and cash flow in particular), and to scale up initiatives which successfully lead to access to finance.

To improve both quality of BDS provision and financial literacy, FSP's main priority will be the introduction of *finfind*, an on-line tool designed to help BDSPs facilitate informed decision-making by SMEs on the need for appropriate finance products needed to expand their businesses.

Linkage facilitation between BDSPs and FIs will underlay all PIR 2 activities during Year 3 and in this respect, will make use of approaches which cut across all FSP components.

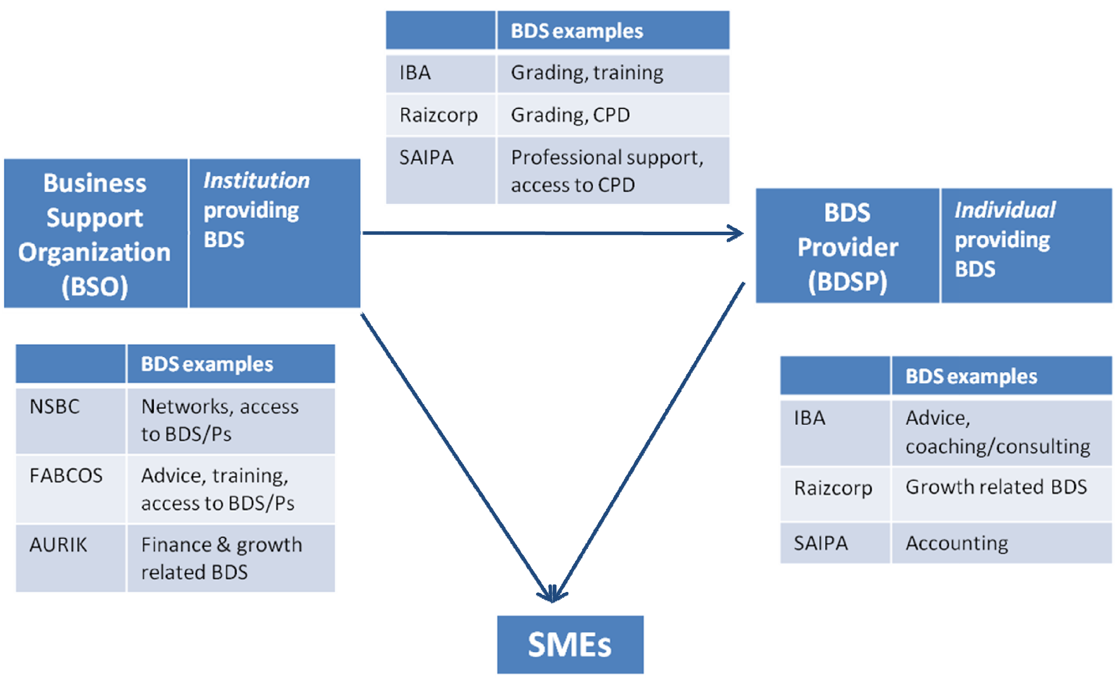
Two Key Results Areas (KRAs) support PIR 2:

KRA 2.1 — Quality of BDS related to finance improved
KRA 2.2 — SME Financial Literacy Enhanced

Each of these KRAs is detailed in the following pages in terms of its key activities, implementation resources/partners, and interim benchmarks. Specific tasks and timing are indicated on the timelines that follow the text in Annex A.

KRA 2.1 Quality of BDS related to finance improved

KRA Strategy:
SMEs can access BDS in a number of ways, either directly from BSO institutions or from BDSP individuals. FSP's primary partners are shown below with their key delivery methods and types of BDS shown.

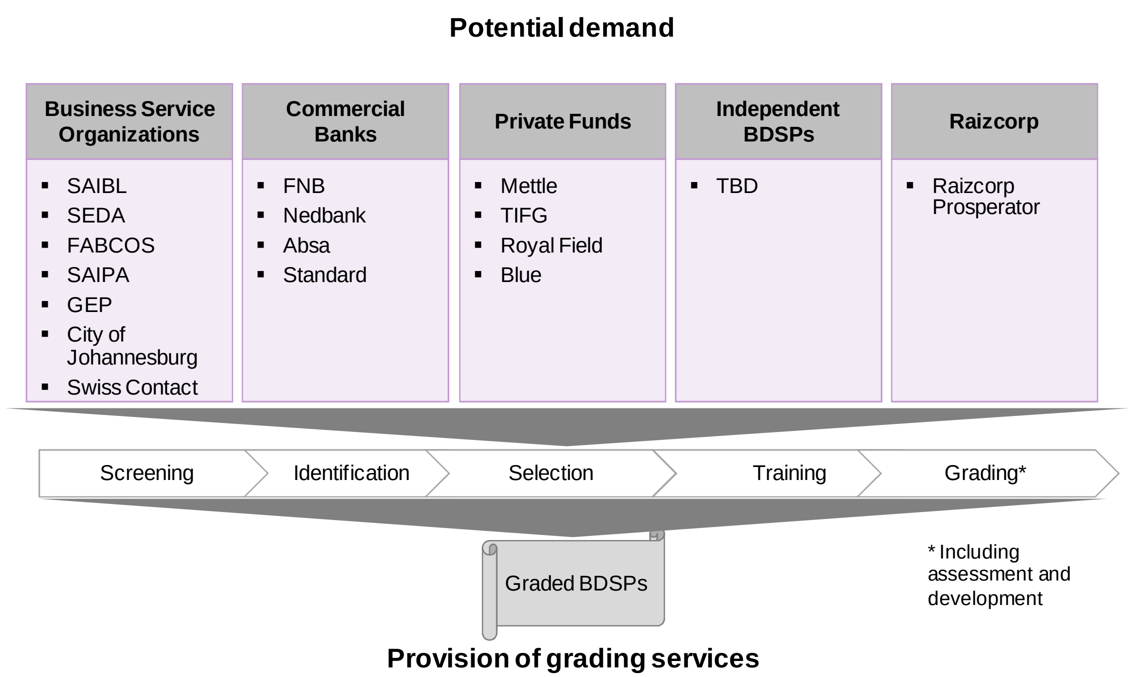


To raise the quality of finance-related BDS, FSP will focus on three key initiatives. FSP will promote the grading and assessment of BDS providers (BDSPs) in South Africa. Additionally, FSP will scale up the capacity of business support organizations (BSOs) to deliver tried and tested BDS which will lead to greater access to finance as well as developing the skills and capacity of BDSPs so that they, in turn, are better equipped to facilitate access to finance more effectively.

In Year 2, FSP facilitated the design and (internal) testing of a framework and tools for grading, assessing and professionally developing BDSPs with its private sector partner, Raizcorp. FSP also undertook an assessment of demand in the market for quality assured BDSPs and developed a strategy for Raizcorp's Guiding Academy (RGA) to scale up grading activities across South Africa. In Year 3, FSP will build on that foundation and assist Raizcorp to establish traction in the market with FIs and BSOs and will invite Raizcorp, in the first quarter, to test the feasibility of its approach by offering grading on a cost recovery basis.

Further, in recognition of the challenge SMEs face in managing their cash flow and the barrier that this presents to access finance, FSP will build the capacity of BDSPs to assist SME clients manage their cash flow, an area and skill set typically lacking in the market of BDS provision. This assistance to BDSPs will deepen their skills and expand their service offering to the market. Targeting service providers with capacity building has the potential to increase the reach of this service to more SMEs seeking access to finance. Concurrent with these activities, FSP will work with existing BSO partners to build their capacity to scale up BDS which will enhance their capacity to better serve the needs of their SME clients and improve their potential to access finance.

Figure 2: Potential demand for grading services in the market



Activities:

2.1.1: Facilitate scale up of grading and professional development of BDSPs. Raizcorp, with FSP's assistance, has designed a framework for grading BDSPs and piloted it with its 15 in-house BDSPs (or Guides). Additionally, FSP developed a strategy with Raizcorp to scale up its grading activities in the market. A crucial element of this process involved assessing the demand for grading in the market and identifying the risks which Raizcorp will need to address in order to scale up. The diagram above shows potential demand for quality assurance of BDSPs based on segments of the market and players interviewed, mapped against the grading services which Raizcorp has developed for the market, from screening through to grading.

While many FIs and BSO's noted above expressed interest in a system to grade and develop BDSPs, Raizcorp's value proposition has not, as yet, been tested in the market of external BDSPs. Under this activity, FSP will collaborate with Raizcorp to implement an external pilot of the process and tools designed to assess BDSPs. Not only will this give Raizcorp the opportunity to test its approach and fee structure for grading and gauge the willingness of BDSPs to commit to and pay for such a service (in order to form a critical mass of demand in the market), it will also indicate whether Raizcorp's business model will cover the cost of the internal capacity needed to expand the grading activities of the RGA.

Based on the results of this external pilot with a minimum 15 BDSPs, FSP will gauge the efficacy of further investment. With a successful pilot, FSP support will focus on three main elements which will contribute to the success of this initiative and manage the risks identified in FSP's Report *Scale-up Strategy for Grading Business Development Service Providers*:

finfind
Business Finance Catalyst

Through trained BDSPs, *finfind*, will generate a cadre of SMEs able to make informed decisions about their business finance needs. Using this on-line tool, BDSPs will help SME owners understand basic financial concepts, know what the most suitable financing options are for their business; where to obtain the relevant products and to interact with confidence with the suppliers of these products and submit more bankable applications.

- Testing and refining of Raizcorp's approach in the market
- Promoting its services to the market
- Supporting Raizcorp's application for accreditation by an international body to establish it as a Centre of Excellence of BDS provision in the South African marketplace.

Concurrently, FSP will review the potential for alignment between Raizcorp's professional standards for assisting SMEs (what they refer to as guiding) and the occupational standards and procedures recently redefined by the government of South Africa GoSA's National Qualifications Framework (NQF). Historically, approval of standards and accreditation of qualifications has been a complex and lengthy process, however with recent changes to the NQF, FSP will gauge whether there is merit in Raizcorp seeking alignment to the national system as an additional approach in seeking to professionalize BDSPs.

2.1.2: Build capacity of BDSPs to assist SME clients to manage cash flow. In line with FSP's strategy to build the intermediate layer of BDS provision to promote SME bankability, FSP will identify a BSO/partner who can train BDSPs to assist SME clients to manage their cash flow. Using a modified version of FSP's existing capacity building program "*Successful financial management of SMEs*", the partner(s) will ensure that BDSPs understand SME cash flow management and know how to assist SME clients manage their business cash flow. The training partner will measure the number of BDSPs it assists and monitor sustained application of the skills taught by using regular feedback forums and identifying additional needs of BDSPs for support and training.

FSP will work with the training provider to promote this program by facilitating links between it and other BSOs such as the Institute of Business Advisors (IBA), FSP's partner SAIBL, and the Gauteng Enterprise Propeller (GEP), as well as to *finfind* BDSPs who may seek further skills development. The expected outcome of this activity in Year 3 is that at least 100 BDSPs will be trained in cash flow management and equipped to help their clients manage what has been identified by FI's as a hurdle to SME's accessing finance leading to at least 1000 SMEs gaining the skills needed to become more bankable.

2.1.3: Build BSO capacity to deliver finance-related BDS. Several FSP BSO partners are involved in initiatives to build BDSP capacity and deliver BDS related to access to finance, however, they are constrained in their delivery by their own capacity to grow and develop these services further. In Year 3, FSP will work with those BSOs that demonstrate potential and/or readiness to scale up their activities, thereby increasing their reach to SMEs and potential to increase access to finance. FSP will identify who to work with based on current relationships with BSOs who are nimble, growth oriented and SME focused, and will determine the nature of intervention required. In short, FSP will undertake an assessment of the BSOs' existing programs, approaches and tools and based on this, provide technical assistance to replicate their initiatives to prepare them for expansion and scalability. FSP interventions will focus, for example, on improving existing methodologies, modifying tools, developing training of trainers programs, or developing strategies to assist with scale up. The outcome of this activity will be that at least one BSO scale up plan will be implemented leading to 1000 SMEs being readied to access finance.

KRA 2.2 SME financial literacy enhanced

KRA Strategy:
Based on Year 2 research efforts entitled *Development of strategy options for SME financial literacy*, FSP identified the market need for a financial literacy product which would promote understanding and knowledge of SME finance providers. It was further concluded that the initiative should not be aligned in terms of promoting one finance provider over and above another.

FSP conducted research and undertook extensive consultation with its BSO partners to assess the needs and behavior of their BDSP members in assisting SMEs to access finance. This was done in order to ensure relevance and create awareness of the product concept as well as to anticipate the way it would be used by BDSPs. Continuing FSP's strategy of working through BSOs, the product is designed to enhance SME financial literacy primarily through building the capacity of BDSPs to understand and be well informed about the financial sector – what products and services it offers, who and where the providers are, how to apply for credit – and to engage with SMEs in a way that promotes access to finance.

Based on the research undertaken, and consultation with FI's and the SME Committee of the Banking Association, and the key BSO partners, FSP undertook a multi-phased approach for the content and technological development for a web-based South African guide to small business finance branded ***finfind.*** This significant undertaking will soon enter the alpha testing phase and be ready for introduction in Year 3. FSP will work with selected BDSPs to test its use and the training which will be developed to demonstrate how *finfind* should be used to facilitate access to finance.

A major focus for FSP during Year 3 will be to secure and build the capacity of a host institution that will champion *finfind*. FSP will use a competitive process to identify a partner with the relevant footprint, national reach and infrastructure to sustainably establish *finfind* in the market.

Currently no product or single platform exists locally which provides such comprehensive information about available credit products and financiers for SMEs. Several institutions have expressed interest in taking custody of *finfind*, both in terms of provision of ongoing training, as well as website hosting and updating the information on a regular basis. This tool, and the training associated with it, has the potential to grow a cadre of BDSPs skilled and equipped to facilitate access to finance in an informed and effective way. It also has the potential to build a community of consultants, facilitate knowledge sharing, promote ongoing professional development and knowledge of the FI sector and professionalize the BDSP sector through deepening BDSP understanding of “access to finance”.

We anticipate creating significant market linkages through this product, by BDSPs understanding FI products and helping SMEs be more effective in their applications for finance, by FIs listing their SME credit products in *finfind*’s directory of finance providers, and by providing trained *finfind* consultant point of contact information available to both FIs and SMEs.

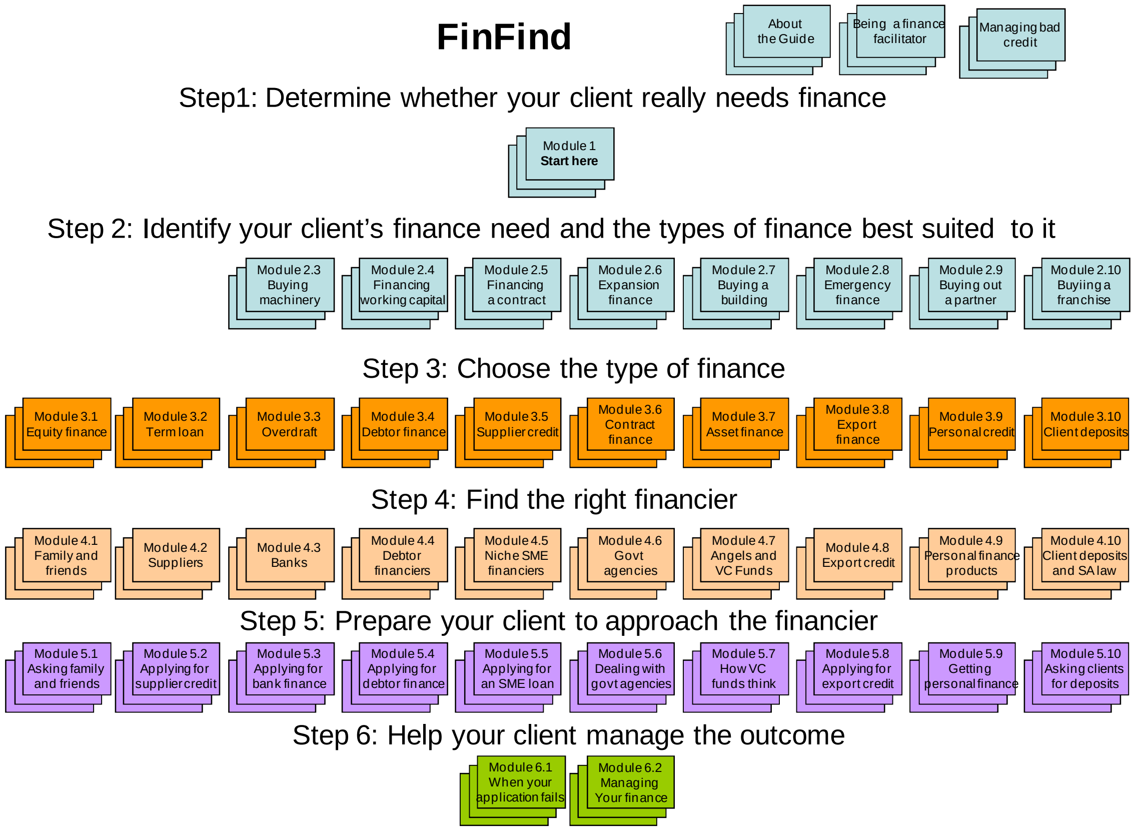
To do this, FSP will engage with FIs to build linkages with BSOs and BDSPs to ensure the SME preparation work addresses the specific deficits identified by the FIs offering the credit. With the relationships built with a range of partners during Years 1 and 2, and with *finfind* as a unique resource in the market, FSP is well positioned to act as a catalyst, facilitating links between BSO’s and FI’s. FSP will create opportunities to bring BSO’s and FI’s together in order for them to learn directly from each other and to stimulate market links within the sector.

Activities:
2.2.1: Finalize development of finfind. The web-based South African guide to small business finance developed during Year 2 by FSP named *finfind*, will be delivered to market via a capacity building program for BDSPs. Before launching *finfind* onto the market, several steps in its development need to be concluded, from completion of technical design to development of a user guide and training materials as well as user testing.

FSP will develop a training program for BDSPs which will integrate the User Guide (focused on how to navigate through the *finfind* site) with training on *finfind*’s approach to facilitating access to finance and how to consult with an SME, namely a step-by-step process which takes the SME through a decision tree based on whether they need finance or not, for what specific purpose they need finance, what products are suitable to meet their financing needs, where to source them and how to approach the providers of specific finance products (see diagram of *finfind* architecture below).

The approach to preparing *finfind* for the market will include extensive testing and interaction with a group of BDSPs selected by FSP from its partner BSOs in this project, namely IBA and SAIPA. The same group of BDSPs will be involved in user testing alpha and beta versions of *finfind*, piloting of the training program, participating in several focus groups to gauge use and usefulness of *finfind*, and to identify and address problems encountered by BDSPs in using *finfind* with their SME clients, i.e. outside of a pilot context. The rationale for this approach is predicated on FSP's intention to preempt as many problems with the product as possible before it reaches market, as well as in recognition that capacity building of BDSPs is a long term process, and to make it sustainable requires ongoing, interactive engagement and continuous learning.

Map of *finfind*, South Africa's guide to SME finance



2.2.2: Build BSO capacity to roll out finfind across the country. In Year 3 FSP will identify an institution that will take custody of and champion *finfind* in the marketplace. FSP will invite several BSO partners to submit expressions of interest to host *finfind*. A partner will be selected based on their recognition of *finfind*'s value and potential to grow as a brand in the market, their technical capacity to manage it as a web-based resource, their capacity and commitment to rolling it out across the country and their vision to grow it as a product and build a community of *finfind* consultants, specialists in facilitating access to finance.

Once an institution is selected, FSP will build their capacity in a number of areas, including, but not limited to:

- Training and technical support in how to maintain and manage the web-based resource as well as produce reports generated by *finfind*
- Development of a training implementation roadmap showing roll out across provincial centers
- Development and implementation of a strategy to raise awareness of *finfind* across the country

- Support during rollout
- Identification of additional capacity building needs.

The major outcome of this activity will be the identification of a suitable host for *finfind* and an approach to implementation which will ensure ownership and sustained use in the market.

2.2.3: Improve finance-related BDS offered through partners. Building on the development and testing of the "*Successful Financial Management for SMEs"* training program developed in Year 2, FSP will collaborate with its FI partner, Blue Financial Services, to pilot the program with its own SME clients and to design a program and demonstrate how it will roll the program out during the coming year.

Additionally, FSP will identify those FIs that would like this program to be delivered to their SME clients and, if necessary, will modify the content and delivery mechanism accordingly. If appropriate, FSP will develop a training of trainers program to organize delivery of the course on behalf of FI's and will facilitate links between FIs and BSOs such as the National Small Business Chamber (NSBC) and the Foundation for African Business and Consumer Services (FABCOS) who may expand their service offering to their SME members by referring them to these FIs for training and possible access to finance.

In addition, FSP may modify the course material to make it applicable to specific sectors and more appealing to sector–specific FIs such as Mettle or Spartan. FSP will measure results achieved by working with the FI partners concerned, and monitoring the records they keep of number of SMEs assisted and number applying for finance. In addition to this, FSP will monitor the number of trainers trained to deliver the program on behalf of FI's.

KRA 2.2.4: Facilitate market linkages between BSOs and FI's leading to improved service delivery to SMEs. FSP will engage in several cross-cutting events which will promote building of relationships between FIs and BSOs and involve staff from all FSP components: SME finance, SME bankability, enabling policy environment and knowledge management. Through its partnership with the NSBC, FSP will facilitate several seminar discussions to take place at the NSBC's "Access to Finance" expo in March 2011. FSP will use this forum to facilitate FI information dissemination and promotion of specific financial products (such as purchase order finance and/or invoice clearing) and finance providers (such as private funds), as well as to engage BSOs and BDSPs on policies and regulations impacting the SME sector. FSP will use the event to launch *finfind*, and will use the seminars to identify potential interest in additional cross-cutting seminars.

If levels of interest are sufficiently high, FSP will facilitate bi-monthly or quarterly "Access to Finance" seminars for BDSPs to grow their knowledge of, and links to, the financial sector, as well as facilitating links between FI's, BSOs and BDSPs. These forums will be used to identify additional information and BDS needs in the sector and to promote knowledge sharing within the sector, particularly among BDSPs trained in the use of *finfind*.

C. PIR 3: Financial Sector (and SME) Development Enabling Environment Improved

To achieve South African government objectives of economic growth, employment creation and transformation, an improved business environment is essential – especially for previously disadvantaged entrepreneurs. An improved business environment is also critical in signaling to potential investors that South Africa is open for business through empirically sound and globally accepted comparative rankings. In recent years South Africa has slipped on many of the independently compiled world indices, not so much because of what was done but rather because other similarly positioned developing powers more aggressively addressed their business environment issues.

All FSP components interface with the policy and business environment. For example, during the development of new, innovative credit products, FSP will identify obstacles in the legal system or business environment which may make such products not viable in this market. One such example is the limitation on perfecting security over a generic category of assets such as receivables or trade inventory without triggering an insolvency event requiring the notification of all creditors, workers etc. with potential disastrous consequences. This will have significant impact on the development of the upcoming purchase order finance and invoice clearing loan products being developed but will be addressed though the FSP policy work on insolvency.

PIR 3 Benchmarks

- Overview of the effects of NCA on SMEs completed
- Interpretative summary on a comprehensive statistical monitoring system submitted
- Report analyzing debt-insolvency harmonization issues submitted
- Financial Sector Regulatory Framework/impact report submitted
- Interpretive summary on competition policy completed
- Companies Act Regulations submitted
- Revised Commission fees completed
- Insolvency Policy update report completed
- RIA framework completed

South Africa is, at the legislative and institutional level, highly developed and sophisticated and, as such, not comparable to most other developing countries. The Managing Director of the Banking Association, at a recent event at the Reserve Bank stated it succinctly: “The banking sector needs to look at appropriate products, but regulators need to enable our ‘developed world’ sector to address ‘developing country’ challenges”. No matter how well intentioned policy is or how it conforms with international best practice, unless entrepreneurs, the public and private support sector and labor are consulted, serious unintended consequences will frequently arise leading to extensive litigation, prohibitive compliance costs and, ultimately fewer jobs with lower compensation.

During the first two years of the program, the FSP team established excellent working relationships with an extensive and broad-based list of key public and private sector stakeholders in developing the PIR 3 policy agenda. In all policy work a strong public/private partnership is essential to contribute to government policy formation and to build trust between stakeholders and government. FSP supports Government of South Africa (GoSA) efforts to ensure all potential ramifications of policy choices are examined and vetted before enactment. An indicative list of policy partners and stakeholders regularly consulted during FSP activities is included in a textbox below.

Broad based public-private consultation is time consuming and frequently adds complexity to the legislative drafting process, but it is an essential tool to present all options to the policy makers. FSP encouraged this approach in the consideration of the Companies Act and drafting of the Companies Regulations. As a result, policy makers designed scalable solutions ensuring that nascent and small scale entrepreneurs can start their journey to formality and success with minimum regulation, administrative simplicity and a low compliance burden in both time and money while imposing more stringent standards on larger firms. In the same manner, FSP aided National Treasury and the dti in strengthening South African Regulatory Impact Assessment (RIA) capacity which will permit policy makers to scope and design better legislation and to better monitor and quantify if such good intentions are consistently and sustainably applied prior to and following the completion of the legislative process. Currently FSP is on the cusp of seeing major policy initiatives it has been deeply involved in coming to fruition. Upon the coming into force of the Companies Amendment Act, the Regulations under the Companies Act (as amended), the revisions to the Close Corporations Act Regulations and other laws and regulations, FSP will have contributed to what has been described in the business media as the most far reaching overhaul of business law in decades. In addition this will have laid the groundwork for the simplification of dozens of processes, assisted with the creation of more transparent public agencies, limited the potential for fraud and corruption; and supported the establishment of internal administrative review mechanisms and alternative conflict resolution mechanisms. Every step must be taken in sequence to support rapid and effective implementation of this legislation and, through the use of outreach and knowledge management techniques, assuring that the giant steps South Africa has taken will be reflected in the future evaluation of the business environment for the country.

PIR 3 Policy Partners and Stakeholders

Department of Trade and Industry (dti)
National Treasury
Department of Justice
Law Reform Commission
Financial Services Board (FSB)
National Credit Regulator (NCR)
Johannesburg Stock Exchange (JSE)
Share Transactions Totally Electronic (STRATE)
Independent regulatory Board for Auditors (IRBA)
National Small Business Advisory Council
KHULA
Banking Association,
COSATU and Solidarity Labor Unions
Reserve Bank
Business Unity South Africa (BUSA)
South African Institute of Professional Accountants
FinMark Trust
South African Institute of Chartered Accountants
All major universities
Association of Insolvency Practitioners of SA
Deloitte
Law Societies of South Africa
Leading law firms and lawyers.

Two Key Results Areas (KRAs) support PIR 3:

KRA 3.1 - Financial sector legal and institutional framework improved
KRA 3.2 - Regulatory environment stimulating business (SME) development enhanced

Each of these KRAs detailed below addresses one or more of these issues and related policy areas. Although initially designed to only support the identification of obstacles to SME finance and designing policy alternatives, USAID clarified during Year 2 that the broader business environment, within which SMEs also operate, should be targeted and that this component be extended past its original end date of June 2010. In the following pages the strategy, key activities, implementation resources/partners, and benchmarks are detailed. Specific tasks and timing are indicated on the timelines that follow the text in Annex A.

KRA 3.1 Financial sector legal and institutional framework improved

KRA Strategy:
A large number of South African business laws and regulations are outdated and have not been revised or consolidated for decades. This places a heavy burden on government to modernize and reform policy while at the same time, move decisively on the reform of the

state, to increase service delivery, economic growth, employment creation and transformation.

FSP assists in the review and reform of a limited number of key policies, laws and regulations. To do so, the project works closely with technical teams in departments and agencies of government and aims to provide assistance in areas requested by government bringing international best practice approaches in modernizing the South Africa business environment. Such detailed collaboration between FSP and government professional staff builds capacity providing a more sustained impact.

In addition, FSP undertakes applied research on a number of specific issues for the purpose of presenting policy overviews and defining potential legislative policy areas to be addressed with identified public and private sector champions. Such assistance can take a two-phase approach. During phase one (covered by KRA 3.1), FSP assists the public and private sector stakeholders in identifying policy issues and collaborating on policy analysis to inform decision-making. Public/private dialogue events are usually part of this process as well as other GoSA-mandated reviews.

Typically a preliminary report or White Paper will be produced setting out the scope and objective of the work to be undertaken and, identify issues for public-private sector consultations and dialogue. The White Paper can then be enhanced into an Interpretative Summary combining the original paper with a summary of cogent observations and policy input received during the dialogue stage. The Interpretative Summary will typically outline potential next steps and actions should follow up action be indicated. If the government chooses to pursue a new law, regulation or administrative procedure, phase two activities (covered by KRA 3.2) support the effort as it follows the South African policy development process — potentially providing legislative drafting and enactment support. FSP is available to provide additional research, analysis or guidance and then may assist the lead department with implementation of the policy change – primarily through capacity building activities.

Success in policy reform is consistent progress in the right direction leading to South Africa achieving the Government's over-arching policy objectives of accelerating economic growth, employment creation and transformation, and an improved business environment.

Activities:

3.1.1: Support the dti/ NCR to make the NCA more conducive to stimulate access to credit for SMEs. FSP previously designed the process and drafted legislative amendments required to implement a National Register of Credit Agreements (NRCA), deemed an important step in enhancing access to credit for all consumers and juristic persons under the NCA. At this point, legislative action to amend the NCA and begin implementation of the NRCA is a prerequisite for future activities. The proposed amendments have not as yet been presented to Parliament, but implementation of NRCA remains an important FSP objective and a critical step in enhancing access to credit, especially for SMEs.

It appears that amendments proposed to the NCA will be held up until the Parliamentary mandated five year review of the NCA is undertaken by the dti. Such a review will undoubtedly need to closely examine the impacts — both positive and negative — the NCA has had since becoming law in 2005 and as administered and applied by the National Credit Regulator (NCR) since its establishment in July 2007. This review will be undertaken by the dti/NCR and this process is expected to commence in 2011. FSP hopes to assist the government in the implementation of this review, especially as the NCA applies to juristic persons - many of which are SMEs. Such an analysis will undoubtedly also need to review and harmonize debt restructuring mechanisms applied by the NCR, assuring that consumer and juristic person over-indebtedness, restructuring and eventual insolvency, is consistent with policies applicable to companies under the Close Corporations Act, the new Companies Act as well as amendments to the Insolvency Act currently under consideration. Such policies must strengthen sanctity of contract, establish clear priorities, simplify and accelerate procedures, rehabilitate debtors, preserve productive assets and employment if possible and maximize recovery for creditors, thus ultimately limiting cost of credit.

3.1.2: Follow up activity on applied research for the establishment of a modern statistical monitoring system for the SME sector. Any policy decision ideally relies on data and a study of the potential costs and benefits of policy implementation. To evaluate the efficacy of a proposed change or the consequences of an existing policy, data is required. Unfortunately, particularly as it relates to SMEs, there is a dearth of statistical information. Currently, in the absence of adequate statistical data, a number of diverse surveys are undertaken. The diversity of techniques, scopes and definitions utilized make such surveys not only very expensive but difficult to compare and of little use in policy formation by government.

In March 2010 FSP presented the National Small Business Advisory Council (NSBAC)/dti with a White Paper outlining policy issues and potential approaches for the establishment of an upgraded system for the statistical monitoring of the SME sector in accordance with OECD practices and policy. The White Paper addressed the absence of adequate statistics on the small, micro and medium sized enterprise (SMME) sectors making it difficult for government to design and implement appropriate policies for this critical sector. The FSP White Paper was widely distributed within the dti and among private sector stakeholders. The NSBAC has indicated it intends to convene a stakeholders meeting to coordinate next steps, based on FSP's recommendations. FSP anticipates working with government to further develop this critical area of need.

3.1.3: Applied research on reforms required to enhance the insolvency policy framework. FSP is currently completing a comprehensive Insolvency Policy Review and planning several workshops and dissemination activities. This review was motivated by FSP work previously undertaken under the NCA, the Companies Act and the Close Corporations Act. A comprehensive and harmonized insolvency regime is an essential element of enhancing

Cooperation with other donor programs

In addition to cooperating with USAIDs SAIBL Program, FSP has developed excellent working relationships with other multi-lateral and bilateral development agencies. EGAT/Washington entered into an agreement with the World Bank to jointly examine consumer protection in the financial sector. "Consumer" within the applicable World Bank definition overlaps substantially with FSP's definition of SMEs. FSP has been working closely with the World Bank to scope and define the pilot program for South Africa and collaborated in the World Bank's first Mission.

The applied research on the insolvency framework supplements work done some years ago by the World Bank as part of its ROSC program. There is substantial interest in FSP/World Bank collaboration going forward if GOSA proceeds with the implementation of the Insolvency Interpretative Report recommendations. Also in terms of FSP work on Improving the SME credit Environment – Modern Risk Management tools, the IMF was consulted and it is anticipated that the IMF Representative will participate in selected workshops on this topic.

Additionally, FSP will also continue to explore possibilities to collaborate with other donor funded organizations working in the SME sector such as the Swiss Confederation and FInMark Trust.

access to credit – including for SMEs. Prior FSP work made it clear that many SMEs could not benefit from insolvency protection under any of these acts. Working closely with the dti, the Department of Justice and the South African Law Reform Commission as well as a broad cross-section of private sector stakeholders, FSP has created a vibrant discussion on the harmonization and modernization of a comprehensive insolvency framework. Such a framework must incorporate the new business rescue provisions in the new Companies Act as well as the provisions for debt review and restructuring under the NCA for consumers and "juristic persons" as well as the residual provisions of the Close Corporations Act within the broader Insolvency Act and pending amendments under consideration.

Potential Impact of Basel III Accords

The Basel Committee announced new criteria for strengthening the stability of the financial system in September 2010. The new criteria will further tighten the bank capital and liquidity requirements – especially important for countries like SA which do not have deposit guarantee schemes. Basel III may also result in big banking groups taking over smaller banks which have traditionally provided finance for small and medium-sized enterprises (SMEs). Again, in SA where the existing banking system was recently described by the IMF MD as "… an oligopoly at best" this requires careful monitoring.

Although a long phase-in period has been agreed to, government will need to develop plans to support the already inadequate financing of SMEs in order to offset any negative impact on liquidity and lending resulting from the Basel III.

This phase of the work will be completed by the production and wide distribution of the Interpretative Summary incorporating FSP findings enriched with the observations and learning from the public sector discussions and the public-private sector dialogue. The Interpretative Summary will include a suggested work plan to move from research to comprehensive policy recommendations to an implementation strategy. The World Bank has agreed to participate in the public-private sector dialogues. FSP hopes that the World Bank will support the implementation stage as described in Section 3.2.3 of this work plan. In anticipation of such donor collaboration a limited supporting role for FSP has been included during the implementation stage.

3.1.4 Applied research on financial sector regulatory framework and its impact on access to credit for SMEs. This research activity addresses a number of fundamental issues faced by the South African banking sector, financial supervisors and policy makers. Especially as government moves forward on the strengthening of financial sector stability, in line with the Basel III accords, attention must be paid to the potentially negative impact of such policies on other government objectives, including increasing access to credit for SMEs. Neither the government nor the private sector appears to have adequate quantitative skills and tools to measure the impact of such proposed measures and consider policy alternatives. Upon completion of the research stage, FSP will circulate the findings for information and discussion and to form the basis for three workshops as follows:

- Public Sector banking and supervisory workshop
- Private/public dialogue workshops focusing on a limited number of indentified obstacles and interaction with the regulatory framework
- The Monte Carlo interactive workshop focusing on the application of IRB under Basel II and III as it relates to SME and consumer portfolios

FSP will engage the government and private sector to define what further activities can be implemented by FSP to continue the dialogue and strengthen both government and private sector technical capacity in this area. FSP has made initial approaches to the IMF to participate in the workshops and potentially support further follow up activities.

3.1.5 Applied research on competition policy and the level playing field impacting SME access to markets. Access to markets and the elimination of anti-competitive behavior, including aggressively pursuing abuse of dominance cases, where a large market player uses their influence and economic power to prevent the entry of new competitive enterprises and, if necessary, drive such new competitors out of the market and frequently into bankruptcy, through the use of predatory prices, convincing banks not to lend and governments not to issue licenses, etc. . Access to finance means little if SME producers and service firms are excluded from markets. If new market entry SMEs are to succeed, aggressive enforcement of competition legislation is essential. Such a notional "level playing field" was deemed essential to address the market power of oligopolies which sprang up as a result of apartheid-era sanctions. It was one of the main reasons for putting in place a modern and effective Competition Law and Policy in the 1990s.

The transfer of the Competition Commission from the dti to the Economic Development Department (EDD) makes it easier for the dti to re-examine this critically important area with a focus on the impact on economic growth and market access for SMEs and other new market players. If government agrees this is a priority, FSP plans to undertake detailed quantitative analysis in close association with the dti, NSBAC and other SME stakeholder groups to establish the status of the competition policy in this regard.

KRA 3.2 Regulatory environment stimulating business (SME) development enhanced

KRA Strategy:
This KRA primarily covers phase two of the policy development process described in KRA 3.1: drafting of laws, regulation and administrative procedures and potentially assistance with their implementation once enacted. During the first two years of the program, FSP identified a number of activities which individually and taken together, will have a major and enduring impact on the corporate sector. Especially with the new omnibus-type Companies Act, its amendments and the Regulations will fundamentally and permanently change many major aspects of the business environments for decades to come. The new legislation has been carefully drafted and designed to make it fully "scalable" — making it user friendly for the smallest firm while at the same time imposing new controls and transparency on State Owned Enterprises (SOEs) and on for profit and not-for-profit firms, both foreign and domestic. With the active encouragement of FSP, the dti engaged a broad cross-section of stakeholders in an open and collegial process of consultation. Although this process is resource intensive and placed an additional level of strain on dti technical staff, dti persevered and, in doing so, provided an important policy discussion and learning opportunity for the drafting team while at the same time winning the trust and admiration of many private sector stakeholders. The business environment will be fundamentally altered when the new laws and regulations come into force, while the process provided an important example for reviewing other laws and regulations and dti benefits from a much more experienced policy analysis and drafting team.

Activities:
3.2.1: Draft regulations for the Companies Act and Companies Amendment Bill. FSP continues to assist the dti drafting team in the finalization of the Companies Regulations.

During the drafting of the regulations it became clear that a number of amendments would be required to the new Companies Act. A Companies Amendment Bill has been drafted and, at this time, is under review by Cabinet and various departments before being introduced in Parliament for debate and adoption. The drafting team, with major FSP participation, will have the amended Regulations, Forms, Rules, Fee Structure completed by end October 2010. If additional, unforeseen changes are introduced in Cabinet or Parliament in the Companies Amendment Bill, further updates may be needed.
The government has indicated that additional assistance will be requested from FSP once the Companies Act is in force to address policy issues, draft Implementing Guidelines, Practice Notes and other secondary legislative measures as needed. All aspects of implementation will be complex and typically present implementation difficulties and will require constant monitoring and technical assistance to make certain that the Companies Act is implemented as designed and in an efficient, timely manner. FSP is working with the dti to design forms, create simple rules and transparent processes, each with safeguards incorporated to achieve a smooth and transparent implementation of the Companies Act and Regulations. Considering that this extensive follow up work cannot at this stage be specifically described, no specific tasks have at this time been included in the work plan beyond the legislative approval stage at this time.

3.2.2: Develop proposed fee structure for the new Companies and Intellectual Property Commission. FSP has been extensively involved in the creation of a new implementation agency which will house all entities created under the Companies Act and already in existence under the intellectual property legislation.

During the last two years, FSP has undertaken the design and preparation of the business plan of the new Commission. Project staff will complete the comprehensive fee structure for the Commission designed to assure full cost recovery. FSP will also participate in the realization of the Commission's knowledge management role and designing mechanisms favoring SMEs moving towards formality in an SME-friendly business environment under the new Companies Act and Regulations. The dti has also requested FSP to document the impact of the final Fee Schedule on the adequacy of cost recovery and to lay the ground work for compliance for Annual Reviews and fee adjustments with the approval of National Treasury.

Photo by Gerald Meyerman of FSP)

CIPRO processes are cumbersome. Hundreds line up. The new Companies Act and Regulations to which FSP is providing extensive technical assistance, is simplifying administrative steps and designing protection against fraud.

3.2.3: Follow up work on insolvency policy framework harmonization and legislative reform. Based on the successful completion of the tasks described in Section 3.1.3 above, FSP anticipates remaining involved in the evolution of this important business environment component. The ultimate goal is to assure that all aspects of the insolvency framework and policy – although contained in various laws administered by various agencies – provides a seamless and careful integration of its various component policies, laws and oversight functions. FSP will assist the dti/NCR to define the scope and application of the NCA debt counseling and restructuring mandate as well as it interaction with the new Companies Act rescue provision and Insolvency Act and amendments to assure consistency and harmonization. FSP is also working with the World Bank as part of this research activity.

3.2.4 Support to the Government of South Africa Regulatory Impact Assessment (RIA) program. The GoSA recognized that for the Cabinet and legislature to exercise adequate and informed control over the legislative process, that additional, independent data was required to inform the process by clearly identifying problems to be addressed, describe the evidence that legislative action is the appropriate method for addressing the problem, identifying the cost/benefit of the legislative measures recommended for all stakeholders and form and present recommendations on whether the problem and solutions expected justify the cost of compliance and implementation to the private and public sector. Based on this, Cabinet mandated that a detailed RIA is required to accompany all new projects presented for legislative action.

National Treasury initially designated the new Companies Act and Regulations as the focus for the RIA component. During September 2009, FSP prepared detailed Terms of Reference in close cooperation with Treasury and prepared and obtained approval from USAID for the SOW for the RIA task, focused on the Companies Act. Shortly thereafter, a Notice of Rectification to correct errors in the Companies Act in 2008 was issued by dti. Therefore the Companies Act was no longer an appropriate target for RIA. Treasury, after consultation with dti, requested to focus the RIA instead on real estate legal reform. Estate agents are regulated by an inadequate 30-year old Act and mortgage brokers, called "bond originators", are entirely unregulated. The broad objective of these legal reforms is to protect the public against unethical practices of brokers and agents and encourage broader participation of historically disadvantaged in employment and equity in this sector. After consultation with FSP it was decided that the dti would proceed with the drafting directly and that FSP would support the RIA activity to be undertaken by National Treasury.

In order to build both public sector and private sector capacity to implement the RIA strategy, a joint international/domestic team has been provided to work with National Treasury to implement the FSP assistance.

Working closely with the RIA division in National Treasury and the dti, Stage 1 of this overall activity has been completed by the FSP RIA support team and a report generated to indicate the way forward. This report forms part of the presentation of proposed reforms to the real estate agents and bond broker legislation currently under review by Cabinet. When Cabinet has completed its review and makes the required policy decisions, it is expected that based on detailed input and control of National Treasury, FSP will proceed with the implementation of Stage 2 which will monitor the final design and drafting of various legislative amendments as well as potentially an entirely new Bill to regulate real estate transactions.

The dti has made it clear that, when the Companies Act and Regulations are in effect, it will be requesting a baseline RIA. Upon the completion of the "hands on" technical assistance, every effort will be made to assure sustainability of the lessons learned. National Treasury anticipates establishing an RIA portal and the knowledge developed during this RIA process will be documented and incorporated into the knowledge management tools available. FSP will also work with National Treasury to assure that practice guidelines for the implementation of RIAs throughout government are updated and finalized.

D. PIR 4: SME Knowledge Management System Strengthened

Knowledge management (KM) can be a powerful tool for the savvy FI and BSO. It can increase productivity, effectiveness and efficiency in management processes and/or practices. A more complete view of the SME market enhances the ability of an FI and BSO to understand new opportunities and solutions to challenges. Through collaborative mechanisms, FSP seeks to foster productive energies among SME financing stakeholders to maximize impact by leveraging the resources of our partners.

Therefore, the FSP Knowledge Management (KM) component seeks to:

- strengthen SME finance-related knowledge management,
- share innovative financing options and opportunities; and
- disseminate successful approaches for SME development in collaboration with private, government and donor programs.

There are a myriad of difficulties that SMEs encounter when trying to access finance. Many difficulties are being directly addressed by other FSP PIRs – such as creating a new or more complete range of financial products and services, better preparing SMEs for finance, reducing regulatory rigidities or addressing gaps in the legal framework. Overall, the lack of information on the SME finance market (among all the actors: banks, BSOs, and SMEs) is a constraint.

To help resolve this information gap FSP will collaborate with other stakeholders interested in SME financing and share expert opinions, ideas and solutions to challenges faced by the SME financing community. All knowledge management initiatives are oriented toward communications and, information sharing. These activities focus on enhancing market awareness of SME financial products and encouraging SMEs to productively access them. Information dissemination to FIs, BSOs and BDSPs will take priority to ensure that they are well equipped to support SMEs. While the knowledge management system targets the credit providers and advisors, SMEs (the ultimate beneficiaries) must know their options to be informed consumers of financial services and best grow their businesses.

Previously, FSP focused on identifying a single partner to collaboratively develop a knowledge management mechanism, but now FSP is facilitating a "community of practice" through the Financial Sector forum (www.fsp.org.za/blog) and through existing, multiple forums hosted by key stakeholders. Additionally, the project expended much effort on consummating *formal* partnerships with collaborating stakeholders. In Year 2 the project recognized *informal* collaborations as equally effective for knowledge management. This addition to the previous approach allows FSP to disseminate information through existing and new relationships. Contributions from both FSP and its partners to knowledge sharing system will contribute to this important sector.

Two key result areas support PIR 4:

KRA 4.1: Public-Private stakeholder collaboration in SME knowledge management expanded
KRA 4.2: Improved awareness of SME finance best practices

KRA 4.1 Public-Private stakeholder collaboration in SME knowledge management expanded

KRA Strategy:
FSP's approach to public/private collaborations employs a two-tiered approach that recognizes informal collaboration as a precursor to formal partnership. FSP will mine our existing collaborations with the Banking Association, dti, FIs, NSBC, ICSB, IBA, SAIPA and FABCOS to integrate their knowledge sharing in the wider sector. To augment the depth and breadth of the knowledge disseminated, FSP will continually recruit new knowledge management contributors, being institutions or individuals, public or private. One of the objectives of expanding FSP's work with these partners is to encourage them to contribute to FSP's knowledge management.

Activities:
4.1.1 Consolidate and utilize current collaborating partnerships. FSP will engage existing partners like the Banking Association, dti, NSBC, IBA, SAIPA and FABCOS among others to expand the collaboration to include knowledge management activities. In addition, monitoring and evaluation visits to FI and BSO partners will offer an opportunity to identify new knowledge management content contributors and will positively contribute to the growth and richness of discussions posted on the blog. FSP will maintain its strong partnership with the Banking Association, and continue to co-host at least four knowledge sharing events, where new collaborations will undoubtedly emerge to further solidify knowledge sharing within the sector. FSP expects a surge in the number of contributions to the knowledge management system as the target audience develops interest in knowledge sharing.

4.1.2 Identify new collaborating partners. FSP will network with stakeholders interested in SME finance knowledge management by attending workshops and events to develop partnerships to expand the community of practice. It is through such events that new partners will be identified to share best practices and innovations that increase market responsiveness to SME financing needs. Effective information sharing among partners can further disseminate successful approaches that result in increasing access to finance for SMEs.

PIR 4 Benchmarks

- 3 FSP partners contribute to FSP KM system
- 2 new collaborating partners identified
  - Communication strategy approved by USAID and implemented
- Post 32 content contributions to the blog

KRA 4.2 Improve awareness of SME finance best practices

KRA Strategy:
FSP strategy is to strengthen information dissemination systems. Building on the collaborations and challenges identified during the past two years of implementation, FSP will leverage all available resources towards information dissemination through coordinated symposia and through the Financial Sector forum. These forums will include such strategic

stakeholders as the dti, Banking Association, FIs, National Small Business Chamber (with an SME database of more than 20,000 members), International Council for Small Business, and other BSOs. The co-hosting, contribution and participation of FSP in these functions will be guided by our communication strategy which inherently supports the KM strategy success. Complementary to the knowledge management events, the project will actively utilize the Financial Sector Forum and nascent *FinFind* tool as rallying points and conduits for information dissemination for greatest market impact.

Activities:

4.2.1 Finalize communication strategy to support knowledge management strategy success. Guided by a strong, focused communication strategy, FSP will build on its relationships with the NCR, BA, NSBC and ICSB to facilitate regular information sharing forums. To ensure maximum return on such investments, FSP will ensure all its consultants conduct information dissemination events. This has been FSP's practice since project launch, but in Year 3 the knowledge management component of each assignment will be enhanced. The focus of these forums will be to tackle key sector challenges and provide solutions and recommendations to stakeholders. At least 12 such dissemination events will be conducted in Year 3.

4.2.2 Effectively manage the Financial Sector Blog for greatest market impact. Together with the dissemination events, the FS Blog will act as a clearinghouse for all communications targeting FIs, BSOs and other stakeholders engaged in supporting SMEs to better access finance. A target of 32 blog content contributions should be easily met with contributions from project component specialists and collaborating partners. By linking its blog with other complementary programs like SAIBL, dti (when its portal is launched) and other partners, FSP will promote information sharing with a broader audience. To ensure sustainability of the blog, FSP will begin identifying prospective partners to take over the management of the Blog when the project comes to an end. It is projected that the number of institutions and individuals seeking information on SME financing should increase to more than 450.

SECTION III: ACTIVITIES MATRIX – SEE ATTACHED PDF