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Pre-feasibility Study

Zimbabwe Venture Capital Report

Continental Capital (Private) Limited
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Produced by
SB Capital Corporation Ltd.
M.J. Kostuch
Nicholas Parker

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INTRODUCTION AND SCOPE OF WORK

"ZIMBANK REQUEST FOR TRAINING AND TECHNICAL SERVICES"
Task Order No. 23 - (Assignment 23A)
Harvey & Company, Incorporated

SB Capital Corporation Ltd. (SB Capital) has been retained by USAID in conjunction with the proposed launch of a new venture capital company in Zimbabwe, Continental Capital (Pvt) Limited (Continental), by the Zimbabwe Banking Corporation Limited, doing business as Zimbank. The Scope of Work Assignment (see Appendix 1) included the following responsibilities:

- conduct a one day Venture Capital Workshop in Harare for Zimbank management and potential investors on Tuesday March 24, 1992;

- determine the conditions required to assure the viability of successfully launching Continental Capital (Pvt) Limited including: deal flow potential; Zimbank's current management capacity to undertake a venture capital fund; availability of potential investors in the fund; exit strategies for fund investments; and assisting Zimbank in preparing an Offering Memorandum to attract private sector investors.

- prepare a pre-feasibility report on the potential viability of Continental Capital (Pvt) Limited including recommendations for future actions, future training and technical assistance required.

The SB Capital team of Mitch Kostuch and Nicholas Parker (Study Team) (see, Background and History of SB Capital, Appendix 10) visited Zimbabwe between March 21 and March 28, 1992. Activities included: extensive meetings with various Zimbank executives and other personnel; successfully completed the one day Venture Capital Workshop with the theme of "The Role of Venture Capital in Economic Development" (see List of Venture Capital Workshop Attendees, Appendix 6); individual meetings (some in company with USAID's Douglas Leavens and Don Greenberg) with venture capital, business and government leaders (see Appendix 2, persons interviewed); and two briefings of USAID personnel. For background purposes, members of the Study Team also briefly visited several retail and department stores, key Harare industrial areas and

nearby agricultural areas between appointments and on the weekends. These area visits included:

Heavy Industry: Willowvale, Workington and Southerton
Light Industry: Graniteside
Mixed Industry: Msasa
Agricultural: Norton, Nyabira and Banket

A drive through Chinhoyi "Growth Point" district was also included to obtain a sense of developments outside of Harare. This Pre-Feasibility Study on Continental Capital (Pvt) Limited and accompanying recommendations reflects the scope of this activity.

SB Capital's access to key Zimbabwean influentials for these meetings, and the quality of data presented at the Venture Capital Workshop, was positively impacted by earlier work done by SB Capital in developing countries, and specifically in Zimbabwe. In February 1992 SB Capital completed a shared cost Contribution Agreement Study entitled "Mobilizing Private Equity for Joint Ventures and Other Enterprise Financing in the Developing World" in conjunction with the Canadian International Development Agency (CIDA). This Study included a review of Southern Africa, and in particular Zimbabwe. Nicholas Parker had visited Zimbabwe in the late Fall of 1991 as part of this research project. The March 1992 USAID sponsored visit was Mr. Parker's fourth visit to Zimbabwe. Many of the persons interviewed had previously participated in the SB Capital/CIDA project, and data gathered as part of that study formed an integral part of the Venture Capital Workshop presentation and handout materials prepared in advance for distribution to the participants. SB Capital has also had extensive prior experience working on Capital Markets Development and Venture Capital Formation in developing countries in conjunction with the World Bank International Finance Corporation (IFC). These prior assignments included two field trips to Kenya.

As part of this study, SB Capital reviewed all available current research and economic reports on Zimbabwe, and Southern Africa in general. These are listed in Appendix 8, Publications, Literature and Materials Reviewed.

The Study Team would like to thank USAID and its personnel, in particular Mr. Douglas Leavens and Don Greenberg, for their active assistance and participation during their visit to Zimbabwe, and for arranging several of the key appointments required in preparing this pre-feasibility study on Continental Capital (Pvt) Limited. USAID reports

prepared by Mr. Douglas Leavens were also made available for review by the Study Team, and are included as Appendix 3 to this report.

EXECUTIVE SUMMARY

Working under Task order No. 23, Harvey & Company, Incorporated on behalf of USAID, an experienced two person venture capital Study Team from SB Capital Corporation visited Zimbabwe in March 1992 to conduct a one day Venture Capital Workshop, and to evaluate the conditions required for success of a proposed new venture capital company, Continental Capital (Pvt) Limited, sponsored by Zimbabwe Banking Corporation Limited (Zimbank).

This Pre-feasibility Study on the proposed Continental Capital (Pvt) Limited examined the political, economic, financial and regional environments for the development of private enterprise in Zimbabwe, the state of the venture capital industry, the availability of international support and assistance programs, and outlined a possible role for venture capital in that country. The team also focused on a variety of factors required for the success of Continental, recommended strategies that might be used, and suggested training and technical assistance inputs that should be considered to assist in the successful launch of the proposed new fund.

The Study found that while not all of the appropriate factors were yet fully in place, the rapidly improving environment for private sector investment and business growth in Zimbabwe was creating conditions that would lead to success of existing, and the proposed new, venture capital funds. These positive changes included the 1990 Economic Structural Adjustment Program which will increasing allow market forces to operate without state interference, opening up of the defacto one-party state run by the ZANU-PF party to permit opposition parties, Zimbabwe's above average economic performance compared to the rest of Southern Africa, revitalization of the ultra conservative financial sector, and the potential for positive change in the region because of the recent Referendum in South Africa with the potential for reduced strife in the region.

The encouragement of the private sector in Zimbabwe by fiscal and economic measures and training programs has already unleashed great interest in new enterprise formation and growth of private companies. In 1991, under government persuasion, the Venture

Capital Company of Zimbabwe was launched and is meeting early success, targetin relatively small enterprises seeking under Z$600,000. The four year old Hawk Venture fund has quietly completed 27 investments averaging more tha Z$1 million in size, an had six early winners and only one severe loss. Very early stage financing throug groups such as Manna Corporation, and the parastatal Small Enterprise Developmen Centre, is also making a contribution to the regeneration of the private sector.

The proposed new Continental Capital (Pvt) Limited is seen as being potentially wel positioned as a venture capital fund with strong sponsorship from Zimbank and sever other corporate or parastatal investors, and a proposed capitalization of Z$60 millior equity, backed up by Z$60 million of debt availability. Significant study of the venture capital process has been undertaken, and initial staff training for one key individua initiated, giving confidence in the chances for success. The new fund would be viable in the Zimbabwe environment with these resources, very much return on investment oriented, structured to provide value added services to investees, targeted at companies with fast growth potential, export development oriented and prepared to hold investments for an intermediate to long term period (3-7 years). It would provide both equity and quasi-equity (unsecured or partly secured debt), be prepared to do add-on investments as required, and to lead syndications by financing groups were initial investment requirements exceeded a targeted average Z$1.5 million per investment. Recently, The African Development Bank stated that "the demand from African entrepreneurs ... for financing is ... is so huge that no one institution can provide all of the answers."

To succeed, Continental will need experienced venture capital management assistance, on a declining basis, for up to five years as its new management group gains experience. Limited training for staff in the US is also recommended taking advantage of established venture capital training programs and related industry activities. The Continental Capital program should be supported by industry wide education and training through a proposed new venture capital association, formed informaly initially, but hopefully could be in a position to sponsor a two day industry conference or convention within the next year on a regional basis.

Recommendations concerning preparation of an Offering Memorandum for Continental Capital (Pvt) Limited have been discussed with Zimbank, potential investors and the proposed manager, and work on this is proceeding within that group. USAID is in a position to make a positive contribution to the success of the new fund, this support having already been initiated through sponsorship of the successful Venture Capital

Workshop held on March 24, and the input provided by the Study Team and USAID personnel while in Zimbabwe.

POLITICAL BACKGROUND

The ZANU-PF party, headed by President Robert Mugabe, has ruled Zimbabwe since the country's independence in 1980. The country is a defacto one-party state to the extent that 147 of the country's 150 parliamentary seats are held by ZANU-PF. However, in 1990 ZANU-PF's Politburo rejected a move to ban opposition parties. There are now signs that organized opposition to the government is growing quickly due to a variety of factors including allegations of rising corruption, distrust of its new economic policy and anger over government handling of the drought that is ravaging the country.

Initially, ZANU-PF was committed to transforming Zimbabwe into a socialist economy. However, the government's rhetoric has always outstripped its practice and in reality the bulk of the economy is still in the hands of the private sector. Where the government has intervened in the economy it has been as much to do with reducing South African influence in strategic sectors, and the desire to redress the gross inequalities inherited from the colonial era, as it has been for overt ideological reasons.

Cabinet approval in late 1990 of an Economic Structural Adjustment Program (ESAP) was in effect the final nail in the coffin of ZANU-PF's socialist ambitions. The ESAP is enshrined in the Economic Policy Statement presented to parliament in July, 1990 and covers the period 1991/95. Dr. Bernard Chidzero, the Senior Minister of Finance, Economic Planning and Development, stated as part of his government's budget speech, "Government has seen this to be the opportune time to do away with most...economic regulations, (and will now) allow market forces to operate in directing both the pace and the course of economic activities in Zimbabwe...The economy is currently subject to a host of economic regulatory mechanisms on prices, incomes, employment of labour and foreign exchange...the government is now convinced that these regulatory mechanisms have served their purpose..." The economic implications of the ESAP are covered in the section called Economic Developments.

From a political perspective, there is opposition to the ESAP. It comes mainly from ZANU-PF's old guard, the unions, parts of the civil service and the poorer section's of Zimbabwean society. The unions, however, are weak - representing only 2% of the total

labour force, and the poor are neither organized nor able to come up with any viable alternatives. The political old guard have been shaken by the collapse of Communism in Eastern Europe and have fallen silent. The civil service is unlikely to mount any substantial opposition on its own. Quietly, there are elements of the business community that have grown comfortable under a relatively-closed economy who are also fearful of economic liberalization, but they do not represent the new wave of entrepreneurs in the country.

On the positive side, the emerging black business community, the financial sector and most senior government officials are solidly behind the ESAP. The government is also making a strong effort to win the support of the rural population. Furthermore, ESAP supporters have been moved into key economic decision-making positions. As many observers note, Zimbabwe has a better chance of success with economic reform than most of its African neighbours.

The most important challenge to the success of the ESAP and the continuation of ZANU-PF rule comes from the drought currently affecting the entire Southern Africa region. It is the worst drought on record and some experts suggest that Zimbabwe could even run out of staple food items by May 1992. Many Zimbabweans feel that the government has bungled the crisis brought on by the drought. Others believe that if hunger persists or increases, disenchantment with ZANU-PF could grow to the point where its position as governing party is seriously threatened.

The government has tried to address the problem of overcrowding and environmental degradation in the "communal areas" - rural land where blacks live - by recently introducing legislation giving the state the power of compulsory acquisition of commercially-owned (mainly white) farm land. This is a hotly disputed move, not over the need to redistribute land, but because of the way the government is going about it. Some observers also feel the government is jeopardizing commercial agriculture which is the dynamo of the Zimbabwean economy. Aid donors, including the influential World Bank, are putting pressure on the government to modify the Land Acquisition Act to introduce greater accountability and transparency. They are unlikely to achieve much success as ZANU-PF sees land redistribution as one of the few ways it can hope to garner enough support to win the next election.

On the international front, Zimbabwe has not altered its hostile stance toward the South African government. Unlike many of the other front-line states - including neighbouring Zambia - Zimbabwe has not softened its tone vis-a-vis Pretoria (although it should be

noted that trade relations have always continued unimpeded since 1980. In 1989 merchandise exports to South Africa reached Z$248,110,000, exceeded only by exports to the United Kingdom and well ahead of merchandise exports to the United States and West Germany). Increasingly, Zimbabwe looks out-of-step with regard to South Africa, at least on the political level.

Elsewhere, Zimbabwe has consolidated good relations with the US and other western governments who are anxious to see the ESAP succeed. Zimbabwe supported the allied side in the Gulf War although it recently abstained in a UN Security Council vote to impose sanctions on Libya over its terrorist activities.

ECONOMIC DEVELOPMENTS

During the first ten years of independence, Zimbabwe's macroeconomic framework was highly interventionist; the public sector share of Gross Domestic Product (GDP) rose from a fifth to a third, numerous new public enterprises were established, and pervasive controls were applied to prices, wages, industrial relations, all foreign currency transactions and investment decision-making. Tax and public expenditure ratios rose sharply and the budget deficit averaged 10% of GDP in the second half of the 1980s.

Nevertheless, Zimbabwe's post-independence economic performance has not been poor: real GDP has grown at 3.3% annually since 1980, well above the 2.2% annual average for Sub-Saharan Africa as a whole, and enough to ensure a marginal improvement in real income per head.

The country also has a strong private sector, a diversified industrial base, an efficient infrastructure, prosperous commercial farming, varied mineral resources, a developed capital market and a plentiful, if still inadequate, supply of skills. Indeed, it is difficult to quarrel with the view that if Zimbabwe's structural adjustment program fails, it is not going to work anywhere in Africa.

Zimbabwe can claim to be the most industrialized state in the region with manufacturing accounting for a quarter of GDP in 1990, easily more than double the African average of 11%, and well above Nigeria's 10%. Zimbabwean manufacturing value added has grown at more than 5% a year since 1984 and has been the main source of national economic growth.

Since 1988, the ruling ZANU-PF government has been shifting the emphasis of economic policy toward a market economy. This shift has now been formalized in the five-year Economic Structural Adjustment Program, published in mid-January, 1991. The Framework for Economic Reform (1991-95) sets out a range of economic, and social, policies designed to stimulate investment and remove the remaining impediments to growth. The incentives being offered to the private sector are discussed in the section called Encouragement of the Private Sector.

The five-year ESAP envisages foreign financing of $3.4 billion to achieve a 5% annual growth rate. Retooling of industry has commenced with borrowing from the African Development Bank and the IFC. At the Paris donor conference held in March, 1991, US$700 million was pledged as the first tranche of the estimated foreign finance requirement. The second Paris donor conference was held in February 1992 and more funds have been pledged although there is concern in Zimbabwe over the slow pace of disbursement of aid flows.

Zimbabwe's ESAP is generally on course, although there is slippage, especially in public sector reform which partially explains why donors have been slow to loosen their purse strings. However, inflation remains a threat as much for political as for economic reasons. And the crisis brought on by the drought will put pressure on the country's balance of payments, negatively affect economic growth prospects and increase the political heat on the government. Also, the economy has to absorb nearly 300,000 school leavers each year.

Almost 50% of Zimbabwe's population of 9.5 million persons is under the age of 16, with students enrolled in various levels of education programs exceeding 2.2 million persons. Creating employment for current and future school leavers presents a major challenge for the government and the economy. The present tax base is very narrow and must be expanded. The most recent available data shows that only some 6000 companies paid taxes, out of more than 50,000 registered companies, many of which are directly or indirectly parastatal and therefore pay no taxes. Only some 200,000 citizens paid income taxes, out of a population of 1,200,000 salary earners in business and government.

The informal economy has grown substantially, filling needs not provided by the socialist directed government of the 1980's. The Zimbabwe National Chamber of Commerce estimates that as many as 800,000 "informal businesses" exist in the underground economy.

For many, trade and foreign exchange reform are at the heart of the changes to which the government has committed itself. In essence, the government is to move away from the present system, of administered import controls and the granting of licenses and forex allocations, to an exclusively tariff and tax-based system of protection by 1995. In the interim, there will be a progressive shift of more and more goods on to what is called Open General Import License. Initially, unrestricted imports are to be raw materials, followed by intermediate goods, capital and finally consumer goods.

Some Zimbabwean industrialists are fearful of trade liberalization because of the prospect of low-cost competition by producers in the Pacific basin and in Europe. Yet this gloomy assessment conflicts with World Bank research that suggests that more than half of the country's manufacturing industry is efficient, and only about 12% highly inefficient.

REGIONAL DEVELOPMENTS

In the 1990s, investment in Zimbabwe will depend on the potential investor's assessment of the entire regional market. In other words, the economic and political climate to be assessed is not that of Zimbabwe alone, but of all of Southern Africa, including South Africa. As such, it is encouraging that, for the first time in a long time, it is possible to take a positive view of the prospects for the region.

Since the beginning of 1990, several significant and positive events have taken place, including:

- Namibia has attained independence, opening the way to the kind of minerals-based economic growth witnessed over the past two decades in neighbouring Botswana.

- Zambia has held multiparty elections, offering the prospect of economic reform and a resumption of economic growth in the medium-term, based on the country's substantial agricultural potential.

- Angola has ended its civil war, enabling Africa's most oil-rich state to begin the task of reconstruction and

development, although substantial non-oil investment will be restricted to social and economic infrastructure for the foreseeable future.

- South Africa has abolished many of the legislated features of apartheid and is starting down the path to constitutional negotiations, thus providing hope that the country can begin to unlock its enormous economic potential and serve as the region's industrial workshop. The March 1992 Referendum strongly supporting the present government's initiatives in changing the laws of the nation to promote equality for both blacks and whites is a major step forward in stabilizing change in the region.

The future of South Africa holds the key to the prospects for the rest of the region:

- South Africa holds the key to a settlement of the civil war in Mozambique;

- South Africa will determine the future of the customs union it currently operates with Botswana, Swaziland and Lesotho;

- South Africa will strongly influence monetary arrangements in the region, possibly turning it into some form of "rand-zone";

- South Africa will largely determine what kind of common economic space and trading regime emerges for the region; and

- South African economic prospects will play a major role in driving the economic fortunes of its neighbours.

Some observers are worried that South African competition will lead to the deindustrialization of Zimbabwe. However, as a recent Economist Intelligence Unit, February 1992, report points out (Zimbabwe in 1996 - at the Heart of a Growing Region, Roger Riddell), Zimbabwe has already stood up to South African competition. In the last

three or four years Zimbabwe has won sizeable orders over both South African and overseas competitors in Southern and Eastern African countries for a range of more sophisticated manufactured products, including pharmaceuticals, pest control chemicals, mining cars, electrical cable, a range of boilers, medical equipment, radiators and parts, agricultural equipment, sweets and chewing gum. For both transport and agricultural equipment, Zimbabwean products have a reputation across the region for quality and durability.

Clearly, South African competition poses a stiff challenge for Zimbabwe but perhaps a more important concern is the potential brain drain away from Zimbabwe to the bright lights of Johannesburg and Capetown. On the other hand, the superior quality and discipline of Zimbabwean workers in relation to their Bantu-educated, South African counterparts might serve to pull South African industry and skills in the other direction. The example of indigenous "multinationals" such as TA Holdings Limited, a publicly traded industry and services conglomerate, should serve as inspiration to other Zimbabwean firms considering regional expansion into South Africa and its neighbouring countries.

ENCOURAGEMENT OF THE PRIVATE SECTOR

Zimbabwe's private sector is probably the strongest in sub-Saharan Africa - after South Africa. It falls into three distinct categories:

- a large, powerful multinational sector, dominated by traditional British multinationals, though with a very strong South African presence, while several leading US and European multinationals also operate in Zimbabwe.

- a strong indigenous business sector with a broad spread of small to medium sized companies owned and managed by white, Asian and black Zimbabweans.

- a numerically huge informal sector, mainly comprising communal land farmers, but also including large numbers of micro-businesses and informal traders in rural and urban areas.

The country's investment climate has been the topic of several serious research studies, most notably the World Bank's "Private Investment and Government Policy" (May, 1989).[1] All such studies have reached basically the same conclusions. Namely that Zimbabwe's poor domestic and foreign investment record since 1980 can be explained by:

- severe supply side constraints on investment - most importantly the non-availability of imported capital equipment and inputs;

- the weakness of the capital goods and construction industries - both constrained by scarce forex allocations and an aging capital stock;

- the crowding out of the private sector by the public sector - especially in terms of access to forex;

- the highly-restrictive and over-regulated business environment;

- a "relatively" high cost of capital, especially for foreign firms.

These bottlenecks have now been recognized by the Zimbabwean government. Under the ESAP the authorities have initiated a series of macroeconomic reforms, discussed in more detail in the section on Economic Developments, that are aimed at liberalizing the business environment by removing price controls, freeing the labour market and making interest rates more market sensitive. In addition to these macroeconomic policies, the government has strengthened its incentives for the private sector at the micro level.

[1]This section of the report draws on the study Critical Issues for American Investors in Zimbabwe, authored by Nicholas Parker and edited by Tony Hawkins.

INVESTMENT AND EXPORT INCENTIVES

The incentives being put into place under ESAP are almost wholly geared towards exports and export-oriented projects, and they build on those incentives included in the new investment code launched in April 1989 under the title of "The Promotion of Investment: Policy and Regulations." The document "Export Incentives and Institutional Support for Industry", produced by the Confederation of Zimbabwe Industries and updated to December, 1991, covers in greater detail the incentives available to the private sector. What follows is a summary, from the perspective of this report, of the most important incentives now in place.

Export-oriented enterprises are now given special access to forex in order to facilitate imports through the various export incentives schemes. The main export incentives, which will continue until the OGIL system makes them redundant are:

1. An **Export Revolving Fund**: manufacturers now producing for export are assured of automatic access to forex (up to 45% of the value of imports) to finance the import content of their products.

2. An **Export Retention Scheme**: allows exporters to retain 25% - and going up to 35% in 1993 - of export receipts from the previous six months, to purchase imported raw materials and capital goods for existing product lines. Items thus purchased can used on the local market, provided they are not on-sold. While the SB Capital study team was in Zimbabwe, Raymond Gripper, Managing Director for Johnson & Johnson (Pvt) Ltd. commended the Export Retention Scheme, pointing out, "We have now started to export as much as possible so that we will generate more foreign currency and retain some which we can use to expand our activities."

3. An **Export Incentive Scheme**: Non-traditional exporters receive a tax free cash payment equivalent to 9% of the value of their exports, providing the goods to be exported have a minimum local content equivalent to 25% of the export value.

It should be noted that the government has also recently established Zimtrade, a joint public-private sector body that effectively moves the responsibility for export promotion out of the government bureaucracy and into the marketplace. Zimtrade is to assist aspiring and existing exporters through the provision of information, technical assistance and grants for overseas travel.

The government has moved to make foreign investment more attractive, including more favourable treatment of capital repatriation and profit and dividend remittances. It is committed to removing all exchange control restrictions on dividends and profits before 1995. The current regulations allow foreign investors to remit 50% of their net after-tax profits arising out of their investment(s), and up to 100% for a stipulated period in special cases - so called New Venture Capital (NVC) status. Dividends in excess of the 50% mark for companies not qualifying for the special dispensation are credited to blocked accounts and must remain invested for five years before qualifying for disinvestment rights.

Two years after their new investment, foreign companies can disinvest and remit the proceeds equal to the amount of their original investment, less a deduction of the amount of income from the investment remitted before the disinvestment. The amount deducted, together with any capital gains made on disposal, can be remitted through the six-year, 4 per cent tax free, Government External Bond procedure. Local borrowing rules have also been relaxed for foreign investors, including special access to blocked and surplus funds.

The question of blocked and surplus funds is fully discussed in the government's investment code, the most recent version being that of September, 1991. A key feature of the blocked funds is that they can be bought by foreign investors at a discount of from 60% to 80% to fund investment projects. Such "switched" funds qualify for NVC status.

Tax levels in Zimbabwe are fairly punitive by international standards but the government is making an effort to gradually remedy the situation. Corporate income tax is 45% although it will be reduced to 42.5% in fiscal 1992, which is a significant improvement over the 50% level of 1990. There are also special allowances for, among other things, investment in so-called Growth Points and training.

Other important taxes that inhibit investment include a capital gains tax of 30% and, for foreign companies, a range of withholding taxes on dividends (20%), interest (10%), fees (20%) and royalties (20%).

The Zimbabwe Investment Centres (ZIC) now vested with legal authority to receive, process and authorize all projects below Z$10 million - up from the original Z$5 million - to promote investment activities, to recommend and coordinate the setting up of free trade zones, and to recommend the granting of particular incentives for approved

projects. Other measures have also been taken to improve investment approval procedures. As a result, it is confidently anticipated that all projects - domestic and foreign - will be processed well within the 90 day period laid down in the investment regulations.

Headed by the dynamic Nick Ncube, Director,the ZIC promises to play an important role in reducing the "red tape" obstacles faced by local and international firms wanting to start or expand businesses in Zimbabwe by affording them "one-stop shopping". Perhaps a useful measure of Director Ncube's interest in development of the private sector was his attendance at the USAID/SB Capital Venture Capital workshop where he was an active participant in discussion of the role of venture capital in economic development. He also subsequently met privately with Mitch Kostuch of the SB Capital Study Team, where discussion focused on the potential job creation and economic multiplier impact of private sector venture capital investment.

Additionally, in September 1989 Zimbabwe joined the Multilateral Investment Guarantee Agency of the World Bank and in June, 1990 signed the US's Overseas Private Investment Corporation (OPIC) Agreement, which provides insurance to US companies investing in countries with which OPIC has an agreement.

TRAINING PROGRAMS

While it has no capital under management, the newly-created Indigenous Business Development Centre (IBDC) has developed a five-phased program to help retrain civil servants to start their own businesses. The program is being operated in cooperation with the Public Service Association which has a membership of 40,000, 25% of whom will leave the government over the next five years. Mr. C. Siziba, Managing Director of the IBDC, participated actively in the USAID/SB Capital Venture Capital Workshop as both a speaker and in active discussion among participants. In particular, Mr. Siziba emphasized the importance of private sector management and economic training as a key role for IBDC. While recycling of former civil servants was a principal focus because of their better than average education and practical experience in government, all indigenous business was of importance to the IBDC.

The Small Enterprises Development Company (SEDCO), a parastatal body created in 1984 to facilitate the growth and development of small businesses, runs training

programs which are considered to be of good quality. SEDCO's mandate is to help emerging businesses with starting capital and business expertise. While the SB Capital Study Team was in Zimbabwe, 29 small-scale entrepreneurs from the Matabeleland region took part in a three day business management course in Bulawayo, many of them being funding clients of SEDCO.

In 1991 SEDCO established the Counselling Assistance to Small Enterprise (CASE) Program modelled on the program of the same name in Canada established by Canada's Federal Business Development Bank. This program is designed to make available to small businesses and entrepreneurs the services of experienced local business persons, usually retired or semi-retired, matched to the specific needs of the business. CASE has some 90 registered Counsellors at March 1992. The business owner pays CASE Z$60 per day for the service (or nothing in special cases) which is then paid to the Counsellor. CASE absorbs all travel and out of pocket cost, and overhead costs. Two recent investments made by the VCCZ were CASE assisted companies.

The Confederation of Zimbabwean Industries (CZI) also runs highly regarded training programs for business managers although there is some concern that these programs do not reach many of the more promising entrepreneurs, particularly those not based in either Harare or Bulawayo.

The Zimbabwe National Chamber of Commerce also focuses on training for entrepreneurs and personnel in the small/medium sized (SME) sector. In particular it established in 1990 a program of Small Business Support Units (SBSU), funded by the German Friedrich Naumann Foundation, which travels throughout the country in specially equipped trucks offering training and skills development programs outside the major centers. Developed to encourage the growth and expansion of the free enterprise sector, the SBSU focus on both training and consultancy services.

"Zimbabwe has no shortage of opportunities, there's plenty of deals that will be flushed out as the government's ESAP program bites," Chamber of Commerce President Jim Toland said in an interview. "There is, however, a skills shortage, a shortage of practical experience, that must be overcome. To some extent such training is a saturated market in the larger centers as more and more private sector programs are developed, but away from the major cities there is a great deal of work to be done."

The University of Zimbabwe has a business school which runs undergraduate and postgraduate programs including an MBA course. Enrolment at the University of Zimbabwe stood at 8,123 students in 1989. Other colleges in Zimbabwe, such as agricultural and teachers colleges, had a 1989 enrolment of 16,727. While the SB Capital Study Team did not have time to visit with any of these schools, anecdotal comments from several other interviews indicate substantial ferment in favour of free enterprise mechanisms is being generated on campuses as the changes in Zimbabwe's economic system develop.

EXPORT POTENTIAL AND INVESTMENT OPPORTUNITIES

The principal high growth potential export opportunities must in the main part be based on Zimbabwe's abundant natural resource base. However, the country's exports are not going to grow fast enough without the combination of new equipment, skills and technologies and a new outward-looking culture. Industrialists are going to have to give much greater attention to quality (which means that access to imported packaging materials will be highly important), as well as service. These realities suggest that Zimbabwean firms need to find international partners who are prepared to engage in joint-venture, licensing, management and other agreements. Many US medium-size firms would make ideal partners in this respect.

For local, US and international investors there are a broad range of business opportunities which go beyond the extractive sectors. Among the areas of opportunity that might be attractive to these investors are:

Textiles and Clothing: Zimbabwe already has a sophisticated garments industry, with a high degree of backwards integration. High quality cotton is produced locally and relatively cheap and well educated labour is available.

Horticulture and Fruit: Zimbabwe is developing an international reputation as a supplier of flowers and fruit all year round. There is scope for investment in direct production and related activities - processing and above all packaging.

Tourism: A combination of regional peace with significant investment in hotels and ancillary facilities, boosted especially by increased international tourist traffic to South

Africa, could lead to a rapid expansion of international tourism to Zimbabwe, based initially on Victoria Falls, and thereafter on the country's well-stocked game parks.

Capital Goods: Zimbabwe has an embryonic capital goods sector. With its iron and steel industry and existing capacity to export heavy equipment, there will be opportunities to export to other African countries, however, this will be an area of intense international competition from South African and Asian suppliers.

Food Processing: As a significant food producer and exporter, there will be opportunities for export-oriented food-processing activities. Canned meat, fruit juices, and malted barley are but a few examples.

Location-specific Mining: This could be the sector of most rapid growth over the next five years with expanded production especially of gold, ferrochrome, nickel and black granite, new production of platinum, and also of diamonds and asbestos products.

Services: Opportunities can be found in Zimbabwe's underdeveloped service sector although export opportunities are few. In the mining industry, for example, opportunities include: geographic mapping, environmental engineering, computer consultancy, and laboratory services. There also appears to be great potential for forex earning through an expansion of trade in services through international data capture. Zimbabwe is also well-placed to become the regional banking and financial centre. Other service opportunities can be found in consulting, health care, education and training.

Infrastructural Activities: Heavy investment will be needed in Zimbabwe's infrastructure - especially telecommunications and transport - during the 1990s. Opportunities will arise for the production of local inputs, with the prospect of exporting to other African countries whose infrastructure needs rehabilitation - Malawi, Mozambique, Angola, Zambia, and Tanzania.

Industrial Inputs: There is a range of opportunities to supply intermediate products to industry. The Industrial Development corporation, for instance, is investigating investment projects for production of hydrogen peroxide, wood chemicals, lace fabric, ammonium paratungsgate, building and construction materials, tractor and vehicle spare parts, ball bearings and industrial magnets.

In terms of regional markets, the real potential lies in export outside of SADCC to South Africa, Botswana and some of the wealthier West and Central African economies

(including those in the hard currency CFA zone). Clothing, textile, footwear, furniture, chemicals, and some machinery all have the potential to develop markets in the region and within South Africa itself.

In terms of off shore markets, the EC offers the greatest opportunities because of the Lome Convention, which provides African states, among others, with duty-free access to the markets of the EC's twelve members states, with the exception of certain agricultural products which come under the EC's Common Agricultural Policy. The Lome Convention makes Zimbabwe a very attractive potential manufacturing or product assembly site for US or other industrial companies seeking to access the EC market, particularly when it involves labour intensive products. Zimbabwe becomes a good location for a joint venture, partnership or a production agreement to produce such products.

The combination of attractive investment opportunities, positive factor endowments - the low cost of electricity and water in some areas - can, for example, provide substantial cost advantages over other parts of the world - an economic liberalization program and access to regional and European markets means that Zimbabwe is increasingly attractive to the US and other international investors it needs to attract. The role of international agencies and private intermediaries in facilitating these new partnerships could be crucial.

FINANCIAL SECTOR, STRUCTURE AND RECENT DEVELOPMENTS

THE FINANCIAL SECTOR

Zimbabwe has a sophisticated and diverse financial sector, with a banking system based on the British model.

The Central Bank is the Reserve Bank of Zimbabwe, which acts as banker to government, issues currency and government loans, controls foreign reserves, acts as lender of last resort to the commercial banks, administers the exchange control legislation and handles gold output. The main commercial banks are Barclays Bank of Zimbabwe, Standard Chartered Bank, ANZ Grindlays Bank, and Zimbabwe Banking Corporation Limited (Zimbank) in which the Government has a 58.3% stake through its purchase of the South African Nedbank holding. Both the Government of Zimbabwe and

management of Zimbank have publicly stated the Government's intention to "privatize" the bank by sale of additional shares, to the public, on the Zimbabwe Stock Exchange. This was to have happened earlier in 1992 but a drop in share prices on the Stock Exchange resulted in a decision to delay the issue so as to not further destabilise the market. (See Zimbank, Group Annual Report 1991, Appendix 9).

There are four merchant (investment) banks, three discount houses, five registered financial institutions, three building societies, an export credit insurance corporation, and about 50 registered insurance companies. There is also one agricultural finance company, a post office savings bank, a small enterprise development corporation and one large venture capital company (see below), a stock exchange (see below) and a national development bank.

The Zimbabwe Development Bank began operations in 1985 with authorized share capital of Z$50 million; it is 51% owned by government, but has a number of foreign banks and developmental organizations in minority positions. It concentrates its activities in the manufacturing sector.

The merchant banks offer acceptance and loan finance, open letters of credit and arrange external lines of credit. They also provide services in the areas of corporate finance, project finance, countertrade and portfolio management.

Three of the five registered finance houses are subsidiaries of the commercial banks. For many years their main activity was providing hire purchase facilities for vehicles and other consumer goods. But the trend in recent years has been towards a more long-term and productive business such as leasing, lease-back and factoring.

During the 1980's, as was the case prior to independence, the Zimbabwean financial sector has operated under government protection and control. As a result there has been little real competition. Banks have also traditionally been highly conservative and risk-averse, making finance difficult to obtain for SME's not able to offer sufficient security to lenders. However, under ESAP, the financial sector is now becoming more active with both policies and attitudes showing signs of positive change. Nevertheless, there is still a large gap for long-term and risk financing in Zimbabwe which might only be addressed through the entry of new players into the financial market.

Recent government initiatives such as the Small Enterprise Development Program which combines loan financing with business management training (see Encouragement of the

Private Sector section) fill an important low level gap in the financial markets. Established players such as Zimbank are also playing a growing role in private sector entrepreneurial financing, having created the Small Business Services Division in October 1990. This Zimbank unit focuses on rural economic activity with emphasis on activities run by women. In its first seven months this unit assisted 146 small projects providing Z$3.8 million of financing.

THE ZIMBABWE STOCK EXCHANGE

Zimbabwe's small stock exchange is controlled by a modern and sophisticated Act. Dealings are limited to local stocks and to South Africa stocks, the later being acquired within a "blocked rand pool". There are 63 Zimbabwe-based firms listed on the exchange. However, many of these listed firms are in fact holding companies such as TA Holdings, encompassing dozens of subsidiary firms which could be listed separately in the future.

Share prices on the Zimbabwe Stock Exchange have risen consistently since 1984, interrupted from time to time by market fluctuations reflecting international market changes as well as local conditions. The three main reasons for this long term increase in share values are:

1. The scarcity of investment opportunities in an excessively liquid capital market. The main alternatives to equity investment are government stock, on which yields for most of the post-independence period have been negative in real terms; and property, whose attraction as an investment has been undermined by rent controls.

2. Strong profit and dividend growth have boosted share prices. Pre-tax profits of listed industrial companies doubled between 1985 and 1988, increasing 50% in constant dollar terms. Over the same term, dividends went up 120%, or almost 60% when adjusted for inflation.

3. Share prices have been rising to reflect the inflationary revaluation - in local currency terms - of real assets.

Institutional investors have played the dominant role in driving prices up. While a substantial volume of institutional money has been invested through the secondary market in quoted equities, very little to date has been channelled through new issues into the private sector. By contrast, because pension funds and life assurance companies are required to hold 60% of total assets in prescribed investments (government, local authority, and parastatal), this has allowed the Government to fund its budget deficit in a largely non-inflationary manner through the issue of domestic stock. Indeed, during the 1985-88 period, insurance companies and pension funds bought Z$1.2 billion of Government stock - more than 40% of the stock issues.

MONETARY POLICY

In October, 1989 the Reserve Bank introduced the base lending rate (BLR), with minimum interest rates on deposit and savings accounts rather than maximum rates prescribed. In accordance with ESAP, the plan is to eliminate administered interest rates by 1995. Thereafter, open market operations will become the main instrument for money market intervention to regulate monetary aggregates and interest rates.

It is anticipated that new banks and financial institutions will be established in the country, with an eventual open entry policy. Overall, however, the pace of monetary reform is tightly linked to the ability of government to maintain control over the fiscal deficit. The goal, in short, is to establish positive interest rates to attract savings and reduce inflation and, as a result, ensure a monetary regime suited to a market economy.

ZIMBABWE'S VENTURE CAPITAL INDUSTRY

Zimbabwe is the only country in the region other than South Africa to have local venture capital funds. The most prominent venture capital company is the Venture Capital Company of Zimbabwe Ltd. (VCCZ), set up in 1991 with assistance from the IFC to provide SMEs with equity financing for start up and expansion. The IFC has made an investment of $1.7 million in the company. Other sponsors of the VCCZ are the Reserve Bank of Zimbabwe (20%), Commonwealth Development Corporation (CDC) (10%) and local banks including Barclays Bank of Zimbabwe, Standard Chartered Bank, ANZ Grindlays, and Zimbank (held through its presently 100% owned Continental Capital (Pvt)

Limited subsidiary) which will collectively have 40%. In total seven industrial firms, five insurance companies, nine commercial and merchant banks are included in the shareholder group.

The VCCZ has committed capital of Z$50 million and a Z$10 million quasi-equity base consisting of 5% convertible debentures subscribed by local shareholders, private companies and insurance firms. It is envisaged that the VCCZ's shares will eventually be floated within five years to the general public through the Zimbabwe Stock Exchange to allow those shareholders who wish to liquidate their holdings to do so at fair market value.

The initial response to the VCCZ has been positive. Over the July-November 1991 period it received investment enquiries worth an equivalent of US$24 million and has approved investments worth US$1.5 million. There is considerable concern, however, over the role of the Reserve Bank in the company which is expected to exert considerable pressure on the company to include non-commercial criteria such as job creation in its project appraisal process. Apparently, most of the local industrial firms and financial institutions who invested in the fund did so after substantial "moral suasion" from the authorities.

Mr. Chris Mwaturura, Managing Director, VCCZ took active part in the USAID/SB Capital Venture Capital Workshop. Subsequently USAID's Doug Leavens and Don Greenberg and SB Capital's Mitch Kostuch met with Mr. Mwaturura and VCCZ Chairman J.A.L. Carter (Chief Executive, Apex Corporation of Zimbabwe Limited) who confirmed that VCCZ's target investee requires financing of Z$200,000 to Z$600,000, averaging Z$250,000 (US$50,000) to date. Mr. Carter was forcefully explicit that this size of enterprise was VCCZ's principal mandate, "We are looking less at the profit motive, and more at the development aspect in our activity," Mr. Carter said. He further defined its role by focusing interest on a "South-South" economic development axis, rather than "North-South." "A hand made nail technology employing 15 workers, based on experience in India, will certainly be of more interest to VCCZ than high-tech machinery technology from the North that could produce all of the nails we need from one location." He cited several other examples of such small scale, low-tech enterprises as targets for VCCZ funding.

VCCZ's management is being actively supported through the presence of a full time, experienced venture capital manager provided by UK based 3i's. David Jackson is 25 years old so as not to intimidate VCCZ management, is technically qualified as an

investment officer, and assists in the development of systems and procedures. His annual contract can be extended for up to three years.

There are several other venture capital investment groups in Zimbabwe. One is Hawk Ventures, a fund managed by the reputable First Merchant Bank of Zimbabwe, funded by the Anglo American Pension Fund. Established just over four years ago, Hawk Ventures has 20 companies in its present investment portfolio, three of which are second time investments with previous investee management. Cost of the present portfolio is Z$23 million. The venture capital fund has successfully divested six investments at a profit, and had one significant loss. Fund managers Paul Maarschalk, Manager Corporate Finance, and John Graham, Assistant General Manager, advised SB Capital that, "it is the company's policy to maintain a low profile." Investment leads are generated through the First Merchant Bank network, through financial intermediaries such as accounting and business advisory firms and by investees. Fund managers (four persons with three support staff) also handle the First Merchant Bank's Capital Markets portfolio, as well as other investment activities for the Bank. Hawk Ventures management has benefitted directly from expertise provided by Anglo American Pension Fund who are also investors in several venture capital funds outside of Africa.

Another local venture capital source is Questor Venture Capital Fund, established in 1986, which has been managed by the Merchant Bank of Central Africa, and has been dormant in recent years. It is being rehabilitated by EDESA S.A., supported by a USAID/AVCP financed feasibility study now under way. Formal decisions on restructuring of Questor and its proposed sale to EDESA are expected in mid-April. This could lead to an increase in Questor's capital to Z$20 million, with a maximum of Z$2 million to be placed in any one investment. Equity participation in any investee would be in the 20% to 35% range.

Another potential local venture capital company is Ipcorn, established in 1958, which is managed by the investment division of Old Mutual, the largest insurance company in Zimbabwe. Old Mutual are also a potential investor in Continental Capital (Pvt) Limited, proposed by Zimbank. Ipcorn has a portfolio of about US$10 million, is managed on a part time basis, but at present all of its investments are made on a permanent basis.

The Zimbabwean government established the Small Enterprises Development Company (SEDCO) in 1984 to facilitate the growth and development of small businesses. SEDCO has funded through term loans over 1000 projects worth over US$5 million. SEDCO has,

however, been unable to meet demand and has, to date tended to concentrate on traditional areas such as printing, retailing and grinding mills.

Senior SEDCO Development Officer Trust Mateta reported that currently an average of 35 new clients per day are coming to the Bulawayo office alone. "Many people are now coming to SEDCO because our interest rates are reasonable, 18% for rural people and 19% in urban centers," Mr. Mateta said. SEDCO offers loans of up to Z$500,000 with repayment periods of between three and 10 years.SEDCO is presently capitalized at Z$56 million, of which USAID has provided Z$12 million and CIDA Z$31.3 million. In addition, SEDCO can draw down a World Bank line of credit of US$10 million. At the present time SEDCO is reviewing its mandate (small business loans and training programs) with a view to setting up a venture capital type equity program (modelled on the Canadian based Federal Business Development Bank program) aimed at micro and start-up business. This study is scheduled for completion in early summer. (See also Encouragement of the Private Sector, Training Programs section.)

It should also be mentioned that there are several private small-scale enterprise schemes operating in Zimbabwe. One is the Manna Corporation which is financed by approximately 47 individuals who are prepared to take a hands-one role in investee companies as well as providing small amounts of capital, frequently in hard currency. The group has current capital resources of about US$200,000. This operation has invested in a number of small manufacturing ventures, most notably Tropical Headgear in Bulawayo. Manna's intervention is normally fairly short-term (up to three years) after which it aims to divest and move on to other projects. Manna is actively seeking additional capital to expand its investment program.

There is also the Zambuko Trust which is designed to provide small unsecured loans to informal sector entrepreneurs. This is geared to a much larger number of investments than Manna but on a much smaller scale. Zambuko is still fairly new and therefore figures on its activities are not yet available. Several well-known non government organizations (NGO's) are also active in financing micro-level entrepreneurship. Women's World Banking, for example, has recently established operations in Zimbabwe.

INTERNATIONAL VENTURE CAPITAL AND ASSISTANCE PROGRAMS

The multilateral and bilateral development institutions have created several mechanisms to finance ventures initiated by African entrepreneurs, including those in Zimbabwe.

The World Bank IFC set up the Africa Enterprise Fund (AEF) to assist SMEs in sub-Saharan Africa. The AEF supports investment projects with total capital costs ranging between the equivalent of US$250,000 and US$5 million. Such projects may involve the establishment of new ventures or the expansion or rehabilitation of existing companies, provided that pre-project capitalization of existing companies does not exceed $5 million.

The AEF supports most types of productive activities by providing up to 40% of project financing in the form of loan and equity capital. Its investments are made on commercial terms. Loans are usually in convertible currencies. Equity investments seldom exceed 30% of total share capital. AEF normally invests between the equivalent of US$100,000 and US$750,000. The AEF never invests alone, it always co-finances projects with a local investment partner. The IFC's regional mission for Southern Africa, based in Harare, handles the AEF's activities in Zimbabwe.

The AEF was set up by the IFC in response to criticisms that it was unwilling to back small and medium scale African entrepreneurs. While the AEF has gone some way to meeting this criticism, many local observers still see the IFC as too bureaucratic, reactive and risk-averse to truly meet the needs of African and Zimbabwean entrepreneurs. For example, the same IFC staff that handle its larger investments are responsible for the AEF's operations, which require a more entrepreneurial and proactive approach to identifying and supporting promising ventures. To date, the AEF has committed US$2.5 million to small projects in Southern Africa.

Like its regional counterparts in other regions of the developing world, the African Development Bank (AfDB) is getting into the business of financing the private sector. In 1991, the AfDB established a Private Sector Development Unit (PSDU) with US$200 million to cover its first two years of operations. The unit began to function in August although investment activities have yet to begin.

The PSDU intends to back enterprises in Africa with a majority private shareholding including joint ventures with foreign companies. Priority will be given to companies that use local resources, are export-oriented or whose activities lead to efficient import substitution, create jobs and lead to the transfer of management expertise and

technology. The total amount of PSDU assistance, whether in loans or equity, will not normally exceed one third of the total cost of the project under consideration, and will range from a minimum of US$100,000 to a maximum of US$10 million. No specific division between equity and loans has been decided.

The PSDU was set up over the objections of some of the AfDB's non-regional members, who felt it would duplicate the role of the IFC and bilateral agencies such as the CDC. The AfDB claims, however, that the demand from African entrepreneurs is so huge that no one institution can provide all the answers. The unit plans to work closely with the Africa Project Development Facility, the African Business Roundtable and the African Management Services Company. But, because the AfDB's regional offices are weak by comparison with those of the IFC and CDC, for example, it is questionable whether it will be able to galvanize sufficient deal flow without working with external partners.

The European development banks have also been active in providing investment capital to African enterprises, including those in Zimbabwe. Only the Commonwealth Development Corporation (CDC), however, maintains a field office in Southern Africa which is based in Harare. The CDC is a 10% equity holder in the Venture Capital Company of Zimbabwe, having committed Z$5 million. In southern Africa, CDC has considered venture capital operations in Botswana and Namibia. The CDC is also actively investigating possible roles for itself in post-apartheid South Africa

The Netherlands Development Finance Company (FMO), German Investment and Development Company (DEG), and others work from offshore, relying on commercial representatives in their respective embassies to identify suitable investments. Of the Europeans, only the CDC had until recently taken an active interest in high risk venture financing, although the Nordic countries have now combined to established an investment fund to help finance joint ventures between Nordic and SADCC enterprises. The Norsad Fund was started in 1990 with capital of US$35 million and is based in Lusaka. Other Europeans have preferred to stick with project financing, often taking a majority equity stake in their investments.

The United Nations Development Program (UNDP) has recently established a Private Sector Unit for Development and has been looking at ways to back new venture capital activity in the developing world, through the financing of feasibility studies and so on. It sponsored the feasibility study for the new Venture Capital Company of Zimbabwe discussed below. It is also a sponsor of the African Project Development Facility.

There are several private sector, pan-African investment vehicles that have been created in recent years that have taken an interest in Southern Africa. Among them are the Equator Bank's Africa Growth Fund which is tied to US interests; Societe d'Investissement et de Developpement International (SIDI), a Paris-based non-profit development assistance program that supports venture capital projects throughout the developing world; and SIFIDA Investment Company, a Geneva-based group that is backed by the AfDB and which engages in a range of corporate finance activities across Africa, although it is currently badly undercapitalized.

A prominent private sector venture capital investor in southern Africa is the Zurich-based Edesa S.A. Edesa is a corporation that provides equity finance and know-how to countries in sub-Saharan Africa. Shareholders include the Bank of Montreal, Marubeni, Daimler-Benz, Dresner Bank, Union Bank of Switzerland, Anglo-American Corporation and the Universal Leaf Tobacco Co. As of 1988, Edesa's investments in Africa enterprises in the form of equity and non-guaranteed loans stood at US$15.9 million. Shareholder's equity in Edesa totalled US$21.2 million. Edesa intends to increase its capital base in response to what it perceives to be are an ever-increasing number of business opportunities, particularly in Southern Africa. It is currently engaged in reviving a Zimbabwean venture capital company called Questor.

The IFC affiliated African Project Development Facility (APDF) is a pre-investment facility that identifies potentially bankable projects, prepares the documentation required for prospective investors and plays a role in attracting capital to those projects, in exchange for a fee.

In their 1990 Annual Report, the APDF stated that 1,700 projects had been submitted for their scrutiny since it was launched in 1986. Funding was secured for 78 of these projects. These projects, represented investments of US$156 million, of which the APDF helped obtain US$108 million. A "large" percentage of the financing came from international donor agency programs, with very little coming from indigenous sources. According to the APDF, this points to "a growing need to step up the mobilization of indigenous sources of equity capital." The APDF maintains a regional office in Harare.

POSSIBLE ROLE OF VENTURE CAPITAL

Venture capital is defined as medium to long term (three to ten years) minority equity or quasi-equity investment in privately held companies. Typically the venture capital investor acquires 10% to 40% of the common shares in the company purchased from treasury, takes an active "value added" role in the management of the company through Board of Directors or other participation, and seeks to realise a gain on the investment by sale of the company's shares at a significant multiple of the original cost of the investment. Quasi-equity in the form of special shares or fully or partially unsecured loans may be used as part of the original financing, or for the second or subsequent rounds of financing usually required by a rapidly growing company. (See handouts provided to Venture Capital Workshop Participants, Appendix 7).

Venture capital financing has certain characteristics which are difficult for people involved in normal financing to understand, or accept. These include:

- you normally have to look at a large number of deals to do a few. The "conversion rate" can be as low as 2 - 4 deals actual done out of 100 potential investments considered. This involves a great deal of time, effort, and often results in dashed expectations on the part of both the potential investee and the investment officers.

- the first money into the investee is invariably just that. Add-on financing, sometimes many subsequent rounds of it, is the rule. Each time a tough new investment decision must be made.

- out of every ten deals made, the rule of thumb is 2/6/2 representing two write-offs, six "living dead" and "walking wounded" and two very large winners. Living dead are companies not going anywhere and losing money. Walking wounded are companies that are producing income and some profits, and will likely survive, but have lost the potential to give an extraordinary return on investment.

- the write-offs and living dead/walking wounded will become apparent long before the extraordinary winners materialize,

making short term measurement of a venture capital portfolio a nightmare at times. This is one reason why there are, for all practical purposes, no publicly traded venture capital funds on North American or European stock exchanges. Some have tried, but stock market purchase decisions are based most frequently on short term operating results, and the market undervalues venture capital holdings for that reason.

For all of these reasons, and many others, investment in a venture capital fund must always be considered on a long term basis. Managing the activities of the fund, and the investee portfolio, requires considerable short term decision making and action, very much hands on. But the performance only becomes truly apparent over time.

Venture capital financing has grown rapidly in North America and Europe, and more recently in South-East Asia including developing countries, because it has proven to be an effective instrument for earning capital gains, speeding the growth of companies, and making a major contribution to the economic well being of the nations where it is available. Equity investment is essential to the start-up and growth of small and medium sized enterprises. It is critical to the rapid development of high growth companies, frequently export oriented, which can rapidly outstrip the traditional sources of business financing.

There have been numerous studies conducted on the impact of venture capital investment. Typical of many, one North American study by Ernst & Whinney on behalf of the Association of Canadian Venture Capital Companies shows that for every Cdn$100,000 invested in a venture capital investee, that company generates **each year**:

- ten full time jobs;
- $348,000 of export sales;
- $50,000 of tax revenues for governments at all levels;
- $8,000 of research and development expenditure; and
- compounded annual company growth of 37% in assets and 40% in revenues. (See Appendix 4, paper by M.J. Kostuch, University of Western Ontario Quarterly)

An April 1991 report in the US Venture Capital Journal reported similar results from the most recent of a series of such studies conducted for the US National Venture Capital

Association. In studying the period 1985 to 1989 the Coopers & Lybrand produced research showed that some 200 venture capital backed companies (average age of four years in business) created some 36,000 new jobs. Key indicators from this study showed compounded annual growth rates in the 1985-89 period as follows:

* 54% Jobs
* 31% Assets
* 49% Research and Development
* 324% Exports
* 209% Tax Revenues

Recent data on the success of venture capital in Indonesia, Malasia and India, the success of the IPS Fund in Kenya, and the experience of Hawk Ventures (see Financial Sector, Venture Capital section) in Zimbabwe indicate that these benefits can be gained in a developing economy such as Zimbabwe.

To be successful, growing companies need financing at various stages of their development. In the Zimbabwean context, recent developments in the equity funding arena show the beginnings of such a multi-level funding capability. At the lowest end, pre-start up and startup financing can be provided by Manna Corporation (less than Z$100,000) or the Zambuko Trust. Long term debt financing (sometimes unsecured) can be provided by the Small Enterprise Development Program.

Early stage, small and medium sized enterprise funding, is the preferred strategy for the new Venture Capital Company of Zimbabwe (Z$200,000 to Z$600,000) now actively in operation. Larger financings are available through Hawk Ventures (average size Z$1 million), or through groups such as the Commonwealth Development Corporation (preferred range Z$5,000,000).

There is a distinct gap in the availability of financing between VCCZ's preferred range of up to Z$600,000 and Hawk Ventures lowest range of Z$1 million, which could be filled by the new Continental Capital (Pvt) Limited.

Another venture capital player could also play a vital role in syndications, two or more investors working together, (see below) or in later stage financings supporting a venture capital portfolio company.

Continental Capital (Pvt) Limited's creation would also spur additional interest among entrepreneurs, creating increased confidence that this new form of financing is here to stay in Zimbabwe, and attracting "green field" (start-up and joint venture) opportunities. Potential foreign investors or joint venturers would also gain confidence in the availability of local equity to finance their programs in Zimbabwe, serving as a catalyst for new developments.

As recommended (see section E, Assist Continental Capital in Preparing an Offering Memorandum...), Continental Capital will be a fully independent, return on investment (ROI) oriented, venture capital fund, significantly different from the "development" targeted VCCZ.

While VCCZ's objectives are entirely lauditory and will likely make an important contribution to Zimbabwe at this point in its history, VCCZ's "development" emphasis will increase its cost of doing business substantially, thus negatively impacting ROI. Increased costs for "development" activity include both direct expenses and use of staff and management time to generate publicity, hold public meetings and seminars, encourage the largest possible flow of potential investment ideas, undertake low level, low skill business projects which while socially beneficial in the short term are not capable of rapid growth, do relatively small size deals, etc. (See Zimbabwe's Venture Capital Industry section.)

Continental Capital will focus its activities on fast growing, export oriented situations and will work with management to provide the most modern, highest quality resources and technologies essential to build highly competitive companies competing in both Southern Africa and international export environments. Continental Capital should provide a developing country model of venture capital investment in the traditional, highly successful approach already proving itself in both the developed, and developing (South-East Asia) world.

As management of Continental Capital, and other venture groups, gain experience they, and their investees, will recognize an additional benefit of equity investing, empowerment of people. Ownership of equity by individuals and groups of individuals opens new, not previously foreseen, opportunities, gives financial and economic leverage to ideas and enterprises, and gives society an increased sense of purpose and confidence that a "debtor" can never attain. Empowerment gives dignity to those individuals, and those societies, that permit ownership of assets in the private sector.

CONDITIONS REQUIRED TO ASSURE THE VIABILITY OF SUCCESSFULLY LAUNCHING CONTINENTAL CAPITAL (PRIVATE) LIMITED

A) ASSESSMENT OF DEAL FLOW POTENTIAL

A complex set of conditions is required for venture capital process to succeed. A US study (International Venture Capital - An Overview of Current Trends, Bernard Tenenbaum, The Wharton School, April 1986) identified these as:

1. Government policies that reward innovation and risk taking. These include: (i) tax advantages for capital gains, limited partnerships, and pension investments; (ii) other monetary incentives; (iii) non-monetary incentives,
2. a supportive institutional environment,
3. a supportive society which respects entrepreneurs,
4. a pool of entrepreneurial talent,
5. an adequate supply of venture capital funds,
6. experienced venture capitalists,
7. an active securities markets,
8. active research and development and technological innovation environment (defined in its broadest sense),
9. a sizable and diverse marketplace,
10. higher education programs.

Clearly, not all of the above conditions are in place in Zimbabwe, but a definite trend in favour of all of these conditions is apparent. Zimbabwe is also well positioned to play a lead role in venture capital development for all of Southern Africa.

The SB Capital Study Team believes that entrepreneurial energies that had remained bottled up under the old set of policies and regulations can now be harnessed, provided an integrated package of equity capital, hard currency market access, technology and management know-how is made available to local business. Increasingly, as in Zimbabwe, other developing nation leaders realize that if free market economic development becomes the goal of any nation, the institutional and attitudinal obstacles to growth of private companies must be removed. Zimbabwe is well positioned to take a lead over the rest of Southern Africa.

Despite some scepticism expressed by several of the persons interviewed, the overwhelming consensus of experienced business leaders in Zimbabwe is that a demand for equity financing already exists, and the increased visibility given to equity funding availability (as demonstrated by the new Venture Capital Company of Zimbabwe) has already stimulated an increased interest in this form of financing. VCCZ reports an almost overwhelming flow of up to 25 or more new investment requests each day, from all sections of the country. Many of these are potential start-up companies stimulated by the prospect of obtaining equity funding since few other sources of financing are available to such early-stage companies.

Additional solid evidence of this deal flow potential in Zimbabwe comes from the experience of Hawk Ventures which made some 27 venture capital investments in just over four years with no publicity other than word of mouth. Hawk Ventures management estimate that they reviewed as many as ten potential investments for every one actually made. These leads were generated by the First Merchant Bank branch network, accounting and legal professionals and by referral from present investees.

The need for venture capital in Southern Africa has been recognized by governments and the private sector for some years. USAID, for example, has recognized that African entrepreneurs face a number of serious financing constraints brought about by such problems as overly conservative banking practices, weak capital markets, poor access to information, management weaknesses and a serious shortage of vehicles for the provision of long term capital. The lack of equity capital has been seen as a fundamental cause for the low rate of investment in Africa in productive enterprises. The 1990 launch of the Africa Venture Capital Project was a direct response to these issues.

The African Development Bank established in 1991 the Private Sector Development Unit (PSDU), with US$200 million to cover its first two years of operation. This move recognizes the importance of developing the private sector through provision of loans and equity, and further emphasises that the potential demand from African entrepreneurs is so huge that no one institution can provide all the resources required.

Zimbank has also recognized the importance of the small business sector and established in October 1990 the Small Business Services Division to provide assistance to existing and emerging enterprises in both the formal and informal sectors. In addition to providing credit on less stringent terms than those used in normal banking, this Division is also prepared to offer advisory and consultancy services to improve the management capabilities of the client.

The experience of VCCZ and Hawk Ventures demonstrates the need for equity investment vehicles in Zimbabwe. It's initial availability has led to a significant increase in deal flow, and that their are good investment opportunities among these has already been demonstrated by Hawk Ventures.

Quality of management, and availability of experienced management to direct future growth of the enterprise, is an area of some concern. However, this is also an area that can be corrected over time through training, provision of experienced support services, establishment of an industry association and educational services, and the practical experience of successfully running an enterprise. In part, lack of business experience has been a cultural issue reflecting an aversion to private sector investment and wealth creation. The ruling ZANU-PF party has now recognized the need for radical change and the many new initiatives described in the Political Background section of this report reflect this new awareness of the importance of entrepreneurship and private enterprise.

Zimbabwe's acceptance and adoption of the ESAP program has not been a sudden decision. It's gestation has been long, involving dozens of working parties and committees made up of both private sector and government members, supported by the World Bank and other agencies active in Southern Africa. This process of change, and the influence of private sector initiatives, has created a new climate which encourages creation and growth of new enterprises. More change is still required, particularly in the regulatory area, but the progress to date has been significant.

A great deal of discussion at the USAID/SB Capital Venture Capital Workshop addressed the issues of skills development and the availability of advisory services to support private sector enterprises. The consensus was that experienced entrepreneurs and business advisors are available, and would be prepared to work with formal or informal advisory boards established to assist individual enterprises, or groups of such enterprises. This was also confirmed by the Zimbabwe National Chamber of Commerce where both structured and informal advisory services are already being provided. Similarly, the CASE experience at SEDCO confirms the potential for such programs. (See Encouragement of the Private Sector, Training Program section.)

Many diverse groups are focusing on providing specialised training and advisory services. VCCZ sees this as an essential part of their mandate for both investees and persons looking to establish or build a business.

While the SE Capital Study Team had a limited time in Zimbabwe it was still able to identify six potential venture capital investments that might be considered by a venture capital company such as Continental Capital. (See Appendix II, Potential Venture Capital Investment Deals.) These might be looked at either as having Continental Capital become the sole investor, or taking the lead investor role in a syndication where the amount required exceeded the Z$1.5 to Z$2 million initial round financing ceiling guideline proposed for the new fund. Such syndication lead positions are quite common for venture capital companies in North America and Europe, and will certainly by required in Zimbabwe. Such syndications usually bring together debt or other forms of financing, as well as other equity players such as other venture capital companies or institutional investors who feel more comfortable because of the presence of an experienced venture capital investor ahead of them. Strategic partners or industrial companies interested in the field served by the investee may also be attracted by the presence of a venture capital investor in the deal. Institutional and industrial investors are usually reluctant to get involved in small company investments where they may be called on to become active in Board positions or other value added roles. They like to have the venture capitalist do this work.

With the permission of the company, Appendix 11 includes the full "Business Plan" prepared by Reliance Marketing (Pvt) Ltd. to create a new company, Reliance Can Industries, for the purpose of manufacturing steel "tin" cans for the food processing industry. The deal was referred to the Study Team by Don Greenberg of USAID, Harare, and Mitch Kostuch met with Mr. Hasu Patel, founder of Reliance Marketing, and father of Mr. Dakshesh Patel, Executive Director for the new company. While far from being a complete business plan for venture capital investment purposes, it is indicative of the potential opportunities available in Zimbabwe, and shows that entrepreneurs already have an awareness of the kind of data required to make an investment decision. It is not a "bankable" deal for normal commercial lenders and would need at least 15% of the requested funding as equity, which had not been envisioned by the entrepreneurs. This was pointed out to Mr. D. Patel in a telephone conversation and he indicated that they would be prepared to accept an equity investor, giving up some ownership, and "might even be able to put up some equity funding themselves" after being pressed on this matter.

The evidence indicates that the potential for deal flow exists in Zimbabwe.

B) EVALUATION OF ZIMBANK'S CURRENT MANAGEMENT CAPACITY TO UNDERTAKE A VENTURE CAPITAL FUND

Capacity to undertake a venture capital fund must be measured in the light of a variety of factors, including:

- understanding the nature, role and requirements of a venture capital operation;
- making the commitment to meet these needs; and
- having the resources, both financial and managerial, to achieve success.

In each of these areas Zimbank and its management group is already well positioned for success in venture capital operations. Any areas of weakness can be underpinned through training and support systems. (See Appendix 9, Zimbank, Group Annual Report 1991)

An understanding of the nature of venture capital financing has been growing at Zimbank for several years. With the Zimbabwe government as its principal shareholder, the management of Zimbank have been part of the process of change leading to new policies to encourage the growth of private enterprise. The present proposal to establish Continental Capital (Pvt) Limited is the fourth look at venture capital by Zimbank's management group.

Zimbank is presently a shareholder of VCCZ, its first direct investment in a venture capital fund. Previously Zimbank had considered establishing its own venture capital division, but after extensive consideration had rejected that proposal since it recognized that a different kind of management, one not tied to traditional banking standards and practices, was required. This appreciation was stated to the Study Team by several different executives of Zimbank, including Group Chief Executive Dr. L.L. Tsumba. This concern about venture capital operational differences from traditional banking was also echoed by World Bank Representative Tom Milton who acknowledged such discussions with Zimbank prior to their investment in VCCZ.

Subsequently, Zimbank entered into negotiations with Bankers Trust (United Kingdom) with a view to setting up a joint venture capital company. The Study Team have been

advised that Zimbank withdrew from these negotiations because of Bankers Trust intention of retaining a controlling interest (51% equity) in the new fund, thus altering its "independent" status for operating purposes.

While the commitment to venture capital financing by Zimbank is illustrated by the VCCZ investment, many observers acknowledge substantial government pressure was required to bring together the financing group. Perhaps clearer evidence of Zimbank's commitment is shown by an earlier experience SB Capital had with Zimbank during the summer of 1991. The Canadian International Development Agency suggested to SB Capital that it submit a proposal to establish a venture capital fund in Zimbabwe under the CIDA Private Sector Development Initiative Fund (PSDFund). At that time SB Capital had not yet visited Zimbabwe, although a trip had already been scheduled for the Fall. SB Capital was also advised of the PSDFund availability only a few weeks before the deadline.

In seeking potential local partners in Zimbabwe to support a proposed venture capital fund, SB Capital was advised by several different sources of Zimbank's considerations regarding venture capital. An approach was made by letter, fax and telephone, ultimately reaching up to the office of Mr. Tsumba. After a remarkably short two week period of discussion and due diligence, Zimbank provided a conditional letter of support for the potential PSDFund initiative, including a willingness to consider a co-investor role and providing personnel and other resources to launch an independent, private sector venture capital fund. Mr. Tsumba and other Zimbank executives displayed both a sound understanding of venture capital, and a willingness to be part of such an activity outside the control of Zimbank. For technical reasons (inability of the Zimbabwe Investment Center to handle in time the volume of deals it was considering), the SB Capital PSDFund proposal could not be considered by CIDA. However, it did demonstrate both the awareness, and commitment, of Zimbank to the venture capital process.

Unknown to SB Capital, a Zimbank Manager, Mr. Jefta Mugweni, was already undertaking advanced independent study of the venture capital process. He was working in Italy on his Masters Degree in Banking and Finance, specialising in the study of venture capital and small business financing, under the direction of Professor Angelo Caloia, President of Fin Africa Foundation, past chairman of the Vatican Bank, and chairman of Cariplo Bank. An experienced employee of the International Finance and Capital Markets Division of Zimbank, on his return to Zimbank in the fall of 1991 Mr. Mugweni was given special responsibility to enlarge Zimbank's role in venture capital. Mr. Mugweni has been an active player in the redefining of Continental Capital's role and

the preparation of initial feasibility studies to attract private sector investors into the new fund. (See Appendix 5, Curriculum Vitae, Mr. Jefta Mugweni.)

Zimbank is now committed at the most senior level to creation of an independent fund, and are prepared to release Mr. Mugweni to serve as Managing Director of Continental Capital (Pvt) Limited, subject to approval of Continental's shareholders and Board of Directors. Having worked with Mr. Mugweni for eight days, including "high pressure" events such as the USAID/SB Capital Venture Capital Workshop and a Study Team meeting with the Continental Board of Directors, we are confident that Mr. Mugweni's knowledge and skill level is sufficient for him to lead the proposed fund, and to bring together a committed and independent management team to run it. Outside assistance and training is required, preferably on a medium to long term basis (three to five years), an area in which USAID's experience and resources can play a key role.

We therefore feel that Zimbank is well positioned to lead the initiative to creation of Continental Capital (Pvt) Limited.

C) DETERMINE THE AVAILABILITY OF INVESTMENT FUNDS

The SB Capital Study Team met with four members of the Board of Directors of Continental Capital (Pvt) Limited, along with Mr. Jefta Mugweni of Zimbank. Subsequently several potential investors participated actively in the USAID/SB Capital Venture Capital Workshop and the Study Team met individually with some of them. The potential investors in Continental Capital (Pvt) Limited include:

Zimbabwe Development Bank
P O Box 7705, Harare
Telephone 705471
Attention: Mr. R. Jaravaza

Fidelity Life Assurance Co.
P O Box 435, Harare
Telephone 702811
Attention: Mr. N. Gwatidzo

First Mutual Life Assurance
P O Box 1083, Harare
Telephone 705981
Attention: Mr. E.F. Muzvondiwa

Old Mutual
P O Box 70, Harare
Telephone 734011
Attention: Mr. J. Ndemera

Southampton Assurance Company
P O Box 969, Harare
Telephone 708801
Attention: Mr. Muchatuta

Zimbabwe Reinsurance Corporation
P O Box 4839, Harare
Telephone 790931

Intermarket Discount House
3rd Floor, UDC House, Harare
Telephone 702782
Attention: Mr. N. Vingirai

All of the above organisations are active players in the discussions leading to formation of the new venture capital fund as an independent, return on investment targeted, private sector driven, organization. They have received and have discussed the Zimbank developed "Feasibility Study into the Background and Establishment of the Continental Capital (Private) Limited - A Venture Capital Company" dated March 1992. (See Appendix 12). All feel that such a venture can be successful in the Zimbabwean environment as it is developing, and that it can function well even if no other investors, Zimbabwean or foreign, are attracted to participate. Zimbank are speaking with other potential investors, including European players. SB Capital is also aware of at least three potential foreign investors in the United States and the United Kingdom.

The March 1992 proposal envisions a fund of up to Z$120 million, 50% to be equity in Continental, authorized share capital of Z$60 million. The proposed equity would be drawn down in several trenches as determined by the Board of Directors. The remaining

Z$60 million would be debt financing provided prorated by the equity holders as requested by the Board of Directors.

The investors interviewed by the study team were confident that they and their associates could achieve this level of financing for a fund to be created in 1992.

D) TEST ALTERNATIVE EXIT STRATEGIES

The USAID/SB Capital Venture Capital Workshop presentation included handout notes as well as substantial discussion about potential exit strategies. Many of the traditional exit mechanisms are already in place in Zimbabwe, and will grow stronger as the ESAP program strengthens the private sector and attracts more foreign investors. The objectives of a venture capital exit strategy is to maximize the compounded rate of return on the investment within a required time frame (usually 3-7 years). This also requires the early recognition of potential loss, or unsatisfactory low return investments so that these can either be written off, additional support financing withheld, or the investment sold while it still retains some value. Such low return companies, often seen as "comfort stage" companies, frequently are viable enterprises but should not be part of a venture capital company portfolio.

Hawk Ventures have already demonstrated that sale of a venture capital equity position can be made in Zimbabwe, to management of the firm or to a related company. Buyouts by management or other shareholders in the enterprise can be structured as part of the initial investment (for example times earnings per share at some future point of time to establish valuation), or negotiated at any time in the investment cycle. While CDC's strategy calls for a long term hold on its position with the intent of generating current income through dividends or other fees, it has been able to divest some investments by sale to related parties.

The presence of holding companies such as TA Holdings also offers comfort when considering disinvestment. TA have indicated their interest in possibly acquiring venture capital company positions in rapidly growing enterprises, as well as the possibility of attracting venture capital investment into subsidiaries to accelerate their growth.

The Zimbabwe Stock Exchange also offers the potential for exiting investments through initial public offerings (IPO). While the Study Team were unable to speak with Stock

Exchange officials because of time constraints, it is our understanding that they are anxious to expand the IPO facilities of the Exchange, and that a potential market for new equities exists among present institutional investors and the public. The recent Barclay's Bank Stock issue attracted some 14,000 individual share purchasers, of whom more than 10,000 are believed to be women. The Exchange, and the government of Zimbabwe, are also aware that in the world many institutional investors and mutual fund managers have developed a strong interest in "emerging market" public stock exchanges, attracted by the potential for higher than average market returns. In the United States alone, more than US$200 billion of pension fund and mutual fund money is reinvested every year.

Joint ventures, strategic alliances, or partnerships with foreign firms will likely by an important part of growing Continental Capital's portfolio companies. The partners in these ventures become potential buyers of the funds portfolio interest, often at a premium price since they know the company and its management very well.

The purpose of venture capital investing is to grow the company and enhance the value of its shares. In doing this the venture capitalist benefits, but recognizing that venture capital is usually a minority position in the company, the other shareholders, including management, also significantly increase the value of their holdings. These "richer" individuals and shareholders are then in a position to acquire interests in other companies, creating a market for the venture capitalists exit. Success is synergistic, and wants to repeat itself. Three current Hawk Ventures deals are alongside individuals they previously invested in.

The Study Team has concluded that the basic infrastructure for exiting deals exists, and will be enhanced by the political, economic and regional developments now well underway as outlined above.

E) ASSIST CONTINENTAL CAPITAL (PVT) LIMITED IN PREPARING AN OFFERING MEMORANDUM TO ATTRACT PRIVATE SECTOR SHAREHOLDERS

SB Capital's input into development of a potential Offering Memorandum for Continental Capital (Pvt) Limited began several weeks before Zimbank approached USAID to finance SB Capital's formal participation, resulting in this assignment from USAID/Harvey & Company, Incorporated. SB Capital was approached by telephone and letter on or about January 6, 1992 and subsequently received by courier an initial pre-feasibility study

developed by Zimbank, dated November 1, 1991. This initial contact also requested that SB Capital consider a long term relationship with Zimbank in developing the proposed Continental Capital (Pvt) Limited venture capital company.

By telephone and fax messages, SB Capital suggested to Zimbank that while their initial study "is a significant first step ... in the preparation of an Offering Memo and Prospectus to be presented to your potential investor group ... it raises many obvious issues which Zimbank and the shareholders must consider." While not closing the door to any potential ongoing relationship, SB Capital suggested an initial familiarization meeting in Zimbabwe as a first step, including "a 1-2 day Workshop on venture capital for your key people (potential management and\or investors) so that we can educate them about the venture capital process and its management." SB Capital then suggested a number of changes in the initial feasibility study, including among others:

- "(training) should be done in the country involved" as opposed to long periods of training of key management staff in North America;

- a focus on developing venture capital values in management as opposed to "notable experience...in banking" as a requirement of management selection;

- the dangers of targeting "60% of your investments to be start-ups";

- the costs and risks of attempting to adopt an "incubation center" role as part of a venture capital fund;

- etc.

SB Capital recommended that Zimbank establish contact with USAID to make them an active player in the planning of the proposed new fund, and subsequently SB Capital was also put into contact with USAID, Harvey & Company, Incorporated, in Washington. Much of this early correspondence with Zimbank, and the initial Zimbank feasibility study, was provided to Harvey & Company by SB Capital with the permission of Zimbank.

During this period Zimbank also significantly revised their internal feasibility study, reflecting the comments and suggestions made by SB Capital, even though no formal

contractual or business relationship existed between SB Capital and Zimbank. This revised feasibility study, dated March 1992 was subsequently reviewed with Zimbank during the USAID sponsored visit to Zimbabwe, and is attached as Appendix 12.

Additional changes have been recommended by SB Capital as a result of the Zimbabwe meetings and will be incorporated into the revised Offering Memorandum now being prepared by Zimbank. In summary, the structure of the proposed Continental Capital (Pvt) Limited as a venture capital company will include the following characteristics and objectives:

PURPOSE:

- to produce an above average rate of return on invested capital through realization of capital gains on the sale of equities held in small and medium sized companies, initially in Zimbabwe only, but extending into other parts of Southern Africa as the staff and financial resources develop and opportunities for profitable investment occur.

- to provide equity and quasi-equity funding to industrial, commercial and, in special circumstances, service ventures capable of attaining substantial rates of growth (30% to 50% compounded) over a 3-7 year period, with a reasonable prospect of achieving liquidity on the investment at the end of this period.

- to provide value added services to these enterprises through participation in Board of Director meetings, and other activities such as Management Committees, so as to, among other objectives:

  * facilitate transfer of technology to the enterprise,
  * strengthen management through training and development of outside advisory services,
  * facilitate joint venture and other strategic alliances with domestic and external partners,
  * promote export sales,
  * improve production and service efficiencies,
  * provide a window on hard currency opportunities,
  * guidance in product upgrading and packaging, etc.

- a principal objective must be to build the strongest, most efficient management team and work force in the company's market sector, using the best methods and most modern technologies available to ensure the long term viability of the organization, and to be competitive in export and international markets where applicable.

- to play a leadership role in the development of a venture capital industry in Zimbabwe initially, and throughout Southern Africa in the future, through active development of a venture capital industry association and related training and public relations programs.

ZIMBABWE DEVELOPMENT GOALS:

- successful venture capital financed companies are powerful engines for economic growth and the development of essential services and experienced personnel required to build a strong society. Job creation, exports, research and development, taxes paid to local and national governments, and the rapid growth in company sales and asset values, are all positive outcomes of successful companies which are the major contributors to a society's well being. These societal development goals can best be achieved by focusing on building successful companies.

- growth of such companies must be consistent with the social values and national development goals of Zimbabwe which include:

  * fostering the development of locally owned enterprises,
  * equity hiring practices,
  * promotion of local personnel to management positions based on ability,
  * fostering ecologically desirable and sustainable development,
  * promoting the participation of women in business,
  * expansion of Zimbabwe's commercial linkages to the outside world,

* increasing the supply of professionally managed entrepreneurial financing in Zimbabwe,
* etc.

CAPITALIZATION AND SHARE STRUCTURE:

- the independence of Continental Capital and its management is a key requirement for success of the venture capital company. This has been extensively discussed with Zimbank management at several different levels, and with representatives of the outside investor groups, with understanding and agreement. As outlined in section C above, the key investors are in place. No one investor, however, should hold more than 30% of the common, voting shares in Continental, and it would be desirable as the investor group grows that this participation be reduced to 25%, or even 20% in the longer term. To be most successful Continental Capital should both operate independently, and be seen to be doing so.

- the targeted capitalization established as Z$60 million equity, with the availability of Z$60 million of debt financing on a prorata basis, provides a realistic base for meeting the needs of Continental Capital for the foreseeable future. This combination of debt and equity reflects the proposed investment strategy of the new venture capital fund as outlined below.

- Continental Capital will be a viable enterprise based on local financing only, but outside capital in hard currency is desirable. To this end, Zimbank have initiated discussion with potential hard currency investors, and SB Capital has identified three potential outside investors (one US and two UK) who are aware of the Zimbank proposal in general terms and would welcome the opportunity to review the completed Offering Memorandum as a potential investor. The appropriate vehicle for bringing in hard currency investors (directly into Continental, an offshore fund managed by Continental, direct co-investment into individual deals, etc.) cannot be determined at this stage.

- the proposed share capital corporate structure for Continental Capital does not follow the most widely used strategy for capitalizing a venture capital fund, however it is realistic and acceptable in the Zimbabwean context. Based on years of experience, most venture capital funds are established as partnerships with investors holding units in a Limited Partnership, and that Partnership in turn is managed be a General Partner independent of the Limited Partners. There are many reasons for the wide use of this structure, including:

  * providing a flow through vehicle for tax purposes thus permitting investors with different tax rates to participate without penalising other investors;
  * limiting liability exposure for investors;
  * independence of management from influence by any one investor;
  * establishing a finite life for the Limited Partnership (currently 10-12 years) to encourage early realizations and return of capital and gains to investors;
  * limiting the expense of running the fund (generally capped annually at 2 1/2% of committed capital under $50 million, 1% to 1 1/2% over that amount) in the form of a fee paid to the General Partner;
  * providing an incentive for the management General Partner in the form of a participation in net realized gains distributed (traditionally up to 20%, after return of invested capital);
  * etc.

While Zimbabwe law recognizes Partnership structures, there is no provision for limiting investor liability, therefore, at this time, making use of this vehicle in Zimbabwe would be risky for venture capital investment purposes.

BOARD OF DIRECTORS AND MANAGEMENT:

- because of the number of proposed, and potential investors, and the learning experience Board of Directors representation affords the investors, an initial Board of 10 persons is recommended.

However, direct investor represention should initially be limited to seven of the 10 positions, with three positions held by independent Directors. These outside Directors should be selected for their management expertise or special knowledge of domestic or export markets, and may in fact be located from outside Zimbabwe. The Chairman of the Board should not be an automatic appointment to represent any particular investor group, rather should represent the best interests of all of the shareholders. An individual representing management of Continental may in the future be appointed to the Board, but this is not essential at this stage since management attendance at all Board meetings can readily be arranged by invitation. Initially the Board should meet at least every two months on a regular schedule.

- the Board of Directors should establish an Executive Committee of the Board. We suggest a Committee of four Board members, including at least one outside Director, and the Managing Director of Continental Capital should also be a member of the Executive Committee. This Executive Committee should meet regularily with management and the investment officers to review current activities and to approve or reject investments in excess of Z$1 million, either a new investment or a cumulative add on valuation. Regular monthly meetings should be scheduled, more frequently if experience dictates a need.

- after considerable discussion with Zimbank and potential investors, SB Capital has recommended a much less aggressive and smaller management and operating staff than previously envisioned by the investors. We recommend the following positions be established and filled:

  * Managing Director, to be held by Jefta Mugweni as a full time employee of Continential Capital, severing his present relationship with Zimbank. This has been discussed with Zimbank and Mr. Mugweni by the Study Team and both have agreed in principal to this move, subject to approval of the Continental Board of Directors. (See section B above.) The Managing Director should also serve as an

Investment Officer, including investee screening, due diligence and monitoring of a group of two or three investee companies in the intitial stages of Continetal's development. Practical, hands on experience, is the best teacher in developing a successful venture capitalist.

* two Project Managers or Investment Officers to be hired after advertising these positions to attract the best possible candidates. These individuals will likely be university graduates in business or finance, preferably with some educational or business experience outside of Zimbabwe, and with practical work experience of three or more years in business or financial services. They must be bright, able to understand and work with technologies, have people skills both on a one-to-one and group basis, prepared to work hard and long hours, flexible in accepting new challenges and responsibilities, committed to achieving personal and group goals, reponsible as to reporting and communications of results, have shown leadership and success in prior activities (sports, social groups, school activities, promotions at work, earlier entrepreneurial endeavours, etc.), and a determination to succeed extraordinarily in what they do. Prior venture capital or investment finance experience is desireable, but probably not available. Investment Officers should be involved at every stage of the investment process, including screening potential investees, due diligence and research, structuring and negotiating deals, monitoring and value adding to investee companies, divestitures, public relations, etc.

* one Project Analyst, or junior investment officer, to work alongside Investment Officers and the Managing Director. This person should be considered as a trainee for a future Investment Officer position.

* one secretary\typist to provide services to the staff and, in general, to act as office manager.

* one messenger will also likely be required, but this should be considered as a possible entry position into the venture capital business. Therefor, a person with upgradable values and goals should be given preference for this position.

- the Board of Directors of Continental Capital must consider as soon as possible after launching of the fund an appropriate incentive system to properly motivate and reward, and ultimately to retain, the management staff of the venture capital company. As mentioned above, the general practice in establishing venture capital funds, based on more than 50 years of experience, has been to allocate a "participation" of up to 20% of net realised gains to the management, payable after repayment of committed capital and alongside distributions to investors. In the case of venture capital Limited Partnerships the participation allocation is made to the managing General Partner of the fund. By any normal banking, term financing or mutual funds management standards this may seem to be an excessive "fee", but it has stood the test of time in the United States, Canada, Europe, and most recently South East Asia, since it recognizes the following factors:

  * experienced venture capital managers have taken years to develop their special skills. They can't learn their trade from books, by programming computer models, by following "past specific practices", or by looking over the shoulder of other practitioners. There is more "art" and "gut feel" based on experience in venture capital investing than there is science.

  * the participation reward is earned only after years of working with individual clients, often taking investee companies through very difficult times, and requires dogged commitment for success. The potential for a participation focuses management's attention on the longer term drive to succeed, rather than taking the easy road of "writing off" an investment that has become a nuisance.

* participation is paid out on "net" realised gains after taking into account write-offs and low return investments. If management has made bad decisions, bringing down net returns, it receives an appropriate low participation reward.

* venture capital managers will see successful entrepreneurs, and the management and shareholders of investee companies, making extraordinary gains. At the same time the venture capital manager may have had an equal, or greater, input into the success of the company, in which he or she personally has no equity interest. This can create great frustration in the venture capital management, leading them to leave and start up their own ventures, or withdraw into a shell and lost interest in their task.

* every time the venture capital manager recommends an investment, or takes part in a value added decision as part of the monitoring process, he, or she, is in effect risking both their reputation and job security. The Investment Officer deserves a reward for taking this risk.

* good venture capital managers are very much in demand, and if not properly rewarded, could leave to join another organization, or to set up their own fund. Losing a good manager at any time during the investee's business cycle, whether a problem company or one that is growing rapidly, can be devastating to both the venture capital fund and the investee company.

* the old saying that "the proof of the pudding is in the eating" holds true. Those venture capital funds that offer participation to management have grown to be the leaders. Those that have tried to operate under salary plus occasional bonuses within a normal industrial or financial institutional payroll framework find themselves out of the venture capital business after one investment cycle.

An alternative to the percentage bonus participation approach described above, and used with some success, is permitting management to "buy into" individual investments on the same terms and conditions as the fund. In most instances the required funds are "loaned" to the investment officer(s) at nominal or no interest by the venture capital company. This has been tried most frequently by the venture capital divisions of industrial or holding companies. The dangers of this approach are two-fold:

* writing-off an investment is personally expensive for the investment officer so there is a tendency to do add-on support funding in order to postpone the day of reckoning, when a tougher decision should have been taken.

* sometimes an investment officer may be extraordinarily lucky on one investment, thus realising a personal gain on shares personally held, and leaves the venture capital firm if other investments in the portfolio look to be potential loss, or low return, clients. The Investment Officer has no incentive to "net" the return on the portfolio, and can leave the problem accounts for someone else to work out, and to take the risk of providing additional support.

Continental Capital must provide an appropriate participation scheme for its management group as soon as reasonably possible, but this is an issue that requires much more study in Zimbabwe context.

- staffing of Continental should not be increased until the Managing Director and Investment Officers each have three or more active investments to manage. Ultimately, each Investment Officer will be able to handle 5 - 8 portfolio companies as their experience level increases.

- training of the Continental staff, both initial and long term is discussed below in the section Outcomes of the Venture Capital Workshop and Study.

- the Study Team strongly recommend that the Continental should take advantage of the latest computer and networking capabilities, including use of portable notebook computers by the Managing

Director and Investment Officers, a networked file server internal computer system with electronic mail and data access from outside by telephone line and modem, and the current versions of business software such as Windows 3.1, WorkPerfect 5.1 for Windows, Lotus 1-2-3, etc. Not only should Continental's staff be proficient in the use of this technology, but it should be a condition of each investment that similar technologies be used by the investee company, including allocation of some part of the initial investment for appropriate equipment and staff training. Hard currency requirements for this purpose are a consideration, but external aid agencies and NGO groups may be able to provide assistance in this area. By modernizing both its own and investee systems, Continental's portfolio companies will become more competitive in their marketplaces, and at the same time substantially improve communications between Continental and its investees while reducing monitoring costs.

INVESTMENT CRITERIA:

- the USAID/SB Capital Venture Capital Workshop handout notes should be considered as an integral part of Continental's Offering Memorandum, in particular the pages entitled The Seven Stages of Venture Capital Growth, Hierarchy of Financing Sources, Structuring the Deal and Underpinning Risks, all of which relate to the investment criteria to be used. (see Appendix 7)

- quality of management in the potential investee is the key consideration, but venture capital seldom operates in a perfect world, with the ideal management on hand. Most frequently the venture capitalist must recognize the need to supplement (underpin) existing management, and have the confidence that investee management recognises the same need both initially and as the enterprise grows. However, the management in place when the investment is done should likely already have the following characteristics:

  * have established a traceable track record of prior success;

* have sound market knowledge including distribution risks and the present and future needs of the ultimate customer;
* understand the technologies and special features of their product and service area;
* have network contacts in both the domestic and export market;
* be a balanced team with complimentary skills matching the needs of the enterprise;
* etc.

- the company and it's product(s) category must be capable of rapid growth, with access to financial resources to finance this expansion as discussed in the Hierarchy of Financing Sources handout referred to above.

- preferred investment size for the initial round of financing would be in the Z$500,000 to Z$1.5 million range, although no investment should be automatically excluded if it offers the potential for substantial growth in asset value. Initial investments over Z$1.5 million should be considered for possible syndications with other venture capital companies, strategic partners, or institutional investors. Such syndications should be considered at any size if the outside partner brings special skills, technology, or market access to the table along with financing. Generally Continental's initial share of equity in the investee should be in the 20% to 40% range.

- structuring of the deal should include consideration of the issues detailed in the Structuring the Deal handout, but it would be highly desirable to use a combination of equity and debt in most investments, even at the first round. Debt instruments can be registered in Zimbabwe as legal agreements, and can provide a substantial level of "control" in the event of default. Even before default occurs, awareness of the potential "teeth" in the debt agreement serves to focus management's attention. Partial security for the debt can also usually be established, locking into the company assets which might otherwise be dissipated, and which could be released by Continental at some future date if

outside debt financing leverage is required. Obtaining some current income from the company also reduces the "cost" of the investment thus increasing longer term ROI. And, at the same time, default in such current income payments is a sharp warning of possible problems in the investee company.

TARGET INVESTMENT SECTORS:

- the Zimbank pre-feasibility study, Appendix 12, details Investment Targets by sector and industry. This area is also explored above in section A, Assessment of Deal Flow Potential. These form an integral part of this report. Not touched on previously, however, is the opportunity likely to open up as the parastatals that now dominate, or monopolize, certain sectors of the economy are forced to open up and change as part of the ESAP program and the restructuring of the government's expense structure. Private sector spin off ventures are very likely to develop, either as joint ventures or independent enterprises, competitively serving a market now controlled by a parastatal. If we consider the Zimbabwe tobacco industry as a model, a vital part of the economy, we find that while government is indirectly involved in marketing, the system is largely in private, very efficient, hands. Similar structures are likely to develop as marketplace realities impact on other parastatals, the largest of which in Zimbabwe are:

  Cold Storage Commission
  National Railways of Zimbabwe
  Cotton Marketing Board
  Grain Marketing Board
  Posts and Telecommunications Corporation
  National Oil Company of Zimbabwe
  State Trading Corporation
  Urban Development Corporation
  Minerals Marketing Corporation of Zimbabwe
  Zimbabwe Electric Supply Authority
  Zimbabwe Iron and Steel Company
  Forestry Commission

and others.

FINANCIAL FORECASTS:

- detailed budget estimates and potential return on investment values have been tested as part of the March 1992 Zimbank Feasibility Study, Appendix 12. These include detailed assumptions, and four different scenarios based on various investment mixes and timing. These are now being redone as a result of meetings with the Study Team in Zimbabwe , reflecting also the significantly reduced early staffing costs of Continental Capital. Substantially more work must be done on these, but due to the limited time available in Zimbabwe, and other priorities required to prepare this report, making detailed revisions of this data was impossible through direct participation by the Study Team. In general, we feel that the assumptions are well founded, the work to date well on track, and the input already provided during the Zimbabwe visit should improve this process.

OUTCOMES OF THE VENTURE CAPITAL WORKSHOP AND STUDY

Information on future technical assistance and training required to make Continental Capital fully operational.

Continental Capital will require professional venture capital assistance in three phases:

- **Short term**: to complete the Offering Memorandum, bring the investment group together and complete a financing agreement with a first tranche draw down of funds, initiate the search for management and staffing, establish a Continental Capital Business Plan, and organize the required office and other facilities to be located independent of any single investor. Because of the amount of work completed to date, this should require no more than 6 -9 months. At this point Continental Capital would be ready to commence operations.

- overlapping the above, and continuing into the **medium term** (2-3) years training of Continental Capital's management and staff must begin alon with establishment of support mechanisms to make available t management the required level of experience and expertise. Othe important activities include setting up of operating proceedures investment selection criteria, due diligence sources and proceedures, dea structuring models, accessing co-investor and syndication participants t alert them for possible future co-financing, setting up deal sourcin networks to generate quality deal flow, etc. The fund must also forg international linkages to develop sources for potential technology transfer distribution agreements, joint ventures and other strategic relationships t assist investees in developing export sales, and building the strongest possible operational bases in Zimbabwe. Continental Capital must als reach out to goverments and public influentials, to encourage continued improvements in the investment climate, particularily for foreign investors. This could best be done through es.ablishment of a venture capital association representing all potential participants in equity financing and policy direction, which could hold public forums and sponsor educational and training activity for the industry.

- overlapping the medium term and for the **long term** (4 - 5 year period) Continental will continue to require staff training and support, and international linkages, on a long term basis, Wisdom comes through both learning from your own experience as well as the experience of others. Research in the United States shows that investment officers must go through more than one investment cycle to become fully trained, with such cycles running 3 - 7 years for individual investments. Monitoring investments at various stages of the investee's cycle of growth is both stressful and demanding, and mistakes are usually very costly. Structuring the divestment of individual deals also calls for special knowledge and experience to maximize the potential return, and the most efficient timing. During this period Contintental Capital will also have to decide on reinvestment vs distribution of gains strategies (often a cause for real tension between management and the investor group), possible expansion to make investments outside of Zimbabwe, or the reorganization of Continental Capital to beome a General Partner managing

These are some of the issues which will develop as Continental Capital progresses. A similar set of needs is being faced by the Venture Capital Company of Zimbabwe, and are being met through seconding of a knowledgeable young venture capitalist to its full time staff for up to three years. The SB Capital Study Team feel that this is an inappropriate response to the needs of a return on investment focused venture capital fund such as Continental Capital, based on SB Capital's experience working with the World Bank IFC in developing countries such as Kenya, Argentina, and Peru. This in house support has the following weaknesses:

- regardless of the outsiders age or level of experience, the outsiders' values tend to dominate the entire venture capital process. Local management usually takes the safest route on any issue by tredding the path of the "expert". After all, if the decision turns out to be wrong, its not local management's fault. In such a system real learning is limited.

- venture capital in Zimbabwe will not be a mirror image of venture capital in the US or any other country. It must be allowed to develop its own local character, policies and values to meet its market requirements. Multi-country venture capital funds managers such as Advent and Alan Patricof long ago learned that local managers must have substantial flexibility in order to maximize opportunities specific to their environment. There is no "cookie cutter" formula for venture capital. Experience, combined with local market knowledge is essential.

- local managers must have the freedom to make decisions, experiment with different approaches, and the opportunity to take credit for their individual and group decisions. While this can be within a framework established with outsider expert advisors, it must permit local management decision making and thus committment to the deals being done.

- because of the generally vast difference in salary and participation levels paid to successful venture capital management in the US, Europe and elsewhere, its far too costly for a developing country fund to support on a full time basis a senior investment officer from abroad. In addition, a foreign investment officer would require hard currency payment, an additional problem where local currencies are not convertible. This has

usually resulted in secondment of a junior, less experienced person who then sets the standard for the developing country fund.

Training of investment officers outside of their country of business has been tried a number of times by World Bank IFC, including training of personnel in SB Capital's offices, or with other venture capital groups in Boston or London, England. On the whole, this experience proved a disaster. Trainees working abroad were faced with types of deals, investments instruments, product areas, market issues and management structures substantially different from their home market. When they returned, not only were the situations different, the resources available in the developed country were not in place, leading to frustration and disenchantment. Also, attracted by the bigger salaries and potential participations available in the developed country, trainees spent most of their free time looking for a new job, and left their home country fund within a short period of time. Another problem arose from the length of time training takes. Even one year is far too short a period to gain proper experience which should encompass more than one investment cycle.

Availability of hard currency when training abroad is another issue. Living costs are high by developing country standards, and must be paid in the currency of the country where traning takes place.

These are some of the training and technical assistance issues faced by Continental Capital, or any other developing country venture capital fund.

IDENTIFICATION OF NEEDS FOR OUTSIDE TECHNICAL ASSISTANCE AND TRAINING TO ENSURE SUCCESS IN REALIZING THE PLAN OF ACTION

RECOMMENDATIONS: CONTINENTAL CAPITAL (PVT) LIMITED

A medium to long term training and technical assistance strategy which combines both mentoring and apprenticeship should be developed, comprising:

First year: the Study Team recommends in-country assistance, training and support on site, through the presence of a consulting venture capital

investment officer for two periods of up to three months each, with loca management left on their own in between to develop their own confidenc and capabilities. The outside officer will be an employee of a prover venture capital company (the advisors) with knowledge of bott developed, and developing, country operations and should preferabl have personal knowledge of Zimbabwe and Southern Africa. This consulting officer must bring to Continental Capital the developed marke perspective, along with venture capital knowledge and capability. This in country activity would encompass every aspect of the venture capita process with local personnel working alongside (apprentice strategy) the consulting officers.

- access to further external support (mentoring), backing up the on-site officer, can be had by telephone, fax and computer modem data transfer to the head office of the advisor venture capital organization. During the first year, all potential investments should be reviewed by the most senior advisor investment officer available, who should also plan to visit Zimbabwe for a least two periods of two weeks each to evaluate the progress being made while the on-site consulting officer is there. Such trips should be coordinated so that Board of Directors meetings and/or shareholders meetings can be attended by the senior advisor while in Zimbabwe. Such visits could also be used to provide seminar or workshop engagements on behalf of Continental and/or the new proposed industy association.

- out of country training for at least the Managing Director and one or both Investment Officers should also be planned. The Study Team recommends attendance at the Venture Capital Institute, a six day training program produced by the National Association of Small Business Investment Companies in the United States. It is the best, most concise program available anywhere. The on-site consulting advisor would also attend this program along with the Continental Capital staff to facilitate common understanding of matters raised in the program, and their potential application in the Zimbabwe context. Based on years of training experience, The Venture Capital Institute relies largely on the Case Study Method for training, and the cases used are developed country situations whose application to Zimbabwe must be interpreted based on experience and knowledge of local conditions. The 1992 Institute is scheduled for

early September and will be held at the Arthur Anderson Training Centre located near Chicago, Illinois. Registration before the end of July is required to ensure participation.

- in conjunction with the Venture Capital Institute training visit which could be extended to two or three weeks maximum, other activities could be scheduled, depending on availability at the appropriate time, including:

  * attending a venture capital "show and tell" presentation conference sponsored by groups such as Oppenheimer & Co.Inc. or Montgomery Securities Inc. These one or two day conferences provide a showcase for dozens of potential investees, feature highly structured, tightly written summaries of individual opportunites in open sessions, followed by scheduled private meetings, and attended by 500 to 100 or more potential investors and investees.

  * visiting the offices of the advisor venture capital company working with Continental Capital to meet the key people, examine operating systems and proceedures, etc.

  * visiting one or both of the major multi-national venture capital funds managers, Advent in Boston or Alan Patricof in New York or California.

  * attending an industry or trade convention or exhibition to learn more about potential opportunities for technology transfer, markets for Zimbabwe products, and the international position of a particular industry or industries of potential interest to Continental for investment purposes.

  * visit one or more potential US or Canadian investment groups who would consider taking equity in Continental Capital, or who could co-invest alongside Continental Capital in the foreign portion of an export oriented investment.

- this combination of formal training (Institute) and related activity, will expose Continental Capital to the best North American venture capital

players and dozens of investee companies. This will broaden managements outlook, establish networks for both potential co-investors in deals and potential joint ventures, etc., and challenge management to new levels of achievement in their own market.

the objectives outlined above for the short to medium term period can be accomplished efficiently in this manner. The Study Team did not have sufficient time to detail this outline any further, and additional consultation with Zimbank and the new management is required.

Second and third years: on-site support (apprenticeship) can be reduced to two periods of 4 - 6 weeks each, with the senior venture capital executive visiting for two periods of two weeks each. However, on going communication by fax, telephone and computer modem should continue with the senior advisor (mentoring), including review of investments recommended for financing, and monitoring results on investments in place. The focus during this period would be the areas outlined above for the medium and long term.

Fourth and subsequent years: on-going support (mentoring) by telephone, fax and computer modem as required will continue to be needed, but visits to Zimbabwe could probably be limited to two week periods by either of the two investment officers familiar with the local market. These trips should coincide with regular Director or investor meetings and other activities of importance to Continental Capital.

RECOMMENDATIONS: OTHER TECHNICAL ASSISTANCE AND TRAINING

Arising from our overview of the Zimbabwe market, and drawing on earlier observations about developments in the Southern Africa region, the Study Team feel the following areas are worth exploring by USAID:

- already mentioned above as of prime interest to Contintental Capital, there is an urgent need to establish a venture capital association bringing together venture capital investors, intermediaries such as accountants and

and lawyers, government ministries allied to business development and small enterprise support, international agencies involved in business development, etc. This could begin informally on an organized adhoc basis, but should quickly lead, within one year, to holding a two day conference, with an appropriate program of speakers and workshops, to bring all interested parties together. This could also mark the formal establishment of the new association. A key objective of this conference program should be to attract active involvement and participation by funds seekers. This conference could be built around areas as basic as "how to write a business plan", or "where to go for help " workshops. or be as advanced as the "show and tell" programs referred to above. The conference and association should be targeted for regional participation throughout South Africa, positioning Zimbabwe as an industry leader.

- the SEDCO activity referred to above (see Encouragement of the Private Sector, Training Programs and Zimbabwe's Venture Capital Industry sections above), and new areas being considered by SEDCO deserve USAID tactical consideration. The Study Team is advised that SEDCO are considering a small enterprise equity funding program built on the Canadian Federal Business Development Bank venture capital program. In our opinion, adding another parastatal equity funding program would be extremely costly relative to funds provided to firms, would be buraucratic and slow to act, and would be another form of government involvement when Zimbabwe needs more private sector development. Nevertheless, there is a need at the low end, start-up and small scale enterprises. In our opinion it might better be met through the US Small Business Investment Corporation model, stimulating small scale enterprise private sector financing organizations by leveraging private sector funds. Despite criticisms, the SBIC program has made a major contribution to the US economy and venture capital industry, and deserves to be considered in the Zimbabwe context. It could be launched through SEDCO rather than creating another parastal organization.

- the Small Business Problems Solver pocket guide series produced by SB Capital has created a great deal of interest, both at Zimbank, but more particularily First Merchant Bank. Production of this self-help series, and its wide availability throughout the country, could be a major benefit for small and medium sized enterprise development, This series is currently

licensed to banking organizations in South Africa, the United States and Canada and rights in Zimbabwe could be made available.

- provision of equipment and training to upgrade management systems and communication at Continental Capital, and/or its investee companies, is a potential participation area for USAID. Equipment would include note book and desk top computers, file servers, printers and related supplies. Software would also be required. Training personnel are available in Zimbabwe, but we have not had the opportunity to confirm the quality of support available and likely outside assistance will be needed. This is a unique opportunity to position the best of developed world technology in a variety of developing world companies to make them international level players.

- USAID should consider a program of public relations both in Southern Africa and in the United States as the success of the African Venture Capital Project is realised. VCCZ is a sound accomplishment despite any misgivings about its lack of return on investment focus expressed above. Hawk Ventures is for real, a symptom of things to come. Continental Capital should get going and has the potential to be an early winner. The world wide venture capital community is interested in these developments. In Southern Africa well directed publicity could stimulate even more venture capital interest and potential development. In the United States it would not only recognize a significant USAID success, but it would stimulate other venture capital and institutional investors to take a fresh look at the opportunities in Southern Africa in general, and Zimbabwe in particular.