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UNITED STATES OF AMERICA
AGENCY FOR INTERNATIONAL DEVELOPMENT
REGIONAL DEVELOPMENT OFFICE/CARIBBEAN

November 2, 1994

MEMORANDUM

DATE: November 2, 1994

REPLY TO ATTN OF: PB/ PDO, Paul Bisek

SUBJECT: PACR - Agricultural Venture Trust - 538-0140

TO: POL/CDIE/DI, Ms. Lee Clift

Please find the above subject PACR conformed copy for your files. Thank you.

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CLOSE OUT REPORT OF THE AGRICULTURAL VENTURE
0140.01).

The Agricultural Venture Trust (AVT) is a venture capital fund which provides equity investments to enterprises in the non-traditional agricultural sector of the Eastern Caribbean. A project supporting the AVT was initiated by A.I.D. on September 29, 1986 (A.I.D. Project No. 538-0140.01) for the purposes of: a) contributing to foreign exchange earnings through higher levels of exports; b) substituting imports on a competitive basis; and c) demonstrating attractive returns to non-traditional agricultural ventures, at acceptable levels of risk. The project was completed on July 15, 1993.

The project was designed to respond to a need of enterprises to reduce their heavy reliance on loan financing from banks. It sought to encourage the expansion of equity investment and the development of financial markets in the region through the establishment of reliable administrative systems; credible business plans; and open management structures in order to increase investor confidence and knowledge. The AVT was not allowed to take more than a forty-nine percent share in any enterprise, nor provide any financing other than equity financing, i.e., no short or long term loans.

The AVT was originally established as part of the AID-financed High Impact Agricultural Marketing (HIAMP) project. The goals of this project were wider than those of the AVT itself, and the organization of the project was more like a development agency rather than those of a commercial venture capital fund. In fact, the AVT was not expected to be involved only in commercial ventures, but in addition, the project envisioned the AVT making "reimbursable grants" to intermediary institutions in the region, that in turn would lend or take equity positions in their clients' enterprises. The Eastern Caribbean Agribusiness Development (ECAD) agency, acting as a sister agency to the AVT, was responsible for performing all the project development, appraisal and monitoring functions on projects financed by the AVT. The overall project was designed in this way to give the AVT a solid base in terms of the quality of its portfolio and the appraisal and monitoring skills of its staff. It also meant that the AVT administrative expenses were covered by A.I.D. grants.

The HIAMP project was completed in 1991, and the AVT was then compelled to address the issue of transforming itself into a commercially viable venture capital fund which could stand alone by its PACD without support from donor agencies. A.I.D. reduced the amount of planned contributions to the AVT's capital base in 1992, from an anticipated $12.0 million to $8.2 million, due to a concern over involvement in "firm level" projects, as opposed to projects that dealt with broader private enterprise development constraints. A.I.D. continued to support its administrative expenses until the PACD.

A total of dollars $11,960,316 was obligated to the AVT for its investment fund, administration, and technical assistance. The AVT invested in 31 enterprises and intermediary institutions throughout the region over the project life, and investigated investment possibilities with many more.

This report is drawn in large part from the project's contracted close out report and evaluation, conducted from June 7 to 23, 1993, and financial reports from the RDO/C Controller Office.

- THE CURRENT STATUS OF AVT'S INVESTMENT PROGRAM, INCLUDING A BRIEF DESCRIPTION AND STATUS OF THE AGRICULTURAL ENTERPRISE INVESTMENTS, THEIR SUCCESS/FAILURE RATES, PROFITABILITY, AND OTHER CHARACTERISTICS.

The AVT invested directly and indirectly through intermediaries in a variety of agricultural enterprises, e.g. production, processing and marketing of: aloe vera; yogurt; meat products; tropical flowers; fruit preserves and drinks, among others. Project selection was largely based on local or export market analysis and potential, and criteria such as foreign exchange earnings or savings were important. Throughout the life of project, the AVT built upon its experience and refined and improved upon its project selection.

An appraisal of the AVT was conducted in June, 1993, just prior to the project PACD. The appraisal reviewed the institutional aspects of the AVT as well as twenty eight enterprise investments (the AVT disbursed to 31 distinct enterprises over the life of the project). Of the twenty eight, six were found to be non-operational or defunct, i.e., not producing or marketing products. Nine enterprises were in the evaluation or early investment stages. The remaining thirteen projects could be regarded as fully operational, producing and marketing commodities. Some of the operational projects were experiencing difficulties, such as financial management and marketing difficulties.

The summary table in Annex 1 to this report provides a schedule of AVT investments and their status as of June 22, 1994, almost one year following the PACD. Of the 31 investments, eight are determined to be non-operational. Twenty three can be viewed as operational.

One of the common features among the projects was the existence of cost overruns, particularly in the construction phase, but also during implementation. This contributed to working capital difficulties in the pre-operational and operational phases. The enterprises consequently became overly reliant on bank overdrafts. This contributed to strained relations with commercial banks. The cost overruns were caused by poor estimating on the part of the project investors.

With approximately $8.16 million in equity capital, the AVT has a significant amount of resources to continue to benefit the region. The important variables in the future sustainability of the AVT are: the amount and profitability of its equity investments; and its administrative expenses.

In its last year of the project, the AVT considerably reduced its dependency on A.I.D financing for its administration by reducing numbers of staff and operational costs. AVT administration has been supported completely since the PACD by investment fees and dividends, and administrative costs are projected at manageable levels in the future (approximately $255,000 from a 1991 high of $769,000), provided the capital base remains of sufficient size to generate returns that cover administrative costs and inflation.

The capital base of the AVT will be adversely effected by non-performing and non-operational projects, and greater reliance will be necessarily placed on ensuring the viability and profitability of remaining investments. Over the coming years, the viable investments of the AVT should be maturing, providing the AVT with the opportunity to reinvest and generate revenues. To date, only one AVT equity investment, Hadley Blooms in St. Vincent, has been partially liquidated in a share repurchase transaction with the principle of that enterprise.

- A SUMMARY OF THE FINANCIAL CONTRIBUTIONS MADE BY THE AVT, OTHER INVESTORS, AND A.I.D. IN AGRICULTURAL ENTERPRISE INVESTMENTS

Over the life of the project, A.I.D. committed $11,906,738 to the AVT. Of this amount $11,869,278 was expended under the following budget elements:

Budget Element	Committed	Expended	Balance
Trust Administration	2,830,663	2,802,078	28,585 [1]
Long Term Technical Assistance	746,538	746,538	0
Equity Investments and Grants	8,221,087	8,162,222	58,865.00[2]
Project Advisor	108,450	108,450	0
Totals	11,906,738.00	11,819,288.00	87,450.00

As of June 1994, all remaining balances have been liquidated or decommitted, with the effect of there being no outstanding expenses or encumbrances under the project.

No detailed audit of the other donor contributions has been performed. The AVT did pursue joint financing with a number of other donor financed equity funds, such as the Commonwealth Development Fund, the InterAmerican Finance Corporation, the European Investment Fund, and the International Finance Corporation, but did not consummate any financial collaboration on any investment in the region.

[1] Final audit costs have yet to be charged against this unexpended balance, 6/15/94.

[2] Represents amounts decommitted from previously approved investments.

The AVT did leverage a considerable amount of other resources. Since AVT share ownership was limited to 49 percent, one can assume that an additional $8.5 million in resources were contributed to the project by other investors. Loan capital frequently represents between 50 and 150 percent of share holder equity in AVT enterprises. A conservative estimate of loan capital contributed to the investments is $8.0 million. All in all, the total estimated amount of investment under the project approaches $24 million, of which slightly more than a third was contributed by A.I.D.

- AN ASSESSMENT OF THE EXTENT TO WHICH THE AVT HAS ACCOMPLISHED THE PROJECT PURPOSE AND THE ISSUES OF AGRICULTURAL INVESTMENT IN THE EASTERN CARIBBEAN;

The Project Logframe included in the project paper that authorized the AVT project outlined the following outputs:

- Equity fund investments made to 28 firms and reimbursable grants to 14 firms;

- Value of AVT equity fund does not decline during project life; staff members trained and actively seeking new agricultural investments;

- Intermediary financial institutions to disburse $3.0 million in loan funds throughout project life.

The AVT was able to make a variety of investments in almost all of the targeted territories, with the projects exhibiting a mixed performance in various countries. Some of the projects have only achieved the original purpose to a limited degree. This may be mitigated somewhat by the fact that many of the investments made in 1991 and 1992, so that many of the projects are still under implementation.

As noted above, the AVT managed to invest in 31 different enterprises. The number of private firms was 26, and the number of reimbursable grants was 5. The failure rate is estimated at 25 percent, with some eight projects of thirty one classified as non-operational and the chances of recovery of investment slim. It is estimated that the present value of the AVT's original investments in these projects to be approximately U.S. $2.055 million. Therefore, one can determine that the value of the AVT equity fund has declined at least by that amount.

Approximately 20 professional staff members of the AVT throughout its life of project were trained on the job. At the PACD, the core full time professional staff of the AVT had been reduced to two, with four support staff. While the staff of the AVT became adept at analysis and systems, skills in agribusiness management and operations appear to be limited.

Perhaps the one objective that has been met more than adequately is the amount of loan funds disbursed in conjunction with the AVT equity. As noted above, the estimated amount of loan capital is $8.1 million. Even if this figure is conservatively slashed, it appears that the AVT accomplished an objective to leverage additional resources for regional enterprises.

- RECOMMENDATIONS FOR FINAL ADJUSTMENTS TO THE ADMINISTRATION AND OPERATIONS OF THE AVT;

A strategy of taking long term equity positions in risky agribusiness enterprises is unsuitable to an institution such as the AVT that hopes to offer financial services to regional businesses on a self sustaining basis and to see its capital base grow. This strategy may have been suitable under conditions whereby a donor is willing to subsidize the operations over a sufficiently long period, but this is no longer the case with the AVT. A.I.D. has completed its support, no other donors appear to be willing or able to support the AVT, and now the strategy must be based on equating revenues and costs. Since the operations of the AVT require a steady stream of revenue, the portfolio must be diversified to include short term and liquid investments with dependable rates of return. Limiting the AVT to agribusiness ventures does not permit the institution to invest in sectors where returns possibly could be higher.

The AVT must be restructured to: a) permit it to offer short term financial services, such as loans, and diversify the types of financial services it offers to its clients; b) permit flexibility in the types and sector of enterprises in which it invests, not limiting it to agribusiness; and c) support a productive administrative staff on a cost effective basis. The AVT should speedily pursue these initiatives through alterations to its Trust Deed.

With the significant number of projects which it has under implementation, the monitoring and investment administration functions of the AVT will continue to be very important activities and indeed, maybe its only major activities for some time. This means that the AVT should ensure that it has personnel available, to enable it to undertake these activities efficiently and cost effectively. In this regard the institution will want to have staff who are multi-skilled, who can assist in the carrying out of day to day administrative functions, as well as engage in project monitoring and advising clients on marketing, management, accounting and record keeping, and other technical issues. It would also want to keep on call personnel (consultants) who have the required skills to assist clients on unique issues, where necessary. Such personnel would be hired and paid on a job basis. The cost of their services being charged to the project. The AVT may also seek to obtain assistance and funding from some of the regional and international agencies in order to defray some of these costs.

The AVT should continue to charge front end and negotiation fees, to cover the administrative and other costs directly associated with its investments. However, it needs to carefully review these as many clients were of the view that they were somewhat excessive, particularly the legal costs. It should also avoid reducing the total amount of funds actually invested for productive inputs into the projects, by adding the fees to the required investment, rather than deducting them. It should also ensure that project sponsors are fully apprised of the various charges before hand.

In the case of those projects which are non-operational and beyond recovery, the AVT should seek to salvage whatever they can cost effectively and write off the investments. To do otherwise will result in additional administrative costs which the Trust cannot afford. the institution has already begun to implement this policy.

In the future, the AVT should consider disbursement in tranches, particularly for large investments, say over $50,000, since they can earn revenue on the balances by investing these in short term instruments, rather than placing them with projects where they are not utilized for long periods. They are compelled to disburse in blocks due to a requirement that the AVT's share certificate reflect the full amount of the investment. Though this is understandable for the purposes of A.I.D. accounting, it is neither logical nor effective after the PACD.

The inability of the AVT to take majority positions and to make loans weakens the AVT's ability to influence the outcome of its projects when difficulties arise. To be truly effective, the providers of venture capital must have the flexibility to make financing arrangements appropriate to the needs of the given enterprise. It may sometimes be in the best interest of the enterprise for the venture capitalists to take control or to advance loan funds secured by the beneficiary company's assets. The ability to expeditiously inject capital by way of loans with appropriate conditions attached may be the most effective method of protecting the AVT's equity investment. The AVT are encouraged to investigate the possibilities of varying the trust deed so as to permit the advancing of loans.

The process adopted by the AVT in declaring default on a project is so cumbersome and time consuming that it diminishes any practical possibility that the AVT may be able to take control at the appropriate moment to protect its interest. The AVT is reduced to being a spectator at the time that it most needs to take charge. This procedure is in need of streamlining. On the occurrence of an event of default, the AVT should immediately have the option of acquiring the requisite number of shares from the other shareholders so as to take control. The AVT may be well advised to seek, with the concurrence of A.I.D. a court ordered variation of the trust deed along the lines suggested.

Stronger action needs to be taken with those projects where repurchase of shares is due and where the investors seem to be adopting dilatory tactics. At the same time, the AVT should continue to exert its influence through moral suasion and other means, on the investor in those projects which are behind schedule in implementation to speed up things, with out jeopardizing the viability and proper implementation. The AVT may need to exercise its default clause in a few instances, and publish this fairly widely in order to let the investors know that it intends to recover its investments. However, the process of the exercising the default clause needs to be simplified as it is currently too lengthy and cumbersome. This clause should therefore be reviewed and simplified.

A concern expressed by some entrepreneurs related to the length of time which may elapse between the financing agreement with the AVT and the actual disbursement of funds. These delays are principally caused by the non-fulfillment of conditions precedent to disbursement. During this interval it was possible that critical aspects of the project, most especially costs, might change. The AVT should consider inserting into the financing agreements a clause which provides for the automatic review of the project's financing needs where no disbursement has taken place within six months of the financing agreement.

The AVT may be called upon to make additional investments in projects under implementation. Ensuring the availability of funds to support ongoing projects is another rationale behind holding some of the AVT assets in short term liquid investments.

- DEFINITION OF CONTINUING AND POST-PROJECT MONITORING RESPONSIBILITIES ON THE PART OF A.I.D.;

The A.I.D. grant agreement with the AVT states that A.I.D. must give its approval prior to any decision tc terminate the Trust. Such a decision however is not contemplated, and the current management and Board of Directors of the AVT intends to continue the Trust, perpetually, returning the full amount of income earned from equity investments and grant repayments.

After the PACD, when funding for administrative expenses ended, the Trust contracted management services to be paid for from the income accruing to the Trust. As per the grant agreement, reflows are to be invested at the discretion of the Trust in a manner consistent with the objective of the Trust. Accordingly, all reflows shall be accounted for separately from the funds disbursed by U.S.A.I.D.

A draft final compliance audit of the AVT was submitted to the AVT in March of 1994 with the following recommendations:

a) With regards to advance request reporting, management of the AVT should ensure that supporting documentation is maintained for review by AID and/or its cognizant auditors;

b) With regards to miscellaneous cost reporting, greater care should be exercised when filing payment vouchers, to ensure easy retrieval;

c) With regards to direct salaries, and specifically allowances and fringe benefits, it could not be determined whether certain disbursements had been made in accordance with A.I.D. regulations and contracts. File keeping should be improved to enable easy retrieval of all supporting documentation when required for examination by A.I.D. and/or its cognizant auditors;

d) With regards to travel and transportation, several supporting documents could not be located, and the project could have been charged with ineligible expenditure. The AVT should ensure that adequate supporting documentation is maintained for review by AID and/or its cognizant auditors.

Related to the above recommendations were questioned costs of U.S. $854.00 for travel expenses and $49,895.00 of Trust administration expenses, due to an inability of the auditors to locate supporting documentation. Upon receiving details of the questioned cost items, the A.I.D. Controller has agreed to search project vouchers, where original supporting documentation is attached, in an attempt to substantiate the questioned costs. Bills for collection will be issued to the AVT for unsubstantiated costs.

- A SUMMARY OF LESSONS LEARNED FROM THE PROJECT THAT MIGHT BE RELEVANT TO POLICY, PROGRAMMING, AND THE DESIGN AND IMPLEMENTATION OF RELATED ACTIVITIES IN THE EASTERN CARIBBEAN.

The final evaluation report cited the following general lessons learned from the AVT project:

- The gestation periods for agricultural projects in the region and the time required for returns on the investments, are considerably longer than originally expected. Implementation and financing schedules need to be critically reviewed, as well as assumptions regarding availability of inputs, access to markets, dependability of supporting infrastructure, and the capabilities of the enterprise management;

- There is a need for close monitoring of investments and the provision of technical, financial, managerial and marketing advice, throughout the life of the investments. Several cases of cost overruns, and subsequent difficulties with creditors might have been avoided with closer monitoring, or at least a closer AVT-client relationship. The AVT should be capable of exercising measures to protect its interest and ensure project viability when difficulties arise;

- Working capital requirements need careful assessment and monitoring. Disbursements must be controlled to ensure that funds are used for the purposes intended;

- Over dependency on single markets, and or single products is risky. Markets and ways to reduce risks through product diversification need to be carefully assessed.

Perhaps the major lesson learned, or rather confirmed, from the AVT experience was alluded to in the prior section outlining the recommendations for AVT administration. That is: a financial institution encumbered with limitations on where and how to invest for the sake of development goals may be constrained in achieving the commercial orientation required for the institution to be sustainable. The experience with directed credit projects worldwide has demonstrated this lesson time and time again.

In the AVT's case, the development of equity investment mechanisms for agricultural enterprises; the training of staff; and the demonstration of adequate returns to agricultural enterprises at acceptable levels of risk are development goals that are broader than mere commercial viability. The AVT was successful in achieving, at least partially, its objectives. However, there was considerable difficulty experienced by the AVT in weaning itself from A.I.D. support for the functions of investment appraisal, design, monitoring, and trust administration because cost recovery was secondary to assisting enterprises and demonstrating the successful operation of equity financing mechanisms. When A.I.D. financing for administration ended, and capitalization of the equity fund was cut short by almost $4.0 million, the AVT was burdened with a portfolio locked into long term investments, and limited sources of current revenues.

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Clearances:
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Annex 1. Schedule of AVT Investments as June 23, 1994

NAME	COUNTRY	TYPE OF PROJECT	YEAR DISBURSED	AVT EQUITY	STATUS
1. Barte Meats	Grenada	Meat Processing	1988	430,219	Operational
2. Lisco	St. Kitts	Shrimp Cultivation	1991	180,000	Non-operational
3. Nonsuch Ltd.	Antigua	Pineapples	1988	61,357	Operational
4. Windward Island Aloe	Dominica	Aloe Production/Processing	1987	710,000	Non-operational
5. Windward Island Tropicals	St. Lucia	Tropical Plants/Fruits	1989	498,621	Operational
6. Stonefort Farms	St. Kitts	Vegetables	1988	52,638	Non-operational
7. NDF Dominica - Passion Fruit	Dominica	Passion Fruit Production	1987	227,700	Reimbursable Grant
8. Corona Development Ltd.	Dominica	Passion Fruit Processing	1988	72,930	Non-operational
9. Southern Agronomics	St. Kitts	Ethanol Production	1988	493,000	Non-operational
10. Funtime Products	Grenada	Seamoss	1989	71,708	Non-operational
11. Ferrand's Dairy	St. Lucia	Dairy Products	1991	500,000	Operational
12. NDF Barbados	Barbados	Small Farmer Assistance	1991	173,588	Reimbursable Grant
13. ORD	St. Vincent	Horticulture	1988	453,423	Reimbursable Grant
14. Newfoundland Estate, Ltd.	Dominica	Horticulture	1993	389,300	Operational
15. Abbott Farms	Antigua	Livestock	1991	424,300	Operational
16. Sunshine Meats	Grenada	Pork Production	1991	500,000	Operational
17. Agro Industries	St. Lucia	Fruit Production	1991	122,593	Operational
18. Windward Lines	St. Vincent	Shipping	1991	500,000	Operational
19. NDF Dominica Carambola	Dominica	Fruit	1989	6,157	Reimbursable Grant

- 11

20. Choiseul Fruit Co./Mt. Lezard Fruit	St. Lucia	Fruit	1990/1992	493,146	Operational
21. Rainbow Tropical	Barbados	Horticulture	1990	400,000	Non-operational
22. Cox Heath Farms	BVI	Sheep	1992	70,000	Operational
23. Sanmac	Barbados	Cut Flowers	1993	98,039	Operational
24. Sugar and Spice Ltd.	Grenada	Frozen Desserts	1993	166,667	Operational
25. Erica's	St. Vincent	Spices	1990	68,773	Operational
26. Tropical Trading Inc.	Barbados	Yogurt Products	1991	74,020	Non-operational
27. Hadley's Blooms	St. Vincent	Cut Flowers	1991	653,703	Operational
28. Tropical Blooms	Barbados	Cut Flowers	1992	110,294	Operational
29. Ro-An Cottage Industries	Barbados	Jams, Jellies	1993	22,059	Operational
30. Rainbow Products	Grenada	Fruit Processing	1991	115,370	Operational
31. NDF St. Vincent	St. Vincent	Passion Fruit	1990	22,617	Reimbursable Grant
Totals				8,162,222.00	
Investment Average				263,297.48	
Amount Non-operational				2,055,276.00	
Amount Grants				892,350.00	
Percent of Non-operational in Total Investment Fund				0.25	