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INVESTMENT PROPOSAL
FOR
REVOLVING FUND
THAI VENTURE CAPITAL LIMITED

US\$3,000,000 LOAN
TO
THAI VENTURE CAPITAL LIMITED

OFFICE OF INVESTMENT
BUREAU FOR PRIVATE ENTERPRISE

JANUARY 1987

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

This project is the first in a program of technology-oriented venture capital initiatives planned by PRE. Other environments being investigated as to suitability for a PRE initiative include Sri Lanka, Indonesia and the Philippines.

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ASEAN VENTURE DEVELOPMENT LIMITED

I. EXECUTIVE SUMMARY

A. The Project

- 1.01 PRE/AID proposes to loan US\$3.0MM to Thai Venture Capital Ltd., (TVC or the "Company") a company under organization by a number of Thai commercial banks which will make equity investments in projects featuring the commercialization of principally, agribusiness technology of United States origin.
- 1.02 The concept of TVC has been refined and jointly promoted by PRE and USAID in collaboration with Siam Commercial Bank (SCB). SCB has subsequently become the lead sponsor, working closely with PRE to finalize a business prospectus, resolve regulatory and legal issues and approach potential shareholders. SCB has held meetings with other Thai banks and has received commitments in principal for the full equity capitalization required. Thai Farmers Bank and SCB will jointly control 60% of TVC as co-sponsors with the balance held by a number of additional commercial banks, all of whom are known to AID. It is the intention of SCB to organize TVC as a venture capital firm by February 28, 1987 having reached agreement by January 31, 1987 with shareholders on the designation of a Managing Director for TVC (the Company). The managing director will assume responsibilities on the day TVC is organized to do business in Thailand.
- 1.03 Primarily, the Company is expected to promote the transfer of agribusiness technologies from the U.S. to Thailand; to arrange joint ventures ("Subprojects") between U.S. and Thai firms to implement such technologies in Thailand; to organize debt and equity capital requirements of such Subprojects; and to take equity positions in them.
- 1.04 The Company's central investment objective is to seek long term capital appreciation by making debt and equity investments in new and existing companies believed to be engaged in the processing of products which feature innovative agribusiness technologies. These Subprojects will largely have the following characteristics:
- (a) are commercially viable, offering potentially significant returns to the Company.

- (b) incorporate product, process or management technologies imported from the U.S. which can be immediately applied to the exploitation of Thailand's agricultural resource base.
- (c) involve a product , process or management technolgy which has a demonstrable track record.
- (d) are eligible for significant fiscal and economic incentives awarded by the Thai Board of Investments (BOI).
- (e) generate exportable product.

1.05 The Company intends to recommend all approved Subprojects to make application to the Securities and Exchange of Thailand (SET) for the Subproject to become a registered company.

B. Capitalization

1.06 The Company will be capitalized at US\$6.0MM of which US\$3.0MM will be Thai equity and US\$3.0MM will be long term debt from AID.

C. Developmental Benefits

1.07 As a result of this project, PRE will be able to demonstrate the effectiveness of a venture capital approach to: a) transfer of agribusiness technology to Thailand; and b) development of local capital markets. PRE plans to introduce this approach in a number of other Asian countries, notably Indonesia and potentially adapted versions in Sri Lanka and the Philippines.

PRE's objective in using of Revolving Fund resources is to create models for effective collaboration with the private sector for achieving Agency development goals. The venture capital model outlined here has broad application for AID. Design discussions drawing on the Thai Venture Capital model have already begun with USAID's in the Philippines, Indonesia and Sri Lanka. In each of these environments, the business sector has also indicated real interest in the Thai Venture Capital approach to investment and technology transfer. It is likely that USAID activity in Kenya on this subject will benefit from consideration of the Thai model. In Latin America, Ecuador would appear to be a suitable home for a venture capital approach to equity mobilization and technology transfer. In short, PRE judges the model for venture capital as will be tested by this project in Thailand, to have significant design value for AID worldwide.

The transfer of technology to environments such as Thailand require the presence of system support. The proposed TVC structure represents such support by organizing: a) complementary local financial resources; b) proven local management to undertake commercial production; c) ability to navigate local regulations and customs; and d) engagement of proven technologies suitable for commercialization. PRE believes that the system represented by TVC will be a model local institution for achieving technology transfer through the private sector.

The proposed venture capital project will also contribute to the development of Thai capital markets on two levels. At the first, the level of capitalization of TVC, the project mobilizes domestic savings for equity investment, the scarcest form of investment capital. At the second, the Subproject level and significantly larger in magnitude, the project attracts local savings through private then public securities issues. Price earnings multiples of ten are common, offering leverage to A.I.D. of ten to twenty times A.I.D.'s commitment.

As an alternative to listing the shares of subprojects on the Bangkok exchange, exit may be sought after consideration of transaction costs and market perception through: (a) private placement, which by the way is used extensively by U.S. venture capitalists; (b) public offering of the Thai Venture Capital Company itself on the Bangkok exchange or, possible on the Singapore exchange.

Fundamentally, this project will generate self-sustaining employment from the application of high value-added technologies to Thailand's natural resource and labor base. As discussed in chapter three below, this directly complements Thailand's developmental focus. The emphasis on commercialization also dovetails, as stated by USAID, with the USAID Science and Technology Development Project stressing R & D in biotechnology.

D. Co-Financing with USAID/Thailand

This initiative is the result of mutual interest of USAID and PRE in development of private sector initiations for the mobilization of equity for productive investment purposes. PRE and USAID have

engaged in extensive discussions of alternative business concepts for venture capital approaches to equity mobilization. As a result of discussions over the last 12 months, PRE's venture capital project has been refined to reflect USAID interests in seeing the venture capital initiative fit with other USAID initiatives in the area of technology development. In light of USAID's significant activities in technology development, the venture capital concept has taken a clear technology focus, emphasizing the commercialization of proven agribusiness technologies (say from the U.S. market place) in Thailand. As the venture capital project matures, it is anticipated that USAID's technology development projects, such as the Science and Technology in Development Project, will be a source of technology concepts for commercialization.

USAID is considering co-financing This project by providing a reimbursable training grant of US\$50,000 for the purpose of enabling TVC management to spend training time with a number of U.S. venture capital companies. USAID grant participation in addition to USAID design participation makes this project an example of PRE/Mission collaboration in implementing the Agency's private sector initiative.

E. Project Timetable

1.08	IOP	10/30/86
	IP	1/15/87
	L/A Negotiation	1/26/87
	Authorization	2/28/87
	L/A Signing-Obligation	2/28/87
	First Disbursement	6/00/87

F. Risk

Venture capital by definition is higher risk balanced by higher rewards. The success of TVC will turn on the strength of management provided by the shareholders and the quality of the subprojects. To optimize high quality management, PRE has teamed with proven commercial lenders who will provide management and management oversight. To optimize investment, TVC has adopted the concept of investing only in proven high

return technologies which are commercialized by established Thai operating companies. The only other credible initiative in this market, that attempted (but never consolidated) by Advent International of T.A. Associates, Boston, also selected commercial lenders as the optimum platform of local support and also promoted the concept of investment in proven technologies.

G. AID/PRE Issues

1. Impact on Reflows to Revolving Fund. The project calls for a ten year loan with five years grace on principal repayment. The average life of the loan, assuming no prepayment, is eight years, an increase in the average loan life of the RF portfolio. Mitigating this slowing of reflows is: a) the profit participation feature which is estimated to return to the RF an amount equal to the loan by year seven; and b) obligatory repayment upon substantial divestments for capital gains. Together the loan and profit participation feature can deliver to the RF a total of US\$1.2MM by year five; US\$2.4MM by year six; and US\$6.0MM by year seven assuming significant sales for capital gains.
2. U.S. Trade Policy. General Counsel has ruled that Lautenberg and Bumpers amendments are not strictly applicable for IFC projects of this variety.

II. THE COMPANY

A. Sponsors

2.01 The sponsors of Thai Venture Capital Limited are as follows:

1. The Siam Commercial Bank, Limited, a limited company registered under the laws of Thailand, with its registered office at 1060 Petchburi Road, Bangkok (hereinafter referred to as "SCB")
2. The Thai Farmers Bank, Limited, a limited company registered under the laws of Thailand, with its registered office at.....
.....
(hereinafter referred to as "TFB")
3. The Thai Danu Bank, Limited, a limited company registered under the laws of Thailand, with its registered office at.....
.....
(hereinafter referred to as "TDB")

4. The Bank of Asia Limited, a limited company registered under the laws of Thailand, with its registered office at.....
.....
(hereinafter referred to as "BA")
5. Nakornthon Bank, a limited company registered under the laws of Thailand, with its registered office at
.....
(hereinafter referred to as "NTB")

2.02 SCB together with TFB will take the lead in promoting and incorporating the Company in Thailand. All sponsors will participate in the equity of the Company and also assist in providing for the management of the Company.

2.03 The sponsors will subscribe to the issued shares in the capital of the Company amounting to US\$3.0MM equivalent as follows:

Subscriber	percentage of shares subscribed	number of shares
SCB	30
TFB	30
TDB	10
BA	10
NTB	10
Others	10
	100%

B. Investment Objectives and Policies

2.04 The Company's primary investment objective is to seek long term capital appreciation by making debt and equity investments in new and existing companies believed to be engaged in the processing of products which feature innovative agroindustrial technology (hereinafter referred to as "Subprojects"). These particular Subprojects will have the following characteristics:

- (a) are commercially viable, offering potentially significant returns to the Company;
- (b) incorporate product, process or management technologies imported from the United States and other industrial countries which can be applied to the exploitation of Thailand's natural agricultural resource base;
- (c) involve a product, process or management technology which has a demonstrable track record in implementation elsewhere, suggesting that the technical and managerial risks involved are well understood and manageable,
- (d) are eligible for significant fiscal and economic incentives awarded by the Thai Board of Investments; and
- (e) generate exportable product.

2.05

The Company may also make investments identified as follows:

- (a) the Company may invest in financially troubled companies in bankruptcy or under reorganization if the Company determines that an infusion of capital or additional managerial expertise will enable such companies to operate profitably. Investments in these special situations will be made only in those cases where management has defined or identified a specific strategy for improving operating performance;
- (b) investments will be made in situations in which a reasonable opportunity for liquidity is apparent, such as the fact that a prospective Subproject or portfolio company would likely be the subject of a later acquisition and/or public offering.
- (c) the Company intends to invest in companies that can employ relatively small amounts of capital productively. Capital intensive projects will generally be avoided.

However, the above are not fundamental policies of the Company and may be changed at any time by the company's Board of Directors. They will remain flexible so that the Company may adapt to a continuously changing investment environment.

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2.06 In general each Subproject organized by the Company, funding and ownership would look as follows:

	<u>Funding</u>	<u>Ownership</u>
The Company	25%	25%
Agroindustrial Firm	75%	55%
Technology Proprietor	NIL	20%

Although the domestic agroindustrial firm suffers the dilution of its investment to accommodate the technology proprietor, it remains a majority owner and principal beneficiary of the Subproject.

In addition, the Company would mobilize required debt for each Subproject, in local or foreign currency as needed, either from third party domestic or foreign financial institutions, e.g. ADB and IFC. Commissions earned in this activity would be a source of revenue to the Company.

2.07 The Company intends to establish commercial relationships with technology proprietors and brokers, particularly in the United States who in assisting in implementing a given Subproject shall be eligible for some of the benefits, i.e.:

- (a) a general or technical services contract to be provided on mutually agreeable terms over the first 1 - 3 years of the Subproject; and
- (b) up to 20% of the equity in the Subproject in return for the contribution of the technology; and/or
- (c) an annual licensing fee on mutually agreeable terms in return for the contribution of the technology; and
- (d) a royalty, amounting to a percentage of total sales generated by the Subproject for a predetermined period

C. Listing Subprojects on SET

2.08 The Company intends to recommend all approved Subprojects to make application to the Securities Exchange of Thailand (SET) for the Subproject to become a registered company or an authorized company, if qualified as such.

In addition to the above mentioned objectives, the Company may also make venture capital investments as a co-investor with other professional venture capital groups and may engage in any other business to the extent that such engagement is not prohibited by or contravened any Thai laws, regulations, announcements or any other governmental directives applicable to or binding upon the Company as the Board of Directors of the Company from time to time considered appropriate. The Company's activities will be almost exclusively in Thailand, but will not otherwise be focused in any geographic region.

D. Organization of the Company

2.09 Board of Directors

(a) Unless otherwise agreed, the Company shall have 10 directors and so long as the parties thereto maintain beneficial ownership of the share capital of the Company as below stated they shall be entitled to designate the number of directors indicated and the parties shall procure that such designated persons are so appointed as directors:

	Percentage of shares beneficially owned	Number of directors to be designated
SCB	30	
TFB	30	
TDB	10	
BA	10	
NTB	10	
Others	10	
	----- 100% -----	----- ----- -----

(b) The Chairman of the Board of Directors of the Company shall at all times be a nominee of.....and shall be entitled to a casting vote.

(c) The Board of Directors of the Company may designate a director to be managing director of the Company.

a

- (d) The quorum for a meeting of the Board of Directors of the Company shall be.....(.....) of the directors in office, present in person or represented by proxies.
- (e) At the Meeting of the Board of Directors a resolution shall be effective if it shall have been passed by a majority vote of the directors present and entitled to vote.
- (f) The Company's management, operation and all business investment and transaction shall be under the control of the Board of Directors. In making any decision under the authority conferred to it, the Board of Directors may consult any persons, juristic or natural with compensation as the Board of Directors considered appropriate.
- (g) A party desiring to change or replace any of its designated directors of the Company shall notify the other parties hereto of such desire and such other parties shall ensure cooperation in facilitating the desired change or replacement.

E. Call and Transfer of Shares

- 2.10 The shareholders will pay the initial subscription amount and the subsequent calls in Baht to the credit of such account of the Company and at such bank in Thailand as the Company shall notify to the parties.
- 2.11 The shareholders shall not transfer or otherwise dispose of their shares in the Company to any person who either is not of Thai nationality (i.e. an "alien" as that term is defined in Clause 3 of National Executive Council Decree No. 281 or the Thailand Land Code) or considered to be of Thai nationality for purposes of holding shares if this would cause the ownership of shares in the Company held by persons who are not of Thai nationality to exceed...%, or such lesser percentage as may from time to time be amended by the Board of Directors.
- 2.12 Unless and until the Company shall become a public company or the shares of the Company shall be listed on The Securities Exchange of Thailand, none of the shareholders, shall transfer its shares in the Company to a third party without first offering those shares

to the other shareholders in proportion to their respective shareholdings in the Company on the same and identical terms which the transferring shareholder certifies in writing to each that a third party, who shall be named, has offered and which offer is acceptable to the transferring shareholder.

F. Non-Competing

2.13 The shareholders of the Company will not without the consent of the Board of Directors of the Company, undertake commercial transactions of the same nature as and competing with that of the Company, either on their/his own account or that of a third person, nor may he be a partner with unlimited liability or make investment in term of shareholding more than..... percent of the total share capital in another commercial concern carrying on a business of the same natures as and competing with that of the Company.

G. Future Funding of Investments

2.14 Although the Company intends to schedule its investment activities in order to ensure the availability of sufficient cash for working capital purposes, it is possible that the Company may require additional capital in order to continue its operations. The working capital needs of the Company may be met either through borrowings, through a later private or public offering of debt or equity securities, or a combination of debt and equity securities, through exchanges of its securities for the stock of portfolio companies or realized proceeds from the sale of its assets.

H. Portfolio Valuation

2.15 At least quarterly the Board of Directors will value the Company's investments. The Board of Directors also values the Company's securities at such other times as circumstances warrant. The investments shall be valued at either market value or in good faith at fair value, whichever is appropriate under the circumstances.

The Board of Directors will use one of the four methods for valuing securities held by the Company:

- The Public Market Method
- The Private Market Method
- The Appraisal Method
- The Cost Method

I. Board of Investment

- 2.16 The Board of Directors of the Company will decide whether or not to make application to the Board of Investment for promotion of the Company. However, if the Board of Directors decide to make application and the promotion is granted by the Board of Investment then the Company shall duly comply with all conditions thereof.

J. SET Listing for Transformation to Public Company

- 2.17 The shareholders recognize that it may become desirable and in the best interests of the Company and the parties hereto for the shares of the Company to be listed on the Securities Exchange of Thailand (SET) and/or for the Company to be transformed into a public company. Should either or both such actions appear desirable the shareholders shall consult among themselves with a view to amending the terms of this Agreement in a fair and equitable manner so as to cause or permit the Company to take such action(s).
- 2.18 In the event the Company, due to increasing number of shareholders, shall be required by laws to transform into a public company, the shareholders shall set up a meeting to decide whether the Company should be transformed into a public company in accordance with the provisions of the governing laws or the Company should reduce the number of its shareholders in order to maintain its entity as a private Company.
- 2.19 In addition to possible listing on the Bangkok securities exchange, consideration will be given to listing the Company on the Singapore securities exchange. The decision as to which exchange to use will be a function of relative registration cost and perceptions of market acceptance.

III. CREATION OF AN AGROINDUSTRIAL VENTURE CAPITAL FIRM AND ITS RELEVANCE TO THAI DEVELOPMENT

- 3.01 The creation of an agroindustrial venture capital firm (the "Company") which focuses on the commercialization of biotechnologies, and other agroindustrial technologies, is relevant to Thailand's development. The discussion below compares the business objectives of the company with developmental objectives of the Government of Thailand as well as those of the U.S. Agency for International Development.

A. Objectives of the Company

- 3.02 The Company intends to achieve its business objective by making equity and/or convertible debt investments in certain kinds of agroindustrial Subprojects which:
- (a) focus on commercially viable agro-processing and biotechnology activities, offering potentially significant returns;
 - (b) involve (generally) a total project capitalization of less than \$5MM;
 - (c) incorporate product, process or management technologies imported from the United States and other industrial countries which can be applied to the exploitation of Thailand's rural agricultural resource base.
 - (d) involve a product, process or management technology which has a demonstrable track record in implementation elsewhere, suggesting that the technical and managerial risks involved are well understood and manageable;
 - (e) are eligible for significant fiscal and economic incentives awarded by the Thai Board of Investments; and
 - (f) generate exportable product.

B. Developmental Objectives of the Government of Thailand

- 3.03 The focus by the Company on commercial agro-processing and biotechnology activities has the potential for increasing rural incomes because of powerful backward linkages to agricultural employment and forward linkages to transport and rural service sectors.
- 3.04 Some of the objectives of Thailand's Fifth Five Year Plan (1982-1986) are abetted, therefore, by the Company's activities, including the emphasis within the Plan on the creation of employment and the alleviation of poverty and income disparities in rural areas.
- 3.05 The newly approved objectives of the Sixth Five Year Plan (1987-1991) are also serviced by the Company's business focus. These objectives include:

- increasing participation of the private sector as the determinant of sustained growth and development;
- scientific and technological advancement with commercialization of science and technology activities;
- employment generation to remedy growing un- and under-employment, especially in rural areas;
- increased agricultural productivity; and
- reversal of natural resource degradation.

3.06 All, except possibly one of the above objectives are congruent with the business objectives of the Company. Moreover, the Thai Fifth Five Year Plan emphasizes the need to develop and commercialize biotechnology. There is an entire chapter devoted to the subject.

3.07 Biotechnology promises to have a vital impact on Thailand's industry in the areas of agriculture, health care, chemicals, and biomass conversion. Thailand is actively interested in developing bioscience and biotechnology primarily because:

- the country has a vast pool of as yet underutilized natural bioresources that can be developed into useful value-added products;
- moreover, Thailand has a relatively large number of qualified personnel in the areas of basic life sciences, health, food, and agriculture;
- finally, some biotechnology requires relatively low capital input compared with other areas of technology and may be suitable for transfer to, and further development in, the country.

3.08 From a historical perspective the development of biotechnology in Thailand has arisen naturally from the growth of both the supply and demand sides. On the supply side, the last two decades, in particular, have witnessed a remarkable growth and maturity of basic life sciences. This is linked to the emergence of a critical mass of scientists in Thailand trained in developed countries and the establishment of research-based graduate schools.

- 3.09 On the demand side, problems in health, agriculture, and rapidly expanding agroindustry have made it necessary to utilize biotechnology at various levels of complexity. For example, Thailand has reached the limits of its ability to exploit available arable land and must increase significantly the yields of the existing land area. Application of additional fertilizer and improved water management will improve yields in the more favored resource locations such as the Central Plains, but higher yields in other parts of the country, particularly in the northeast, will require the contributions that applied biotechnology research may make in the future to improve crop characteristics.
- 3.10 The lack of adequate linkages between the supply side (largely located in the university sector) and the demand side (mainly located in the private and government sectors) must account in large part for the government focus on biotechnology within the Fifth Five Year Plan. As a result, a Thai National Center for Genetic Engineering and Biotechnology (NCGEB) has been established by the Thai government. This center is conceived as a national program or a "center without walls" to coordinate and facilitate communication among the numerous disciplines required for the practice and implementation of biotechnology in Thailand.
- 3.11 When planning the program of the NCGEB, Thai officials identified 14 areas that fall broadly into the category of biotechnology as major areas for investigation and development. These include:
1. Plant and tissue culture
 2. Rhizobia, mycorrhizal fungi, and organic fertilizers
 3. Bacterial larvicides
 4. Production of selected enzymes
 5. Starch (cassava and corn) conversion
 6. Biofuel production (starch, cellulose, and biomass conversion)
 7. Development of natural rubber
 8. Nutritional biochemicals
 9. Improvement of small- and medium-scale bio-industry
 10. Industrial waste utilization
 11. Development and design of pilot plants
 12. Molecular biology (genetic engineering)
 13. Human and animal health products
 14. Biochemical and food engineering.

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The 14 project goals of the NCGEB logically fall into five groupings:

1. Agriculture (food production)
2. Food processing
3. Health
4. Biochemicals
5. Biofuels.

3.12 Of the first nine Subprojects which have been identified by the Company as suitable for implementation, all fall into one or more of the above five general categories. The nine Subprojects include:

1. Processing of activated carbons from coconut shells for sale to U.S. markets;
2. Irradiation (chicken, shrimp, onions and potatoes);
3. PVC Bunker Storage technology for grains, including export grains such as corn;
4. Extraction of bromelain from pineapple stems for export to the U.S. and/or Japanese pharmaceutical marketplaces;
5. Processing of leucaena leaf- and stemmeal for export to Japan as a protein ingredient;
6. Processing of certain pure and crude compounds from plants for sale to U.S. pharmaceutical and/or the Japanese food processing marketplaces;
7. Processing of fresh strawberries for sale to the Asean and European marketplaces; frozen strawberries to the United States;
8. Processing of frozen vegetables to Japan;
9. Controlled environment aquaculture of shrimp and oysters for export to West Coast of U.S.

3.13 Of the nine, three involve new agricultural production for export; four food processing; three, health; and one, biochemicals. (Two of the proposed Subprojects fall into more than one category). Moreover, four are biotechnologies; (i.e., numbers 1, 4, 5 and 6); the rest are not.

Five of the nine Subprojects were selected for in-depth discussion.

At least three of the five could be implemented in the Northeastern provinces known as the "Golden Triangle".

C. Relevance of USAID Activities to the Company

3.14 To assist the Government of Thailand in meeting its objectives under the Sixth National Plan, USAID has proposed a Rural Industry Development Fund and a Rural Industrialization Assistance Facility designed to achieve several objectives which are synergistic with the objectives of the Company. The USAID objectives under the Rural Industry Development Fund and Rural Industrialization Assistance Facility include:

-a fully-functioning agro-processing institution to promote and assist formation of new agro-processing enterprises (and expansion of existing ones), and to help enterprises deal with incentive and other government-interface aspects of private project formation;

-a network approach to provincial enterprise lending emphasizing longer term loans and involving joint participation of the Industrial Finance Corporation (IFCT) and bank branches of several Thai commercial banks;

-institutionalization of experience in the formulation of agro-processing projects, including solution of production and farmer-supplier relationships at one end, and export marketing of new crops in new markets at the other end; and

-development of new lending methods in participating commercial banks, designed to increase the role of project analysis (as compared with reliance on collateral), in lending to small and medium scale enterprises.

Through placement of a targeted \$60 million of loan funds, the A.I.D. project would facilitate creation of roughly 350 new agro-processing investment projects.

3.15 Moreover, a special allocation under the project will finance policy studies of problems and issues relevant to rural industrial development. It is expected that

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many of the agro-processing loans will finance export-oriented enterprises. At least three subjects relating to export efficiency and competitiveness will be explored under this allocation.

First, the cost of certain intermediate products used by agroprocessing firms vary from country to country. Cans, probably the main example of such inputs, are significantly more costly in Thailand than in Taiwan. Reasons for this are to be explored;

Second, the access of agro-processing firms to export incentives (especially where the incentive system appears to discriminate in practice against the small and medium scale enterprise in favor of the large direct exporter) will be addressed, also;

Third, possibilities for strengthening Thailand's export financing, and increasing its efficiency, are being studied by World Bank analysts from the perspective of assisting manufactured exports generally. The possible special needs and problems of agro-processing will be considered in the context of this work, and may call for additional analysis beyond the scope of the IBRD work.

3.16 Both the objectives of the Rural Industry Development Fund and the Rural Industrialization Facility with their emphases on technology transfer provided to agro-processing entities; institution building, to financial institutions that lend to agro-processing entities; and the policy studies are foci extremely congruent with the business objectives of the Company.

3.17 In addition, USAID has special interests and programs directed at the problems of the Northern provinces.

Opium poppies are grown currently in eleven Northern provinces. Of the estimated 5,000 hectares under cultivation approximately 73% fall within the two provinces of Chiang Mai and Chiang Rai. Production of the poppies in 1984 was estimated at 41.5 tons. Net farm income associated with this production ranges between \$190 to \$1,140 per hectare depending upon current prices. Thailand's opium consumption is estimated at some 35 tons per year.

Opium and its derivatives produced in the "Golden Triangle" are transported in illicit trade routes to all parts of the world and it is the source of between 10 and 15% of the heroin imported into the United States annually. While middlemen and traffickers make handsome profits, the hilltribes who cultivate the opium poppy

live in primitive and impoverished conditions. The roots of their poverty and low standard of living are deep and solutions proposed must address the full range of constraints placed on their self-development.

USAID plans to initiate in FY 1986 a Highland Village Development project to be supported by \$5 million in ESF grant funds. The goal of the project is to reduce the cultivation and use of opium in several contiguous sub-districts in the provinces of Chiang Mai and Chiang Rai. The project's purpose is to overcome the structural conditions of poverty (poor health, illiteracy, low incomes, marginal agricultural productivity) of highland tribes.

3.18 As indicated previously, several of the Company's initial Subprojects could be implemented in the Northern provinces.

3.19 Finally, now in implementation is USAID's Science and Technology for Development Project. This project is a long-term effort being undertaken by the Ministry of Science and Technology, with USAID assistance, aimed at helping Thailand increase its capability to identify, develop and produce scientific knowledge and technology required to resolve problems which hinder its industrial and agricultural development. The project aims, specifically, at fostering and facilitating increasing interaction between Thailand's "science and technology" community (i.e. higher education institutions, and government and private research organizations) and its agricultural/industrial community so that, increasingly, the scientific and technological research, development and engineering (RD&E) efforts undertaken by the former will be focussed on addressing problems facing the latter. The project envisions the provision of substantial assistance to the S&T community in order to enable it to be more responsive to RD&E needs of the agricultural/industrial community. The three principal areas of scientific emphasis of the project are: bioscience/biotechnology, material technology, and applied electronic technology.

A number of windows appear in this project which can support private sector investigations in biotechnology leading, if positive, to commercialization. These windows include:

- o Competitive Research, Development and Engineering program for grants to resolve problems hindering industry profitability; and

- o Company-Directed RD&E program to facilitate the organization's RD&E activities.

The establishment of the venture capital company featuring commercialization of biotechnology in the agroprocessing sector represents "demand-pull" for RD&E activities of the S&T in Development Project. A continuum from research to commercialization is attained.

IV. FINANCIAL PLAN AND PROFITABILITY

A. Project Cost

- 4.01 The Company will be financed at US\$6.0MM, half in Thai equity and half in long term debt from AID/PRE. The debt will be drawn over a three year period from date of establishment of the Company and placed as equity and equity-like investments.
- 4.02 The US\$6.0MM will be placed in some ten subprojects, of which six have been tentatively identified, including:
 - o Leucaena Lecuocephala - High Quality Leafmeal and Stermeal. The concept involves cultivation, harvesting and processing for export of Leucaena Lecuocephoia as a high quality protein ingredient for use in balance animal feed formulas.
 - o Irradiation for Disinfestation and Shelf Life Extension. The concept involves the establishment of an irradiation facility aimed at improving the quality of exportable agro and fishery products by controlling bacteria and pathogens responsible for spoilage and rejection by importers.
 - o Nucleus Estate/Satellite Farming Dedicated to Production of Frozen Vegetables. The product will be frozen vegetables processed and packaged in special containers of standard size for shipment to the institutional and manufacturing marketplaces.
 - o Deodorized Soy Bean Base. The concept involves the elimination of the strong beany flavor from processed soy beans making the product acceptable to Japanese and American tastes.
 - o Aquaculture Shrimp. The concept involves the establishment of life-cycle shrimp farms for salt water shrimp production using proven intensive production technologies.

- o Controlled Environment Farming. The concept involves intensive production of high quality vegetables for export using technology commercialized in Hawaii.

An average of US\$600,000 would be invested in 10 Subprojects accounting for 25% of equity. Total equity mobilization at the Subproject level would be, therefore, US\$24.0MM.

4.03 SOURCES AND APPLICATIONS OF FUNDS, THAI VENTURE CAPITAL LTD FOR FIRST YEAR OF OPERATION

(IN U.S. DOLLARS)

Sources

CORPORATE THAILAND AID	\$3,000,000 EQUITY <u>\$3,000,000 DEBT</u>
TOTAL	\$6,000,000

APPLICATIONS

MANAGEMENT FEE, YEARLY 3% AVAILABLE FOR INVESTMENT	\$180,000 <u>\$5,820,000</u>
TOTAL	\$6,000,000

B. Profitability

4.04 The Company will generate revenues from investment banking fees associated with its project developer role and, more significantly, from capital gains. The fees to be collected from Subprojects by the Company may consist of:

- Origination, 1% of total captitalization
- Documentation, \$25,000
- 4% of equity raised from the Thai joint venture partner
- 2% of debt raised from the Thai banking system
- Trading fees, 2 1/2% on gross sales proceeds
- Work out, as needed and delivered by TVC

4.05 NET EFFECT OF A 25% INVESTMENT BY TVC AND FEES DERIVED

Assume:

- Total Project captialization of US\$5.0MM
- Debt to Equity of 1 : 1

Calculation

1. Equity investment by TVC	\$625,000	
2. Equity investment by Thai J-V Co.	<u>1,975,000</u>	
	Total Equity	2,500,000
3. Total Debt		<u>2,500,000</u>
	Total Capitalization	\$5,000,000
4. Less fees		
- Origination		\$50,000
- Documentation		25,000
- Equity mobilization (4% of 1,975,000)		79,000
- Debt mobilization (2% of 2,500,000)		50,000
- Trading fees		variable
- Work Out fee		<u>variable</u>
	Total fees	\$204,000
	less trading, workout	
5. Net Investment (\$625,000-204,000)		\$421,000

4.06

DISTRIBUTION OF PROFIT WITH ACTIVE STOCK MARKET
(OPTIMUM)

Assume:

- CAPITAL GAIN, 10 TIMES EARNINGS
- EARNINGS TO TVC OF \$3,000,000 FOR ALL SUBPROJECTS DURING YEARS 4,5,6

Total Profit Distributions Years 4,5,6	9,000,000
Total Capital Gains	30,000,000
Total From Fees	<u>1,958,400</u>
Total Profit	40,958,400
Management Fees @ 3% p.a.	1,080,000
Debt Servicing	720,000
Profit Participation	<u>3,000,000</u>
Total Expenses	4,800,000
Net Profit	36,158,400
Repayment Loan	<u>3,000,000</u>
Net Equity	33,158,400

Exit from investments to capture Capital gains will be through those which most likely to yield maximum appreciation. The projections above assume exit through public offerings, of the stock of the subprojects. Exit may also be attempted through public listing of TVC itself which, presumably, would yield 10 times earnings. Alternative exit strategies include private placements and public offerings on the Singapore stock exchange. Costs of registration and placement and perceptions of market acceptance will govern the choice of exit strategy.

V. TRANSACTION SUMMARY

BORROWER: Thia Venture Capital Company Limited, TVC, a wholly Thai-owned corporation.

AMOUNT: \$3.0 million loan.

TERM OF LOAN: 10 years from disbursement

PURPOSE: Provide seed money for the start-up or expansion of small- and medium-sized agribusiness enterprises in Thailand.

GRACE PERIOD: 5 years (60 months) from disbursement on principal only.

INTEREST RATE: 4% per annum interest, compounded annually, will be paid semi-annually in arrears on all outstanding balances.

PRINCIPAL REPAYMENT SCHEDULE: Nine approximately equal semi-annual installments commencing 60 months from disbursement.

USE OF FUNDS: Loan proceeds will be used to capitalize TVC and subsequently for investment in subprojects.

PROFIT PARTICIPATION: AID will receive in assistance fees (profit participation) 20 percent of net profits per annum up to a maximum of US\$3,050,000 payable at the beginning of the following year.

TVC INVESTMENTS--
GENERAL REQUIREMENTS:

(1) TVC investments will be made only in Thailand.

(2) All TVC investments will be principally in agribusiness or biotechnology projects that emphasize employment generation, net foreign exchange generation, and/or forward/backward linkages to other local entrepreneurs.

(3) TVC will invest only in companies having at least 40% local ownership (or higher if prescribed by local law).

(4) TVC's investment in a subproject shall not constitute more than 25% of the total cash capitalization (equity plus term debt) of the subproject.

(5) TVC will exercise due diligence to determine that any subproject in which an investment is made will be in compliance with U.S. laws and regulations concerning licensing of U.S. technology for use overseas.

COLLATERAL:

As collateral for the AID loan, TVC will assign to AID a security interest in all its assets including its investments in subprojects.

CURRENCY OF
REPAYMENT:

All payments of interest, principal, and loan fees will be in U.S. dollars payable, unless otherwise specified in writing, to the U.S. Treasury.

APPLICATION OF
PAYMENTS:

All payments received by the U.S. Treasury (or as otherwise specified) on behalf of AID will be applied to the payment of interest, principal, and payment of loan fee, in that order.

Payments will be deemed made as of the date received by the authorized payment office.

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PREPAYMENT:

At the option of TVC prepayment of part or all of the loan may be made without penalty upon 90 days written notice. Partial prepayments shall be applied to a pro rata reduction of maturities.

Prepayment will be required to the extent significant portfolio sales are made for the purpose of capturing capital gains.

TERMINATION IN FULL:

Upon payment in full of all principal, interest, and loan fees due, all obligations of the Borrower and AID under this agreement will cease.

CONDITIONS PRECEDENT TO DISBURSEMENT:

The AID obligation will terminate on January 1, 1987 unless the conditions precedent to disbursement are met.

(1) Drawdown on the AID loan is contingent TVC or its affiliates raising a minimum equity of \$3 million.

(2) AID approval is required for the selection of the individuals who will serve as managing director and and Chairman of the Board of TVC.

(3) AID reserves the right to review and approve the following documents:

1. Shareholder Agreement
2. Statement of Investment and Operating Policies
3. (Other)

(4) Other normal conditions precedent to each disbursement will be included, e.g., disbursements will not be made if Borrower has undergone a material and adverse change in financial conditions, etc.

GENERAL COVENANTS:

There will be general covenants as to:

1. Program evaluation.
2. Consultation.
3. Execution of the program.
4. Reports, records, inspections and audit.
5. Financial reports of the Borrower.
6. Completeness of information.
7. Other general covenants to be determined.

FINANCIAL COVENANTS:

1. TVC will draw down AID funds for capitalization on the following schedule:

At least \$1,000,000 by, June 1, 1987; \$2 million by June 15, 1988; and \$3 million by June 1, 1989.

2. TVC will not contract any additional debt (including senior debt) from that contemplated in the initial capitalization without the written approval of AID.

3. TVC's audited net worth must at all times exceed \$2 million.

4. Dividend participations and/or preferred share redemptions permitted after year five subject to the condition that all scheduled payments of interest, principal, and loan fees due to AID are current.

5. Any interest earned on the AID loan prior to investment in Subprojects shall be used only to defray operating costs of AVD.

NEGATIVE PLEDGES:

No portion of the total capitalization of TVC will be used, unless AID agrees in writing, to finance enterprises involved in the production, processing, or marketing of sugar, palm oil, cotton or citrus for export; or to finance the procurement, research development, production or distribution of weapons; or to finance the manufacture, importation, distribution or application of pesticides.

SPECIAL COVENANTS FOR INVESTMENTS MADE:

1. TVC will adhere strictly to the Statement of Investment and Operating Policies as amended from time to time and approved by AID.

2. By the beginning of the 60th month, at least \$3.0 million of all investments made by TVC will be joint ventures with U.S. companies or investors.

EVENTS OF DEFAULT ON
THE AID LOAN:

Standard, including but not necessarily limited to the following (applying to both Borrower and Guarantor):

Representation and warranties.

Failure to report to AID in a timely manner any material adverse change in the financial condition of the Borrower.

Material failure in reporting compliance.

Failure to comply with Financial Covenants 2, 3 or 4; or with Special Covenant 1.

Non-payment.

GOVERNING LAW:

The Loan Agreement will be governed by the laws of the District of Columbia of the United States.

VI. CONTRIBUTION TO DEVELOPMENT

A. Impact of PRE Participation on USAID Policy Areas

6.01 The proposed PRE participation would provide a positive impact in four key USAID policy areas: basic human needs, private sector development, institution building and policy dialogue.

6.02 The project addresses basic human needs (BHN) criteria by focusing on growth in the agribusiness sector which will have a positive impact on rural employment.

The project will promote private sector development, by catalyzing a number of new enterprises through the mobilizing of private risk capital, private technology and private management.

The project has as a central element institution building of Thai-owned and supported venture capital. This project is born from close collaboration with commercial banks and with which the new organization and professional investment approach is being developed.

Finally, the project has potential in the area of policy dialogue, in that it meshes well with the USAID Science and Technology in Development Project by filling a gap between R & D and the market.

6.03 Specifically, USAID highlights the following:

* Increasing reliance on the private sector as the determinant of sustained growth and development

The proposed project relies precisely on a private sector delivery mechanism and the disciplines of profit and loss decision making;

* Redirection to agribusiness and rural industrialization

The project focuses precisely on this redirection and can be expected to support mobilization of new technologies by entrepreneurs making investments in the rural sector;

* Biotechnology development in the Thai environment

The project represents an important segment in the continuum between research and the market. It provides system support for commercialization of technology.

* Hardening of concessional terms

The proposed project is priced to produce a yield commensurate with the risks and rewards of venture capital.

- 6.04 The technology venture capital project, in addition to earlier PRE loans, offers tangible case material and a methodology for replication elsewhere. This project adds to previous financial instruments introduced by PRE and will demonstrate its utility for effective, self-sustaining collaboration with the private sector.

B. Relation To The CDSS

- 6.05 The project conforms with the priorities established in the USAID CDSS, particularly as concerns the Mission's goal of developing strategies to expand productive self-sustaining, rural employment. and its focus on technology development.

C. Relation to PRE Objectives and Policies

- 6.06 PRE's objective is to meet the Basic Human Needs mandate of the Foreign Assistance Act of 1961 (revised) using self-sustaining private sector vehicles. In addition, PRE utilizes a variety of operating policies for its Revolving Fund investments to ensure high development and secure financial returns. The AVD project satisfies both. The proposed investment is responsive to the Basic Human Needs mandate by targeting its resources to the agribusiness sector. The rural sector is typically disadvantaged, especially in the area of credit. This project will leverage US\$24.0MM equivalent in equity alone on a self-sustaining basis.

The project also meets PRE guidelines for management of Revolving Fund investments. These are as follows:

- o Has a Demonstration Effect by: a) introducing a new type of financial institution; and b) mobilizing alternatives to public sector, subsidized credit. (see executive summary)
- o Exhibits Financial Viability based on qualified effective demand, proven management, and focused marketing.

- o Targets Development Impacts Appropriate to Thailand by responding to identified constraints on capital expansion and technology transfer in the private sector.
- o Makes Resources Available to the Small-Scale Enterprise Sector by leveraging the PRE/AID facility to create a pool of credit for investment in small-scale agribusinesses.

In addition, the facility meets project-specific financial constraints, namely: a) the facility cannot exceed US\$3,000,000 (the proposed amount is US\$3,000,000); b) the facility cannot be more than 50 percent of project capitalization (the proposed facility would amount to no more than 50 percent; and, c) the facility must be near market interest rates (the yield to AID will be considerably above cost to USG reflecting the risks). The facility will be financed under Section 108 as legislatively permitted.

D. Economic Impacts on the Small-Scale Enterprise Sector

- 6.07 The proposed PRE/AID facility specifically targets the small-scale enterprise sector with a matched pool of funds totaling US\$6.0Mii equivalent. This amount will be made available to provide long-term financing to agribusiness enterprises. This source of capital represents additive credit and, as such, will stimulate incremental investment, sales, and employment.

VII. MONITORING AND EVALUATION

- 7.01 Project monitoring will consist of review of: a) loan and financial performance; and b) adherence to investment guidelines. Both (a) and (b) will be done on a semi-annual basis based on debt service schedules and reporting requirements imposed on the borrower. It is not anticipated that project monitoring will require site visits; this will be left to the evaluation function.
- 7.02 Reporting on the project will consist of annual reporting by borrower of data describing subprojects population by size, product, sales, exports and estimated increased employment as a result of financing.
- 7.03 An evaluation of the project is planned two years after first disbursement. Its objectives will be to determine:
- o Whether venture capital investment in Thailand by private institutions has proved viable;
 - o The effectiveness of the technical assistance provided by AID, if any;
 - o The replicability of this model elsewhere.

IX. PROPOSED TIMETABLE

IOP	10/30/86
IP	1/15/87
L/A Negotiation	1/26/87
Authorization	1/28/87
Obligation	2/28/87
First Disbursement (latest)	June 1, 1987
Last Disbursement (latest)	June 1, 1989

X. DISBURSEMENT SCHEDULE

- 10.01. Per borrower request, disbursement may be made in anticipation of imminent reinvestment in subproject over a three year period from establishment of the Company, targeted by January 31, 1987.
- 10.02 Interest earnings, if any, on the AID loan prior to use for investment in Subprojects will be used to defray operating expenses of the Company only.

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AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON D C 20523

MEMORANDUM

TO: AA/PRE, MS. NEAL PEDEN
SDAA/PRE, MR. CHARLES GLADSON
AA/PRE, MR. DOUGLAS TRUSSELL
AA/PRE, MS. AILEEN KISHABA
PRE/PR, MR. ROBERT BECKMAN
PRE/H, MR. MARIO PITA
PRE/PD, MR. RUSSEL ANDERSON
GC/PRE, MR. MIKE KITAY
PPC/PDPR/IP, MR. NEAL ZANK
ANE/EA, MR. DAVID CAHN
ANE/PD, MR. RICHARD WILLIAMS
MR. DOUGLAS BENNETT

FROM: PRE/I, MR. Sean Walsh 

SUBJECT: IP Review of Thai Venture Capital Limited (Previously called Asean Venture Development Limited), PRE Revolving Fund.

The IP review for a US\$3.0MM loan to Thai Venture Capital Limited from PRE's Revolving Fund is scheduled for Thursday, January 15, 1987 in Ms. Pedens's office, Room 6212 from 11:00 a.m. to 12:00 p.m. Attached is the IP document.