

ASSESSMENT OF ACDI/VOCA PROJECT UNDER FSRP IN KAZAKHSTAN AND KYRGYZSTAN

I. PURPOSE

The purpose of this assessment is: 1) to document and assess activities conducted by ACDI/VOCA under the Food Systems Restructuring Project (FSRP) in Kazakhstan and Kyrgyzstan and 2) to develop recommendations concerning continuation of these activities. The assessment team consisted of Mark Smith, ENI/ED/SB; Peter Thatcher, ENI/ED/AG; Mike Feldtmose, ACDI/VOCA - Washington. The team visited Kazakhstan June 16-19, 1998, to conduct the field assessment portion of this report.

The current estimated completion date of the project is September 30, 1998. Of the \$5,000,000 authorized under the FSRP Cooperative Agreement, the current obligated amount is \$3,460,000. As of June 30, 1998, the project has just under \$300,000 remaining for current subgrants as well as management and administration.

II. BACKGROUND

Private businesses in the Central Asian Republics (CAR), especially those in food processing and agriculture, are currently confronted with extremely tight credit conditions, stringent financial constraints, and an acute lack of technical, managerial and marketing skills to operate enterprises effectively.

Moreover, the need for agricultural modernization is extremely urgent in the region. For example, in Kazakhstan, with 38 million hectares of productive agricultural land, **35%** of the gross national product is derived from agriculture and **40%** of the population is employed in the agriculture sector. Indeed, the future of the country will be strongly influenced by the viability of its rural economy.

The FSRP was designed to identify suitable investment opportunities and promote partnerships between local and U.S. enterprises. FSRP's role is: 1) to help interested U.S. agribusinesses to develop investment opportunities, 2) to support the development of the required business plans necessary to obtain project specific funding, and 3) to provide matching funds for technology transfer as investment incentives once a deal is made. The basis of this program was to use and facilitate private U.S. agribusiness interests in stimulating capital flow, the transfer of U.S. technology and managerial skills, and the demonstration of viable alternatives to the former, state-controlled systems.

Over the last four years, the FSRP has assisted Central Asian enterprises by facilitating business relationships with U.S. firms interested in pursuing joint venture opportunities. The goal of the project is to improve the Central Asia's food processing industry through technology transfer, technical assistance, trade and investment - - in short, getting U.S. firms to invest in one of the riskiest, little-known markets of the former Soviet Union in order to increase private sector ownership and SME sustainability.

FSRP provides two types of subgrants to U.S. companies pursuing joint venture investments in Central Asia. The first type is the Business Development subgrant. These subgrants assist both the U.S. and Central Asian partners with the up-front activities that are crucial to a successful joint venture. This includes feasibility studies, business plans, and marketing assistance as well as assistance identifying appropriate sources of financing. The second type of subgrant is the Joint Venture Training subgrant. These subgrants are used for management, marketing and operational training as well as technology transfers. Joint Venture Training subgrants are based on the equity contribution of the participating U.S. companies. The formula generally followed is that for every \$2.5 dollars U.S. companies provide in equity to the venture, they are eligible to apply for \$1 in Joint Venture Training subgrant funds.

III. USAID/CAR MISSION'S STRATEGIC OBJECTIVES

USAID/CAR strategic assistance areas are: 1) market transition, 2) democratic transition and 3) social transition. Each strategic assistance area is further divided into Strategic Objectives (SOs). The ACDI/VOCA activity in Kazakhstan and Kyrgyzstan addresses the market transition strategic area and within this area the SO dealing with "improved, more sustainable private business operations" in the agribusiness sector.

IV. PROGRESS

Over the last four years FSRP has continuously evolved, adopting best practices and lessons-learned in order to increase the number of joint venture activities and assist local agribusinesses in attracting outside investment to increase efficiencies, productivity and ultimately profits. To date the project has achieved the following results.

A. Joint Ventures

- A \$5 million Dairy Processing Joint Venture that is now valued at over \$10 million and has a 45% share of the Almaty market.

- A \$3 million Meat Processing Joint Venture that is supplying Kazakhstan's new capital city with high quality, western-style meat products.
- A \$1 million Walnut Processing and Packaging Joint Venture in the economically depressed region of Jalal-Abad, Kyrgyzstan.
- A Beverage Processing and Bottling Joint Venture in Bishkek, Kyrgyzstan valued at over \$4 million. This agreement is with Kyrgyz-American Inc. of Augusta, GA and Dasmiya Company in Bishkek, Kyrgyzstan.
- An Agricultural Equipment Leasing and Maintenance Joint Venture in Western Kazakhstan between AppTech International of Des Moines, IA and Investment Industrial Corporation of Almaty, Kazakhstan.

A sixth new joint venture is expected to be completed in September 1998. This will be a Potato Chip Processing and Packaging Joint Venture with an estimated value of \$3 million. DTR, Inc., the U.S. partner, has recently purchased the equipment for this joint venture and expects it to be in full operation by October 1998.

B. Future Business Development and Technical Assistance

- Currently, FSRP is working with 7 Kazakhstani private agribusinesses and U.S. firms on prospective joint venture projects. The following is a list of the prospective joint ventures:

- Meat Processing Plant
- Dairy Collection Facility
- Poultry Processing Plant (2)
- Fast Food Restaurant Chain
- Brewery
- Cold Warehouse Facility
- Apple Juice Concentrate Plant

- In total, the FSRP Joint Ventures hired over 400 employees, 60% of whom are women.
- Privatized 15 agricultural production cooperatives in Kazakhstan.
- Implemented over 25 transfers of technology in food processing, packaging, and labeling (e.g., dairy packaging lines from the U.S. and meat processing equipment and processes).

- Provided over 30 technical assistance interventions focusing on improving management, marketing and finance and accounting systems.
- Designed a privatization plan for Kazakhstan agricultural production cooperatives and assisted the government in drafting a Western-style cooperative law.

C. Achievement of Results

The project has achieved the above results by:

- Providing U.S. and Central Asian companies much needed technical and logistical support in all stages of business development.
- Highly leveraging subgrant funds by requiring participating companies to cost-share at least 20% of all subgrant money received.
- Concentrating on small to medium-sized joint venture projects that have rapid implementation schedules and build on success.
- Keeping project administrative and management costs at a bare minimum in order to increase subgrant assistance funds.

D. Evolution of the ACDI/VOCA FSRP Model

Until recently, Central Asia's economy has been in extreme flux. Since 1990, the region's economic output has declined by over 40%, unemployment reached as high as 35%, and the political landscape has been in constant change. In order to entice U.S. investment to this challenging environment ACDI/VOCA implemented a two-prong approach under FSRP. First, a comprehensive subsector analysis of the food processing industry was made, including an assessment of the types of related companies. As a result, strong, marketable firms were identified as potential investment partners with U.S. firms, and company profiles were then created and marketed to ACDI/VOCA's network of U.S. cooperative members and affiliated agribusinesses. Second, to complement the first effort, selected companies from ACDI/VOCA's extensive network were brought to Central Asia to validate the subsector assessments and to explore investment opportunities.

Once the U.S. companies committed to an investment project, FSRP would facilitate all necessary steps from local partner identification, business plan creation, negotiations, and financing. Targeted technical assistance to all parties in the investment process is an integral part of FSRP's success. FSRP staff in the field is well acquainted with all aspects of

investment regulations, policies and privatization. In effect, FSRP was functioning as a specialized "business support center."

Initially, FSRP concentrated on large-scale investment projects that would immediately capture a significant market share. These were usually fully integrated investment projects that ranged from production to processing, distribution and retail. These projects required a high-degree of management, resources, time and investment. With a nascent region such as Central Asia, these ambitious projects were premature. For example, in 1994 Koch Supplies, Inc. of Kansas City, MO identified a dairy investment opportunity in Kazakhstan. With only several minor processors supplying the market, Koch worked with FSRP to create a dairy modernization project that would immediately supply 60% of the market's dairy products. Financing for this venture was never realized because the project appeared too large for the overall market. Although investors such as the IFC and the Central Asian-American Enterprise Fund (CAAEF) believed the project to have merit and potentially high returns, they were not convinced that the market could handle an increase in supply at such a rapid pace. Consumers were simply not ready to pay high premiums for milk products.

In 1995, FSRP began concentrating on smaller, more manageable investment projects. ACDI/VOCA learned that the more successful investment projects were those that began on a modest level and focused on targeted or niche markets. Projects that had clearly defined marketing plans that met specific demand were more likely to succeed. With this evolving model, FSRP has had a more positive impact.

The latest joint ventures under the project typify the ACDI/VOCA model and approach to agribusiness linkages and joint venture creation. Companies must first examine the market's potential, structure operations relative to the market's size and adopt an incremental growth strategy. With this approach, FSRP has had outstanding development success in increasing employment, bringing healthy, high quality products to market and strengthening and enhancing SMEs by improving marketing, financial and entrepreneurial business skills. Currently, the project is assisting over ten Central Asian private businesses to create joint ventures with U.S. companies.

V. SITE VISITS

Six site visits took place June 16 - 19, 1998, in the Almaty region, and one day in Astana. Two prospective sub-grantees were also interviewed in Almaty, as well as several staffers of the Central Asian - American Enterprise Fund.

A. FoodMaster Dairy JV, Issyk, Almaty region: DTR originally bought into this project by leasing space in a dairy. DTR, a

Minneapolis company, is the subgrantee, having received \$60,035 of USAID funds under FSRP for equipment and training. When the dairy went into receivership, DTR bought the whole facility. With additional equity from a U.S. venture capital fund, they formed a new corporation called FoodMaster International, and have expanded operations to Astana, the new capital 1300 km north of Almaty. Their experience in Kazakhstan, which was aided by technical assistance provided through FSRP subgrants, has encouraged DTR/FoodMaster to expand its dairy operations in Moldova and the Ukraine. In Kazakhstan, FoodMaster claims to have 50% of the market for yogurt, kefir, sour cream, and a good share of the ice cream market.

B. "Yrys" meat processing plant, Astana: a joint venture of Koch Supplies, Inc., of Kansas City, MO, the Central Asian - American Enterprise Fund, and Tsesna, a Kazakh corporation. To date, the Koch JV has received \$217,575 of FSRP subgrants for technical assistance for training in marketing, accounting, and equipment installation. Koch has received an additional \$50,000 to assist in replicating this successful project in southern Kazakhstan. Reportedly, "Yrys" is already profitable. They slaughter, process, package, and market sausages and meat cuts. The products are attractive, and up to Western standards in appearance and taste.

C. FoodMaster dairy: visited Astana branch. This is a branch of the first FoodMaster dairy project, which effectively doubles the capacity and production of the original plant. ACDI/VOCA was instrumental in the success of this replicable project, which, given the experience and confidence level resulting from now two successful endeavors, means the concept can be expanded even further to other CAR locales.

D. Alexander's Nuts/Pardue Associates: Mr. Chuck Pardue reviewed the operation in the ACDI-VOCA offices. He was plainly very grateful for the assistance given by ACDI/VOCA, both on the ground in Jalalabad, Kyrgyzstan, and in Almaty. This project is of particular interest because it brings together a small American entrepreneur with Kyrgyz partners in an extremely remote environment, and developed a project that brings modern processing and marketing to a neglected CAR region. Seasonally, the project employs up to 150 women who harvest and process walnuts. Mr. Pardue is so pleased with his first project, that he is now undertaking the feasibility of additional projects in Kyrgyzstan.

E. DTR Potato Chip Project, Almaty: DTR received a subgrant of \$23,000 to perform a feasibility study of the snack food manufacturing and market potential in Kazakhstan. They have already leased and optioned a state-owned potato storage and processing facility, and plan to proceed with the venture. The premises are old, but solid and weatherproof, with adequate

water, sewer and electric power on hand. When launched they will compete with imported snack foods. DTR imported two containers of seed potatoes, which are currently growing, and anticipate a September - October harvest of their first crop. Given DTR's success with FoodMaster, their chance for success is good, assuming they can source an adequate supply of quality potatoes.

F. Abacus Group, Inc.: an American company exploring the possibility of building a cold storage food and distribution facility in Almaty. The principals are experienced at marketing in the former Soviet Union, having been chief financial officer of Quality Foods, a Little Rock company that sells frozen chicken and other foodstuffs in Russia.

G. Realma: toured a facility at which Pierce Street Ventures, a California company, is considering a brewery project (15,000 bottles/day capacity). Realma, the joint venture company, currently bottles and sells vodka and wine.

VI. ADDRESSING USAID/CAR SOs

As documented above, the ACDI/VOCA activity in Kazakhstan and Kyrgyzstan addresses USAID/CAR market transition strategic area and the SO dealing with "improved, more sustainable private business operations." Thus, not only does the activity directly address one of the Mission key SOs but it does so in a sector - agribusiness - that desperately needs assistance and is, in fact, receiving very little.

VII. LESSONS LEARNED

There are a number of lessons learned in the development of this activity. **First**, the gestation period to develop a joint venture in this part of the world is considerably longer than anticipated. One has to be patient and take the long view. In this regard, the activity has now gone through the learning curve phase and is prepared to move substantially quicker in the development of a next generation of joint venture activities. **Second**, given the uncertain business climate, tight credit, lack of appropriate technology and remoteness of the location, the funds provided by the project to support the early investigative stages of the joint venture process served a very important, even essential role, to attract investors, particularly from the U.S. **Third**, "keep it simple" definitely applies when working the CAR. Focus on one or two activities (i.e., a dairy processing plant) and not an entire sector (i.e., dairy farm, transportation, marketing, etc.) and the chances of success are dramatically increased. **Fourth**, the infusion of a small amount of funds for technical assistance (e.g., Western style accounting system) can dramatically increase the appeal of the activity to U.S. investors.

VIII. ASSESSMENT OF PROGRESS

The activity has been operational for nearly four years. During this period ACDI/VOCA has developed a workable model that has produced five sustainable joint ventures and currently has seven more in process. Of the five joint ventures three (i.e., the dairy joint venture, the meat processing joint venture and the walnut processing and packaging joint venture discussed on pages 2 and 3) are totally operational and should be considered successful and financially sustainable. The dairy processing joint venture has been replicated in the new capital city of Astana. Two joint ventures (i.e., the beverage processing and bottling joint venture and the agricultural equipment leasing and maintenance joint venture discussed on page 3) were initiated in June 1998 and therefore it would be premature to assess their prospects. While these accomplishments may seem modest, they are very significant given the difficult local investment environment and the remoteness of the location.

Also of importance is that the model developed by ACDI/VOCA is highly leveraged. As summarized below, a comparatively small amount of USAID funds has leveraged a large amount of joint venture and investment resources.

Number of Joint Ventures:	5
Total Grant Funds Disbursed:	\$353,500
In-Kind Contributions:	\$202,000
Total Investment (Equity) Value:	\$12,450,000

Also, as shown below, when considering all project activities, it has been very efficient in the use of a comparatively small amount of USAID funds.

ACDI/VOCA Overhead:	\$634,311
Technical Assistance to Kazakhstan/U.S. Co.:	\$1,733,089
Subgrant Funds for Joint Ventures:	\$1,038,600
Total:	\$3,406,000

Thus, on balance, the project is doing very well and continues to attract and assist investors. The quality of personnel, both local and support in Washington, is high. The experience of the contractor, ACDI-VOCA, in accomplishing these tasks is considerable.

IX. RECOMMENDATIONS

The FSRP has played a significant role in the development of sustainable and profitable agribusiness joint ventures in Kazakhstan and Kyrgyzstan. While the number of these joint ventures to date is modest, very valuable experience has been gained by ACDI/VOCA during this process. They have developed a workable model that can now be used to initiate future joint ventures. They also have a significant pipeline of interested investors in the U.S. and Kazakhstan and Kyrgyzstan that would like to explore joint venture opportunities. The ACDI/VOCA activity directly addresses one of the USAID/CAR SOs, "improved, more sustainable private business operations." The activity's PACD is September 30, 1998.

Accordingly, ENI/ED/AG recommends that: 1) the activity be extended for six months and \$200,000 be added to the project to support operations until February 1999 and 2) during this period the USAID/CAR Mission consider providing sufficient funding to extend the activity for an additional two years. This period of time will provide the current pipeline of interested investors sufficient time to consummate potential joint venture activities. If further funds can not be provided by the Mission, the six month period would be used to close out ongoing activities.