

MICROENTERPRISE STOCK-TAKING:
THE DOMINICAN REPUBLIC

A.I.D. EVALUATION OCCASIONAL PAPER NO. 24

by

Jeffrey Poyo, Team Leader
(Robert R. Nathan Associates, Inc.)

David Hoelscher
(Agency for International Development)

Mohini Malhotra
(Robert R. Nathan Associates, Inc.)

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FOREWORD

During 1988 and 1989, A.l.D. undertook a major stock-taking of its experience in microenterprise development. The stock-taking examined differing approaches and techniques that have been used in efforts to assist microenterprises, including alternative institutional delivery mechanisms. The study was designed to identify the patterns of A.l.D. project interventions that generate success, with the goal of establishing which were the most successful programs, institutions, and delivery techniques. It required an examination of the different types of microenterprises and of the way their problems differ, and an analysis of A.l.D. project approaches, to see which work best under which conditions.

The stock-taking included a conceptual overview paper of published evaluations that identified many factors that are important to project success. It also developed a conceptual framework for analyzing the types of problems microentrepreneurs face.

The stock-taking included field assessments of A.l.D. microenterprise assistance projects in 10 countries. These assessments provided an excellent opportunity to examine in a systematic, consistent manner a large number of project approaches operating under a variety of economic conditions.

The final part of the stock-taking was a synthesis, which pulled together the findings of the conceptual overview paper and the field assessments to develop lessons learned and recommendations for microenterprise assistance programs.

The Dominican Republic was one of the 10 countries examined in the field assessments, and the assessment focused on ADEMI and PROAPE/FONDESA. This assessment provides interesting insights on one approach to promoting microenterprise development. We think that those who are working on microenterprise programs in Washington and in the field will be able to draw on the findings of this report to help in the planning, implementation, and evaluation of other microenterprise programs.

Janet Ballantyne
Associate Assistant Administrator
Center for Development Information and Evaluation
Agency for International Development
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PREFACE

Two microenterprise projects, implemented by ADEMI and PROAPE/FONDESA with financial support from the A.I.D. Mission in the Dominican Republic were assessed by a three person team over a three week period in November 1988.

The team wishes to thank Anne Beasley, Robert Asselin, and Kenneth Lanza of the Private Sector Office of the A.I.D. Mission, Pedro Jimenez and the staff of ADEMI, and Maria Cuevas and the staff of PROAPE/FONDESA for their assistance cooperation, insights, and time.

SUMMARY

The Dominican Republic is one of the poorest and most densely populated countries in the Western Hemisphere. Its burgeoning urban population requires productive employment, and A.I.D. has sought to create this employment by promoting micro and small enterprise. It has done this both through policy dialogue and support to intermediary institutions.

The stock-taking team assessed the microenterprise programs of two intermediary institutions; the Asociacion Para el Desarrollo de Microempresas, Inc. (ADEMI), and the ProBrama de Asistencia a la Pequena Empresa/Fondo para el Desarrollo (PROAPE/FONDESA). ADEMI provides credit to microenterprises and occasional technical assistance to resolve specific difficulties faced by its clients. PROAPE/FONDESA concentrates on providing training and technical assistance prior to extending credit both to microenterprises and larger firms.

ADEMI is a non-profit organization centered in Santo Domingo the capital, but now operates throughout the country. The original ADEMI program consisted of two components: the microenterprise portion, which targeted enterprises with six or less employees and the solidarity component, which lent to groups of five to eight members and used a group guarantee mechanism to ensure loan repayment. In 1984, ADEMI began to phase-out its solidarity group component, and in 1987, decided to concentrate all of its resources on individual microenterprises.

ADEMI presently targets microenterprises, which it defines as businesses that have been operating for at least one year, with six or fewer employees, and less than \$1,592 in fixed assets. Loan amounts and terms are escalated for repeat borrowers, on the basis of their repayment and growth records. At the time of the initial loan, the average size of fixed assets of microenterprises is less than \$1,000, and the average number of employees is three. From its inception in 1983 until September 1988, ADEMI extended a total of 19,428 loans. Technical assistance offered by ADEMI is demand driven, and is not a prerequisite for obtaining a loan. Beneficiaries contact loan officers as problems arise.

PROAPE and FONDESA are two separate divisions within the Asociacion para el Desarrollo, Inc. (APEDI) which is a local development foundation in Santiago, the Dominican Republic's second largest city. PROAPE provides managerial training and subsequently conducts feasibility studies for microenterprises. The enterprises are then referred to FONDESA or to financial institutions which participate in the A.I.D. and government sponsored Fondo de Inversiones para el Desarrollo Economico (FIIDE)'s Small Industry Development program, depending on the size of the loan requested.

PROAPE/FONDESA's microenterprise program targets businesses

with sales less than \$11,943 per year, net worth less than \$7,165, and investment per job created not larger than \$1,433. The small enterprise program targets enterprises with fixed capital not exceeding \$31,847, and investment per job created not greater than \$1,592. In order to reach the poorest people in the country, PROAPE also targets solidarity groups, usually made up of five members conducting similar economic activities.

PROAPE/FONDESA reported that as of October 1987 it had identified 1186 enterprises for assistance. By October 1988, it had given 116 courses in various aspects of management to 1562 participants, and had extended loans to 583 small-and microenterprises. It had assisted 332 solidarity groups with 1,641 members and facilitated loans of \$108,914.

The average size of the initial loan made under the PROAPE/FONDESA program to individuals is \$796, while that to solidarity group members is \$398. PROAPE/FONDESA's training program is a prerequisite to receiving a loan. PROAPE/FONDESA requires program beneficiaries to take standard core courses in accounting and cost analysis, and perhaps up to seven additional courses, in labor law, industrial security, marketing, production, internal control, and personnel administration prior to qualifying for a loan.

Factors influencing project performance and impact include:

- (1) ADEMI benefits from clear and realistic objectives and the institutional autonomy to achieve and monitor those objectives. PROAPE/FONDESA is constrained by the social welfare orientation of APEDI, its sponsor, which is in conflict with its business development thrust. Further, its dependence on FIDE, which has been slow and inefficient, undermines its own efficiency. The lack of independence and confusion in goals has handicapped PROAPE/FONDESA.
- (2) ADEMI's decentralized organization structure, operational flexibility, qualified personnel and sophisticated management information system are factors which contribute to its operational efficiency.
- (3) The separation of technical assistance and credit functions in ADEMI helped maintain and monitor the attainment of its goals. Their linkage in PROAPE/FONDESA makes it impossible to assess the impact and costs of either.
- (4) ADEMI now covers its operating costs and has capitalized its loan portfolio by charging positive real interest rates. However, these relatively high rates may lead to problems with loan recovery, or reduce demand for credit,

and the loan portfolio should be monitored carefully to detect borrower distress. PROAPE/FONDESA's negative real interest rates are decapitalizing its portfolio.

- (5) ADEMI's program has had some differential impact on employment and perhaps production by its clients. Employment generation, labor productivity, and income generating effects were higher for larger manufacturing firms, which dictated ADEMI's decision to continue to serve those firms, and move away from the very small groups which had been involved with its solidarity group lending. No data were available on PROAPE/FONDESA impact on clients.
- (6) Graduation of clients to formal sector financial institutions was not feasible despite the growth and prosperity some achieved. Graduating one's best clients would decrease the financial viability of a project.
- (7) The team considers that several years of support for groups like ADEMI is justified in terms of the client benefits reported.
- (8) Government demand management and regulation were the most important factors in explaining microenterprise success and should continue to be addressed through policy dialogue.

The **lessons learned** from the ADEMI and PROAPE/FONDESA:

- (1) Clear institutional objectives and the autonomy to pursue them leads to improved project performance. Credit and technical assistance activities have different goals and objectives, and need to be measured and evaluated as such.
- (2) Microenterprise projects should incorporate project design elements to ensure equal access to project resources by women, especially by targeting the type of enterprises they serve.
- (3) Financial intermediation can be self-sustaining if they charge positive real interest rates, and have decentralized organizational structure, flexibility, well trained personnel and sophisticated management.
- (4) Graduation of microenterprises to formal sector credit institutions is based on unrealistic assumptions. Institutional graduation is a more realistic goal. ADEMI was able to borrow from banks to on-lend funds to microentrepreneurs.

GLOSSARY

ADEMI	Asociacion para el Desarrollo de Microempresas, Inc.
APEDI	Asociacion para el Desarrollo, Inc.
A.l.D.	Agency for International Development
ATI	Appropriate Technology International
FIDE	Fondo de Inversiones para el Desarrollo Economico
FONDESA	Fondo para el Desarrollo
GTZ	German Development Agency
IDB	Inter-American Development Bank
PROAPE	Programa de Asistencia a la Pequena Empresa
STP	Secretariado Tecnico de la Presidencia
TAC	Technical Assistance Center

1. COUNTRY SETTING

The Dominican Republic has a total area of 48,400 square kilometers and occupies the eastern half of the island of Hispaniola. With an estimated population of 6.7 million in 1987, the country is the most densely populated in the western hemisphere. While population growth has slowed in recent years, from an annual average of 3.6 percent in the 1960s to 2.5 percent in the 1970s, 41 percent of the population is under 15 and the percentage of women of child-bearing age is rising. Growth of the urban population has been explosive. It increased at an annual average rate of 5.3 percent during the twenty years ending in 1980 as compared with a rural population growth of under one percent over the same period. The rapid urbanization of the country reflects the combined impact of an income loss in the rural sector arising from a deterioration of the country's terms of trade, and governmental import substitution policies, which sharply increased the number of available jobs in urban centers. However, urban unemployment remains high, and job creation is still a priority for the country.

For thirty years prior to 1961, the political situation in the Dominican Republic was dominated by General Rafael Trujillo. Trujillo controlled all political institutions and most sources of economic growth. Reflecting rapid increases in the international prices of the Dominican Republic's principal export commodities, economic growth was rapid during the Trujillo regime. However, internal pressures resulting from the inequitable distribution of the benefits of such growth came to a head in 1961 with the assassination of Trujillo, and the beginning of a five year period of intense civil unrest. The political disruptions and resulting economic deterioration were brought under control in 1966 when Joaquin Balaguer was elected president of the Republic in a free election. Since that time, the Dominican Republic has had a stable political situation and peaceful transitions of power following the end of each presidential term.

The Dominican Republic, with an estimated per capita income of \$710 in 1986, is the third poorest country in the western hemisphere. The economy is highly dependent on sugar and mineral exports. Reflecting sharp improvements in the country's terms of trade, income per capita grew at an average rate of about seven percent during the 1970s. However, as world commodity prices deteriorated between 1979 and 1985, income growth slowed to one percent. The Government of the Dominican Republic has sought to diversify the economy by stimulating tourism and non-traditional exports. Although important progress has been achieved, the impact of the government initiatives has been limited by the relatively small economic base from which such activities started.

In 1985, the government sought to reverse the continuing deterioration of the economy with the adoption of a comprehensive

adjustment program including a sharp depreciation of the Dominican currency, measures to strengthen tax collections and adjustments in the price control system, including raising the price of gasoline. The impact of the program was enhanced by improvement in the balance of payments arising from increased tourism receipts and debt relief. The initial results of the program were quite positive. Domestic inflation, which had risen to 38.1 percent over the twelve-month period ended December 1984, fell to 28.4 percent in 1985, and then fell further to 6.5 percent in 1986. At the same time, economic growth accelerated from -3.6 percent in 1985 to 3.2 percent in 1986. Following presidential elections in 1986, the government began a large public works program aimed at continuing economic growth and reducing unemployment. The expansionary policies accelerated economic growth to over 8 percent in 1987, but inflation increased to 25 percent, and the balance of payments deteriorated, after having improved during the previous four years. The net international reserves of the Central Bank also fell sharply. In 1988, the expansion of economic activity has moderated, although demand pressures remain high and inflationary pressures have intensified.

Although recent economic policies have led to an acceleration of economic growth, income distribution remains skewed. According to a 1984 population survey, the poorest 60 percent of the population receives only 28 percent of total income. Furthermore, it is estimated that the deterioration in economic conditions during the 1980s made income distribution even more unequal. The incidence of absolute poverty is significantly higher in the urban centers off Santo Domingo and Santiago. As rapid migration continues into the urban centers, both unemployment and poverty levels are expected to steadily increase.

During the period 1970-1985, the relative share of both agriculture and manufacturing in total national income fell as construction and mining activities increased at a relatively fast pace. This shift in economic activities reflected the exhaustion of import-substitution industrialization policies followed by the government during the 1970s and the impact of the long-run deterioration in the terms of trade. Reflecting this trend, employment in agriculture and manufacturing fell from 65 percent to 40 percent of total employment between 1970 and 1987, while employment in construction and service industries increased accordingly.

Although the financial system of the Dominican Republic is highly diversified, complex controls imposed by the government have limited the system's ability to mobilize domestic savings and meet the financial needs of the private sector. Interest rates are controlled and have been negative in real terms during much of the 1980s. The government further restricted flexibility by imposing complex portfolio composition requirements aimed at directing credit to priority sectors. Over the same period, the uncertain

economic situation resulted in substantial capital flight. As a result, commercial banks experienced increasing domestic arrears and severe liquidity constraints.

The private sector in the Dominican Republic plays an important role in economic activity. As a result of the import-substitution strategy followed throughout most of the 1970s, the private sector extended itself into virtually all sectors of the economy. Throughout the 1980s, the private sector employed about 85 percent of the economically active population, and private sector investment accounted for over 80 percent of gross domestic investment. Public enterprises, on the other hand, are active only in a few key sectors such as mining and electricity generation.

Government policy towards the private sector is mixed. Although few direct controls are imposed and the role of public enterprises is limited, the macroeconomic policy adopted by the government limits the ability of the private sector to operate efficiently. However, the government has followed expansionary policies and adopted an unstable foreign exchange rate policy which has hampered private sector development. At the same time, these policies have reduced the ability of the banking system to finance private sector activities.

2. DESCRIPTION OF A.I.D. PROJECT ACTIVITIES IN SUPPORT OF MICROENTERPRISE

Even though microenterprise development in the Dominican Republic is a major focus of A.I.D.'s interest, as specified in its various strategy documents, U.S. dollar Development Assistance funds have not been used in recent years to support this interest. A.I.D.'s small and microenterprise support has been provided through the use of local currency funds and policy dialogue. The dollar and local currency assistance and policy dialogue are all related in that the local currency funds are created as counterparts to Economic Support Fund (ESF) balance of payments support that the U.S. extends in dollars, and the influence in policy dialogue is underwritten by the dependence of the government on these and other U.S. foreign assistance.

The use of local currency funds, generated by sales of PL-480 Title I commodities, shifted in mid-1984 from providing assistance to small farmers through the Secretariat of State of Agriculture, to direct support of both microenterprise and small-scale industries. Programs were developed with a variety of local organizations, such as ADEMI (Asociacion para el Desarrollo de Microempresas, Inc) and PROAPE/FONDESA (Programa de Asistencia a la Pequena Empresa/Fondo para el Desarrollo), the two studied in this report, that provide both credit and technical assistance to microenterprises. The emphasis of the A.I.D. program was further refined after 1984 as relatively more emphasis in program lending was given to microenterprises. Total financial support for these

organizations was S2,244,900 in FY 1988.

Earlier support through both U.S. and local currency had been extended to a variety of microenterprise promotional institutions. In addition, Central A.I.D. funds have been used for a number of years to support such institutions. For example, the Dominican Development Foundation received central support through ACCION/AITEC for its Program for the Development of Microenterprises (PRODEME), as part of the PISCES II Project sponsored by A.I.D. under the supervision of the Bureau for Science and Technology. Under this program, loans were extended to microenterprises, both individually and in solidarity groups, and courses provided for them. Despite problems with inefficiencies in disbursement and difficulties with repayment the project was generally considered to be a success. The ADEMI project described in this report emerged from the PRODEME experience. Several U.S. PVOs have and are conducting microenterprise promotion activities on the basis of Matching Grant support from the A.I.D. FVA/PVO office, such as Women's World Banking (ADOPEM). These efforts and similar ones may be supported in a more organized manner under a new PVO co-financing arrangement which A.I.D. has under consideration.

On-going policy dialogue is conducted with the government in conjunction with the Economic Support Fund and PL-480. Efforts are being made to ensure that an appropriate macroeconomic framework is adopted by the government, and that government policies and activities that inhibit the performance of the private sector are revised.

A.I.D.'s U.S. currency funded private sector activity has included a Small Industry Development project, directed through FIDE (Fondo de Inversiones para el Desarrollo Economico), which is a "window" within the Central Bank, to assist predominantly small, but also microenterprises. Following a "pyramid strategy," credit to the enterprises was to come through a refinanced line of credit from banks, and technical assistance was to be provided by independent Technical Assistance Centers (TAC) which are sponsored by local development foundations. Five TACs have been organized and are in operation, including one in PROAPE, an organization covered in this report. The results of the FIDE program have been deemed unsatisfactory, inter alia, because of the inefficiencies of the FIDE organization. The entire plan is undergoing reconsideration and redesign.

2.1 Other Private Sector and Donor Support of Microenterprise

A.I.D.'s private sector strategy has been formulated in concert with all principal bilateral and multilateral donors. Both the German Development Agency (GTZ) and the Inter-American Development Bank (IDB) have provided financing for a broad range of local agencies supporting microenterprises, including ADEMI and

PROAPE/FONDESA's parent development foundation. The terms of such support, however, differs considerably from those for A.I.D. funding. Whereas A.I.D. has provided mostly grants, and insists that funds be lent at market rates, both the Germans and the Inter-American Development Bank have provided loans at concessional rates and terms. GTZ in particular has been supportive of low interest rates charged by its borrowers. This may soon change because the headquarters of GTZ is as committed to market level interest rates as A.I.D. In the interim, however, the fact that roughly similar programs, operating in the same financial markets are supported by various donors, has occasionally undermined A.I.D.'s ability to impose financial discipline on the institutions it supports.

3. FINDINGS AND ANALYSIS

3.1 Project Descriptions

3.1.1 ADEMI

The stock-taking team assessed two institutions in the Dominican Republic: ADEMI and PROAPE/FONDESA. ADEMI emphasizes the provision of credit to microenterprises and occasional technical assistance to resolve specific difficulties faced by its clients. PROAPE/FONDESA concentrates on providing training and technical assistance prior to extending credit both to microenterprises and larger firms.

ADEMI is primarily a financial intermediary, providing short-term working capital and some fixed-asset loans to microentrepreneurs. It is a private nonprofit organization, founded in February 1983 with financial support from Dominican private and public sector leaders, and technical assistance from ACCION/AITEC. ADEMI has received extensive A.I.D. local currency support in the form of loans from the government. Other funds have come from the GTZ, the Inter-American Development Bank and local funders. ADEMI was founded by several individuals who had been associated with the Dominican Development Foundation and its PRODEME program, and had wanted to move beyond its group lending approach to pursue some of the ideas they had been developing with ACCION/AITEC. ADEMI's principle objectives are to 1) increase the income of Dominican microentrepreneurs, 2) create new employment, and 3) strengthen existing jobs within the informal sector.

ACCION/AITEC is an independent non-profit organization with business development programs which aim to create employment opportunities and a better quality of life for low-income families in the Americas. Headquartered in Cambridge, Massachusetts, it assists more than 30 local organizations like ADEMI in Latin America, with technical advice and financial support.

ADEMI's and ACCION/AITEC's original project consisted of two

components: the microenterprise portion, which targeted sole proprietors or enterprises with six or less employees, and the solidarity component, which lent to self-organized groups of five to eight members, and used a group guarantee mechanism to ensure loan repayment. While both components had the objective of increasing income and employment, the solidarity group had the additional objective of increasing 'empowerment': the ability of its members to wield influence on their political and social environment.

In 1984, ADEMI began to phase-out its solidarity group component, and in 1987, decided to concentrate all of its resources on individual microenterprises. Given its limited resources, ADEMI believed that it could have a wider and more sustainable impact on somewhat larger microenterprises than solidarity groups. ADEMI's own surveys showed that the individual enterprises had a higher income and employment generation capacities. Service costs for microenterprises were projected to be lower. For ADEMI, given its initial limited institutional endowments, the promotion of individual and somewhat larger enterprises, rather than the smaller enterprises involved in solidarity groups was a more cost-effective way of achieving its objectives. In addition, several other microenterprise credit programs were already serving the very small enterprises through solidarity group mechanisms.

ADEMI has expanded from a pilot project operating in Santo Domingo in 1983 to a nationwide program with 20 offices dispersed throughout the country. This expansion has been matched by an increase in both its administrative staff and its field advisors. Its staff has increased from seven persons in 1983 to 81 at present.

ADEMI presently targets microenterprises, which it defines as businesses that have been operating for at least one year, with six or fewer employees, and less than \$1,592 in fixed assets. Loan amounts and terms are escalated for repeat borrowers, on the basis of their repayment and growth records. At the time of the initial loan, the average size of fixed assets of microenterprises is less than \$1,000, and the average number of employees is three. Seventy-three percent of loan beneficiaries are men, and 27 percent are women, although in 1988 women received 36 percent of the loans extended.

From its inception in 1983 until September 1988, ADEMI extended a total of 19,428 loans. In 1983, the institution made 2,980 loans. In 1986, this figure increased to 3,065 loans, and to 5,152 in 1987. All initial loans are for working capital, and the initial size of the loan ranges from \$25-50. The loans have an average loan term of two to three months. Eighty-nine percent of loans outstanding are for manufacturing enterprises, and 11 percent are for service and retail enterprises. For a first time borrower, loan procedures from application to disbursement, average one week.

Subsequent loans take two days.

Technical assistance offered by ADEMI is demand-driven, and is not a prerequisite for obtaining a loan. Beneficiaries contact loan officers as problems arise. If the loan officer is unable to resolve their difficulty, outside help is sought. Over the past several years, technical assistance has been offered in a variety of areas including production, marketing and accounting. An effort is always made to ensure that the solutions offered are consistent with the operating methods of the beneficiary. For example, three different accounting methods are provided by ADEMI: a "back-of-the-envelope" method for the least sophisticated enterprises; a somewhat more complex method that can be easily managed by someone with little or no training; and a complex accounting program for its largest clients. The major function of the technical assistance is to ensure repayment of the loan, and to monitor that loans are being used for productive purposes. Each advisor has 90 to 130 active clients in his/her portfolio.

3.1.2 PROAPE/FONDESA

The Programa de Asistencia a la Pequena Empresa (PROAPE) and Fondo para el Desarrollo, Inc. (FONDESA) are two separate divisions with closely linked functions within the Asociacion para el Desarrollo, Inc (APEDI), which is a local development foundation in Santiago; the Dominican Republic's second largest city. In addition to PROAPE and FONDESA, APEDI also includes two other divisions, which concentrate on animal husbandry and agriculture. PROAPE is one of the Technical Assistance Centers referred to earlier, funded with U.S. Currency as part of the Small Industry Development Project. FONDESA manages the loan portfolio. It receives no A.I.D. funds, but has been funded by the Inter-American Development Bank and the InterAmerican Foundation. PROAPE/FONDESA's objectives are to increase employment in the lowest income groups; to improve the administrative and managerial capacity of small and microentrepreneurs and to incorporate the informal sector into the formal one.

APEDI was founded in 1961 by leading professionals and businessmen in Santiago. Its creation represented an attempt to mobilize private resources in response to the challenge of the era of "the Alliance for Progress." In ensuing years, it has achieved a considerable reputation for organizational competence in Santiago. In 1979, APEDI conducted a study on the microenterprise sector in Santiago through the facilities of the Instituto Superior de Agricultura in Santiago, and with financial support from Appropriate Technology International (ATI), a nonprofit foundation primarily supported by A.I.D. As a result of the study it launched PROAPE in June of 1981, with assistance provided by ATI and the Central Bank, to provide technical assistance to microentrepreneurs. FONDESA was created in 1982 to make loans to microenterprises served by PROAPE.

The first group of PROAPE/FONDESA entrepreneurs were financed by a finance company on the basis of refinancing by the Central Bank. In 1983, PROAPE/FONDESA extended its services to solidarity groups of street vendors and other similar enterprises. In order to meet the needs of different sizes of enterprises, the project created three subdivisions, one for small enterprises, one for microenterprises and a third for solidarity groups composed of microentrepreneurs. The small enterprise unit is supported by A.I.D. through the Small Industry Development Project. The microenterprise unit has received two grants from the Inter-American Development Bank; for \$225,000 in 1983, and \$275,000 in 1985. The solidarity group unit is funded in part by the Inter-American Foundation.

PROAPE provides management training and conducts feasibility studies for small-and microenterprises, which are then referred for loan applications to FONDESA or to financial institutions which participate in the A.I.D. and government sponsored FIDE Small Industry Development program. The referral depends on the size of the loan requested. The larger enterprises receive loans through FIDE, and the microenterprise and solidarity units receive loans from FONDESA. PROAPE's income is based in part on a commission received for conducting the feasibility study, and for providing additional technical assistance once the loan has been approved. FONDESA lends to microentrepreneurs through a fund provided by the Inter-American Development Bank, and to solidarity groups, through a fund provided by the Inter-American Foundation.

PROAPE/FONDESA's microenterprise program targets businesses with sales less than \$11,943 per year, net worth less than \$7,165, and investment per job created not larger than \$1,433. The small enterprise program targets enterprises with fixed capital investments not exceeding \$31,847, and investment per job created not greater than \$1,592. In order to reach the poorest people in the country, PROAPE/FONDESA also targets solidarity groups, usually made up of five members conducting similar economic activities. The objective of its solidarity component is to ensure that the microenterprise can earn an income level which will meet basic needs, strengthen microenterprise so that they can sustain existing jobs, increase solidarity, and foster a change in attitude.

PROAPE/FONDESA lends to urban-based enterprises which have been operating in the manufacturing sector for at least six months. At the time of the initial loan, the average net worth of the borrowers has to be less than \$6,370, average annual sales must be less than \$11,465, and the number of employees must range from five to 10. Eighty-two percent of the loans are made to men, and the remaining 18 percent to women.

PROAPE/FONDESA reported as of October 1987 that of 1,186 enterprises which it had identified for assistance, it had loaned

\$970,632 to 583 small- and microenterprises. It had also loaned \$108,914 to 332 solidarity groups with 1,641 members. As of October 1988, It had given 116 courses in various principles of management to 1,562 participants.

The average size of the initial loan made by the PROAPE/FONDESA program to individual microenterprises is \$796, while that to solidarity group members is \$398. The average loan term is 1.5 years for microenterprises, and 40 weeks for solidarity groups. Thirty-four percent of all loans are for fixed asset investments, 63.5 percent are for working capital, and the remaining 2.5 percent are for consumption and other purposes. The loans are disbursed by FIDE and FONDESA. Loans up to \$2,400 are disbursed by FONDESA, and amounts exceeding that are disbursed by FIDE.

Eighty-eight percent of PROAPE/FONDESA's loan portfolio goes to small-and microenterprises, and the other 12 percent to solidarity groups. Approximately 69 percent of the loans are for manufacturing purposes, 10 percent are for services, and 21 percent are used for trading activities by the solidarity group members.

PROAPE/FONDESA's training program is a prerequisite to receiving a loan. PROAPE/FONDESA requires program beneficiaries to take standard core courses in accounting and cost analysis, and perhaps up to seven additional courses, in labor law, industrial security, marketing, production, internal control, and personnel administration prior to qualifying for a loan (Chart A). The courses are for 10 hours each, and are scheduled in the evenings. A course program is designed by the loan officer for the applicant, on the basis of a needs assessment. Upon completion of the courses, the beneficiary can request a loan from FONDESA or from the FIDE/Small Industry Program. If additional financing is requested, the loan officer revises the initial assessment and identifies an additional training program for the applicant.

3.2 Demand for ADEMI's and PROAPE/FONDESA's Services

ADEMI treats liquidity constraints, arising from restricted access to formal financial markets, as the major bottleneck to microenterprise development. As a result, ADEMI operates as a financial institution whose objective is to eliminate that constraint; technical assistance is provided to solve specific problems that interfere with the ability of the beneficiaries to repay outstanding loans.

PROAPE/FONDESA's activities are based on the proposition that the long-term development of microenterprises is constrained by technical limitations often not recognized by the beneficiaries. Formal training in a variety of areas is considered a prerequisite for self-sustaining growth of the beneficiary. Credit is provided principally as an inducement for the microenterprises to begin the

training process.

Although impact data for these programs is difficult to compile, and the objectives and methods of the programs are quite different, there is some information on the demand for the services of both ADEMI and PROAPE/FONDESA. Demand for financial assistance from ADEMI has risen at an increasing rate since 1986, stimulated by the streamlining of loan application procedures, and the falling real interest rates as inflation accelerated.¹ At the same time, the demand-driven nature of technical assistance ensured that such assistance would be utilized. On the other hand, PROAPE/FONDESA has faced some difficulties in increasing the assistance provided to beneficiaries. Although no information is available on the number or the amount of loans provided by PROAPE/FONDESA per year, the number of course participants per year has not increased significantly since 1985. In addition, between 1982 and 1987 only 12 percent of participants (50 out of a total of 416) requested additional training or access to second loans. This lack of demand may reflect a variety of factors including reduced funds with the PROAPE/FONDESA program, few unmet training needs or reduced demand arising from the long period between loan application and disbursement.

Although no conclusions can be drawn about the relative benefits of, or demand for credit versus technical assistance, the need for a clear separation of the costs between the two activities was evident. This cost separation, or "financial transparency," will allow an unambiguous evaluation of the costs of each activity and the degree of subsidization necessary, if any, to maintain them. In the absence of such separation, evaluation and appropriate adjustment to external developments become difficult.

3.3 Sustainability

3.3.1 ADEMI

ADEMI has demonstrated that financial intermediation can not only be self-sustaining, it can even be profitable. ADEMI has become self-sustaining after five years of operation. After its annual operational losses had increased from S44,390 in 1984 to \$63,323 in 1985, its deficit declined consistently thereafter. In the first 10 months of 1988, ADEMI has been able to generate an operating

¹As described below, real interest rates fell through October 1988 when ADEMI sharply adjusted both the nominal interest rate charged and the method of calculating interest charges. In December 1987, ADEMI raised its commission from six percent to eight percent, and raised the monthly interest rate on the outstanding balance from 1.5 percent to 1.9 percent. In October 1988, the monthly interest rate was raised to 2.5 percent of the total amount of the loan.

surplus of almost \$64,000 which represents a return on net worth of about 20 percent in nominal terms. These results have been achieved through a combination of rapid growth, effective control of the loan portfolio and relatively high interest rates on loans. Although this surplus does not yet entirely compensate for inflation, it is a significant improvement over the loss of 2.8 percent of net worth in 1987.

ADEMI's liability structure is composed of long-term loans at highly subsidized rates of interest from the Inter-American Development Bank and local currency loans from the government, representing the counterpart of A.I.D. ESF funds. Recently, it has also received a loan from a private Dominican Bank (Banco Popular). By October 1988 the loans from the governments' A.I.D. local currency counterpart funds were the single largest source of funds for ADEMI representing approximately 38 percent of its asset base. ADEMI's accumulated net worth represents almost 32 percent and the Inter-American Development Bank and the Banco Popular provided 12.5 and 15.7 percent respectively of its assets (see Table I in Appendix).

Between December 1984 and September 1988, ADEMI's nominal loan portfolio had grown from \$222,988 to \$1,018,657 which represents a nominal growth of 456.8 percent. Discounting for the increase in prices over the period, in constant 1980 terms this represents a growth of 278.7 percent. The number of loans processed increased from 2,762 in 1984 to 5,152 in 1987. During the first nine months of 1988 ADEMI had disbursed 3,507 loans.

ADEMI's rapid growth has led to economies of scale. Its annual operating costs as a percentage of its average portfolio declined from 71.2 percent in 1985, to 44.9 percent in 1987, to approximately 30.6 percent in 1988. Its interest income plus commissions on its outstanding portfolio has risen from 37.9 percent in 1985 to 46.4 percent in 1987, and is projected to be 42.1 percent in 1988, again as a percentage of its average loan portfolio. Because both the loans from the government and the Banco Popular carry higher interest rates than the loans from the Inter-American Development Bank, ADEMI's weighted interest cost of its liabilities has risen from 1.6 percent in 1985 to 3.2 percent in 1987 and 3.8 percent in 1988. Its gross financial margin (interest income received minus cost of capital) has grown from 23.4 percent in 1985 to 31.1 percent projected for 1988.

Effective interest rates have risen significantly between 1986 and 1988. In 1986, ADEMI charged its borrowers a 6 percent commission and 1.5 percent monthly rate on the outstanding balance. Following a series of revisions between 1987 and 1988, the commission is presently 8 percent and a rate of 2.5 percent monthly is charged on the original amount of the loan.

From Table 5 (see Appendix) it is apparent that a three month

loan rose from an effective rate of 4.74 to 8.21 percent per month as a result of the changes. Likewise a six month loan rose from 3.37 to 6.77 percent. Because of the relatively high commission, the effective rate charged for the loan declines quite rapidly with a rise in the term of the loan. The effective real rate of interest charged ADEMI borrowers rose from .17 percent monthly to 3.47 percent monthly. On an annualized basis, real interest rates on a six month loan rose from 2.04 to 41.64 percent. To underline the impact of the 8 percent commission, if the same borrower would have obtained a 12 month loan rather than two six month loans, the annualized real rate would have risen from -7.68 to 30 percent. Given this large increase in effective interest rates, it is not surprising that ADEMI has been able to turn a profit in 1988.

However, this rapid growth in operating surplus could lead to future difficulties. These high rates of interest have the potential of creating problems with loan recovery for ADEMI depending on the relative importance of ADEMI loans in its clients' capital structure, and the effect it will have on their costs. The effect on costs will in turn affect the prices they will have to charge, and thus the demand for their products. If the demand falls off more than proportionately to the increase in price, their profits will fall.

These effects may not be immediate. In the short run the demand for credit may not fall off despite the fact that there may be many microenterprises that cannot sustain these high rates. The borrowers may not and are not expected to know the effective rate of interest being charged, though they are aware of the increase in monthly loan repayments. Therefore, waiting for the demand for loans to decline as a signal that rates are too high may come too late to avoid loan recovery problems.

If the present ADEMI structure of interest rates is to be maintained, given plausible assumptions on the prospective rate of inflation, careful monitoring of its portfolio is warranted to detect any distress on the part of ADEMI borrowers. After having risen to levels of over 30 percent in 1985, loan delinquency is down to 10.23 percent as of September 1988. The percentage of delinquent payments over 90 days rose from 31.9 to over 50 percent between 1985 and 1986. By September of 1988 payments delinquent over 90 days fell slightly to 45 percent of total delinquent loans (see Table 4 in the Appendix).

3.3.2 PROAPE/FONDESA

A detailed analysis of the sustainability of the PROAPE/FONDESA program is not possible due to the lack of financial information, and because their operations are consolidated with the other divisions within APEDI. However, from APEDI's consolidated balance sheets it is evident that a significant degree of external subsidization is required. Comparative balance sheets presented in

Table 6 (see the Appendix) show that yearly operational losses were of the order of S 108,181 for 1985, and \$154,457 for 1986, and S100,566 for 1987.

According to a budget for fiscal year 1988, PROAPE received its income from three major sources: donations (56.9 percent), commission on loans through FONDESA and FIDE (38.1 percent), "other" sources (3.1 percent) and user charges for training courses (1.9 percent). It is interesting to note that its major service; its courses, represent the least important source of income. If the loan request is above S2,400 then the loan application is channelled to the formal banking system for refinancing by FIDE. However, if it is below this benchmark it goes to FONDESA. PROAPE receives a 3 percent commission on the loans which are channelled through the formal banking system, using FIDE funds for preparing the "feasibility" study. In addition, if there is a need for further technical assistance, a contract is signed with the client enterprise and PROAPE receives an additional two percent per year on the outstanding balance of the loan. If the loan is channelled through FONDESA, PROAPE receives a one percent commission for the preparation of the study and 2 percent additional if technical assistance is required. Since technical assistance is normally required as a loan condition, it normally receives the 2 percent surcharge.

As of November 1985 FONDESA was legally separated from APEDI. however, the analysis of its sustainability is made difficult by the lack of financial information. Table 7 (see the Appendix) presents the balance sheet obtained from the APEDI and A.l.D. This information shows that the loan portfolio grew from \$424,180 in December 1986 to \$570,407 in June 1988. In constant 1980 pesos, the portfolio grew by 8.3 percent in 18 months.

FONDESA had been charging its borrowers 12 percent annual average interest which has recently been raised to 24 percent. Given a monthly inflation of 3.19 calculated above, the real rate of interest is -1 . 1 5 percent per month. Based on calculations from the balance sheets and income statements, FONDESA received interest income which represented 12.57 percent and incurred operating costs which represented 8.76 percent of its portfolio in 1987. This estimate seriously underestimates its real operational costs since advisors from PROAPE serve as loan officers for FONDESA. This cross-subsidization makes any comparisons with ADEMI impossible.

Any profitability analysis of each of the different departments within APEDI would require a detailed cost study to ascertain the distribution of operational expenditures. However, given profits of approximately \$5,824 over an 18 month period, it is clear that if the costs had been adequately allocated between divisions, FONDESA would have had an operational loss. The negative rates of interest charged by APEDI will lead to the

decapitalization of its net worth.

Loan delinquency at the end of 1986 stood at about 13.9 percent of the portfolio but 62 percent of the number of loans had delinquent payments. Presently, the delinquency is estimated at about 15 percent. A significant proportion of the portfolio is in long term loans which means that the delinquency problem could get significantly worse as these loans come to term. According to information provided to A.I.D., on average the PROAPE/FONDESA microenterprise credit program takes up to one month to process a loan application. This lengthy delay is due in part to the lack of liquidity which affects the program. Loan applications for FIDE funds must be channelled through the formal banking system, which can take anywhere from six months to a year to process.

An issue that has surfaced in both the ADEMI and PROAPE/FONDESA programs is the question of which institution is absorbing the exchange risk of the InterAmerican Bank loans. If the Central Bank or the Inter-American Bank are absorbing the exchange risk, then any reference to the dollar amount of these loans in the balance sheets is irrelevant. However, there appears to be confusion on this point on the part of the external auditors of both institutions. If the Inter-American Bank or the Central Bank are not absorbing the exchange risk, both ADEMI and PROAPE/FONDESA are financially insolvent.

3.4 Graduation

Among the various objectives which the ADEMI and PROAPE/FONDESA programs are supposed to achieve, "graduation~ of their clientele into the portfolio of the formal banking system is among the most important. The design of both programs has been made with this objective in mind.

Both programs are designed so as to promote a bank-client relationship between the microenterprises and formal financial institutions. ADEMI initially required that microenterprises open a savings account in a formal financial institution. The purpose of this requirement was to establish a bank-client relationship between ADEMI borrowers and formal financial institutions in order to facilitate the "graduation" of these entrepreneurs into the bank's portfolio. In addition, it was believed that it also played a social educational function by insisting on the benefits of savings. However, as a result of the negative rates of interest paid on savings by the formal financial institutions, this requirement has been dropped.

The actual numbers of microenterprises which have achieved graduation to the formal banking system are so small as to be insignificant. In the case of ADEMI, the director of the program requested a loan from the Banco Popular and provided a list of borrowers with an established credit record so that the Bank could

lend to them directly. The Bank offered to lend the funds to ADEMI so it could continue to serve as a "retail" intermediary for these borrowers. This response on the part of the Bank should not be surprising since the objective of graduation is based upon unrealistic assumptions.

Even if graduation were possible it would not be advisable for these microenterprise credit programs to transfer their least risky and least costly clients to the formal banks because this would tend to undermine their own financial viability.

3.5 Institutional Factors

ADEMI's organizational structure was changed as a result of a "personnel crisis" in 1986, going from a centralized top-heavy structure to a horizontal and functionally decentralized system, which allows for a clear delegation of authority and communication, and overall operational flexibility. An accounting and management consulting firm helped it develop a new administrative structure, and document the procedures and routines it needed to adopt. Each advisor is responsible for managing a "mini" loan portfolio, and is evaluated by clearly established measures on the basis of its performance; by factors such as low delinquency, new clients reached, etc. The organization has instituted several innovative mechanisms for motivating field advisors, and for reducing loan arrearage, such as a recently installed incentive plan, which provides a bonus payment for the advisors to maintain a loan portfolio above a certain size with arrears below a certain level. In addition, the institution's activities are implemented by highly qualified and motivated individuals. All advisors are university graduates, with degrees in economics, accounting, or business administration.

PROAPE/FONDESA's structure is more complex. The program lacks clear institutional objectives, and is inhibited by the institutional structure of APEDI. Less fluidity exists in the structure, and the fungibility of funds between divisions means that it is more difficult to hold the divisions separately accountable for their activities.

3.5.1 Management Information System

ADEMI's management information system was designed at the very start of the program, with a clear vision of what the informational needs of an expanding program would be. It incorporates a large element of flexibility, and uses 20 different computer programs to provide current data on loan portfolio characteristics; client profiles; delinquent loans by age of delinquency, and other necessary information for it to evaluate the growth and quality of its loan portfolio.

ADEMI maintains a computerized information system which serves

its management needs very efficiently. Although some beneficiary information on increase in sales and profits, and number of employees by enterprise is also available, the data is aggregated so that performance over two points in time is difficult to measure. The figures are not presented in a form which lends itself to drawing significant conclusions about impact. However, no matter how well designed the management information system is, it alone is not sufficient to determine impact. External studies and use of control groups is probably necessary.

3.5.2 Transactions Costs

ADEMI has systemized its lending procedures so that a loan is disbursed within a week of the loan application, and every additional loan is disbursed within two days. Loans are issued by checks drawn on a commercial bank (Banco Popular). which the borrower can cash at any branch of the Bank, and repayments are deposited directly into ADEMI's checking account, again at any branch office. The system has been designed to minimize the opportunity cost of lost labor time to microenterprises, to socialize the borrowers into the formal banking system, and to limit the costs of loan collection to ADEMI.

FONDESA and FIDE have not been able to attain such operational efficiency. FONDESA requires an average of one month to disburse a loan, from the time of application, and the larger FIDE borrower waits anywhere from six months to a year prior to receiving a loan. Although the reasons would require further research, the low number of repeat loans for FONDESA may reflect the high cost to the borrower of having to take up to nine courses, and then wait another long period before actually receiving credit.

3.6 Gender Issues

ADEMI has overcome a number of major constraints to credit access faced by women. These include eligibility and collateral requirements, transaction time and costs, and loan sizes and terms appropriate for microenterprises. The number of women participating in ADEMI's program approximates the proportion of women who are economically active in the urban Dominican population. According to an evaluation report of 1984 (Reichmann, 1984), 14 percent of the microenterprise clients and 43 percent of the solidarity group members were women. A greater percentage of women in the solidarity groups reflects women's lower income levels in the Dominican Republic. By phasing-out its solidarity group component, ADEMI could have lost a significant portion of its women clients.

This has not been the case. Although ADEMI has not consciously targeted women, largely due to the presence of women-specific programs in the Dominican Republic such as ADOPEM (Dominican affiliate of Womens' World Banking) and MUDE, the percentage of women beneficiaries has risen to 36 percent in 1988, from 28

percent in previous years.

On the basis of data provided by ADEMI on the types of activities assisted, disaggregated by gender, almost half, or 45 percent of women beneficiaries are in the manufacturing sector, 35 percent are in the service and retail sector, and 20 percent pursue other unspecified activities.

Women are most represented in clothing production, and ceramics, as well as food preparation and selling. Project data was provided on the growth of enterprises from the point of entry into the ADEMI program until November 1988, disaggregated by type of enterprise activity and gender. Employment in male-owned enterprises increased by a larger percent in all cases, with the exception of food vending or retailing, than for women-owned enterprises. In several cases, employment in women-owned activities actually declined. Sales, profits, fixed assets, savings and salaries increased in all of the assisted enterprises, but increased by a larger percent for male beneficiaries versus women beneficiaries. The data should be interpreted with caution, because it is not known at what point these enterprises entered the program. It could be that women are recent entrants into the program, and their relatively more modest gains reflect a shorter period of assistance from ADEMI, or that women-owned enterprises are performing less well than men-owned ones. Further research is required to determine the cause of such differences.

Eighteen percent of PROAPE/FONDESA's program beneficiaries are women. PROAPE/FONDESA targets larger manufacturing enterprises than ADEMI does, in its small- and microenterprise component, and also reaches a smaller percentage of women. No data was available on the percentage of women in the labor force or in the microenterprise sector in Santiago where PROAPE/FONDESA is located, to discern whether 18 percent was a representative proportion of women. However, targeting the larger enterprises may be a partial explanation for the low percentage of women participants, since women are concentrated in smaller enterprises, such as those targeted by ADEMI, or in solidarity group programs. Although PROAPE/FONDESA targets 12 percent of its loan portfolio to solidarity groups, where women are more often concentrated, the relatively small size of this component does not ensure equal access to project resources by women.

The constraints posed by both programs to women is their focus on lending for manufacturing activities. Manufacturing firms tend to be larger than trading or retail enterprises, and thereby include fewer women, who are typically concentrated in the smaller enterprises, and in retail and trading activities. ADEMI has compensated in part for this by targeting the very small firms, where women are concentrated. Its target client group consists of enterprises small enough to include a representative proportion of women beneficiaries. Another constraint to women's participation

may be the lack of female extension workers. ADEMI contended that this was due to social or cultural factors, since Dominican society frowns upon women riding motorcycles, which was the means of transportation used by male workers, as well as working late evenings, which were often the only possible times to visit the microentrepreneurs at their worksites.

3.7 Impact on Beneficiaries

Evaluation of the impact of ADEMI and PROAPE/FONDESA on microenterprises and of microenterprise development projects in general is hampered by the diversity of project approaches, limited statistical information and methodological difficulties of separating the effects of project-related characteristics from the impact of broader macroeconomic developments. In spite of these difficulties, a number of generalizations about employment and income effects have emerged, as summarized in a recent review of A.I.D.'s experience with small and microenterprise projects (McKean, 1988). Employment effects have been found to be high, with the larger small enterprises in the portfolio creating relatively more jobs than the smaller microenterprises while the smaller microenterprises were relatively more efficient than the larger ones in reducing underemployment. The same review also found production in both cases to be positively affected, but the increases were considered to be both low and short-lived. Finally, all studies reviewed emphasized that external developments, including the demand management policy of the government and its regulations, have the largest impact on the activities of microenterprises.

Although both ADEMI and PROAPE/FONDESA were studied, impact data were available only for the beneficiaries of ADEMI. A sample of about 60 microenterprises in both the manufacturing and service sectors was selected and classified, according to the period they had participated in the program. While changes in value added is an appropriate measure of enterprise performance, such data was unavailable. Instead, the change in gross sales, deflated by the appropriate factor to account for inflation (using the sectoral price deflator), was used as a proxy for changes in production. Employment by enterprise was available. In order to isolate the effect of the program from the impact of external developments, the growth and employment of the microenterprises were compared with appropriate comparable sectoral growth averages over the same period.

Enterprises in the sample had been in operation for an average two years and had created about 210 new jobs between 1983 and 1987, and their output had grown at an average annual rate of 30 percent in real terms over the same period (see Table 9 in the Appendix). Both employment and output increased at the fastest pace during the first year following receipt of assistance from ADEMI, with output growing by 62 percent and employment tripling.

The pace of output and employment slowed as the enterprises matured. Further analysis showed that a portion of the slowdown reflected the impact of economywide developments. After correcting for external developments, total output of the microenterprises increased considerably faster than sector averages, with the largest increase occurring in the third and fourth years of operations (see Table 10 in the Appendix). At the same time, employment generation by the microenterprises grew 12 percent faster than sector averages.

Important differences in the ability to generate employment emerged when microenterprises were classified by sector. Employment generation by manufacturing microenterprises was, on average, seven times higher than average manufacturing firms while employment generation by service microenterprises increased at only half the pace of the total service sector (see Table 10 in the Appendix). This discrepancy reflects the impact of the development strategy followed by the government. Throughout most of the 1970s, the government followed a policy of import substitution industrialization which resulted in a highly inefficient manufacturing sector and a rapidly growing, labor-intensive service sector.

An additional issue is whether labor productivity in microenterprises--employing 10 workers or less--is higher than in small-scale enterprises--employing between 11-50 workers. All of ADEMI's initial loans are made to the smaller group; the microenterprises. However, the total number of workers increase as the enterprises grow; thus making them small enterprises. As a result it was possible to examine labor productivity in both microenterprises and small-scale enterprises, because ADEMI continues to serve enterprises which have grown. Only enterprises that had been operating for more than three years were studied. Preliminary results indicate that labor productivity increased sharply in the larger enterprises. On the other hand, labor productivity fell in the smaller enterprises reflecting the fact that labor grew faster than output in such enterprises (see Table 11 in the Appendix). This conclusion held irrespective of the sector in which the enterprise was involved. As employment generation fell in the service enterprises--see above--the increase in labor productivity in large firms in that sector suggests that smaller enterprises predominate in the service sector.

4. FACTORS INFLUENCING PROJECT PERFORMANCE AND IMPACT

4.1 Institutional Factors

- (I) ADEMI benefits from clear and realistic objectives and the institutional autonomy to achieve and monitor those objectives. PROAPE/FONDESA is constrained by the social welfare orientation of APEDI; its sponsor, which is in conflict with its business development thrust. Further,

its efficiency is undermined by its dependence on FIDE, which has been slow and inefficient. The lack of autonomy, and unclarity of project goals has handicapped PROAPE/FONDESA.

- (2) The clear institutional objectives and selection of clientele connected with an assessment of its comparative advantages in attaining its goals have enabled ADEMI's positive performance and impact. The diffused and conflicting goals, different clienteles, and lack of strategic thinking about comparative advantage have inhibited PROAPE/FONDESA in achieving self-sustainability, and perhaps improved beneficiary impact as well.
- (3) ADEMI's autonomy helps to avoid the confusions both in terms of accounting and goals that stemmed from PROAPE/FONDESA's involvement with APEDI.
- (4) ADEMI's decentralized organizational structure, operational flexibility, qualified personnel and sophisticated management information system are factors which contribute to its operational efficiency.
- (5) The separation of technical assistance and credit functions in ADEMI helped maintain and monitor the application of both to its goals. Their linkage in PROAPE/FONDESA, makes it impossible to assess the impact and costs of either. PROAPE/FONDESA's credit portion could be as self-sustaining as ADEMI's, if it adopted a similar approach to credit. It could then design a technical assistance program to address the constraints with which technical assistance is concerned. Since it does neither, both components appear less effective than those of ADEMI.

4.2 Financial Factors

- (1) ADEMI now covers its operating costs and has capitalized its loan portfolio by charging positive real interest rates. However, these relatively high rates may lead to problems with loan recovery, or reduce demand for credit, and the loan portfolio should be monitored carefully to detect borrower distress. PROAPE/FONDESA's negative real interest rates are decapitalizing its portfolio.
- (2) High transactions costs rather than risk are the main reasons that private sector banks in the Dominican Republic are not interested in lending to microenterprises. Given the good risk experience of ADEMI they were willing to lend money to it, provided it accepted the administrative responsibility for the loans. ADEMI's keeping of its clients as they grow, not only

accommodates them but makes it a more viable financial institution, and increases its impact, as shown by survey data.

- (3) The low transaction costs achieved by ADEMI through simplified loan application, repayment, and loan disbursement procedures increase its viability by increasing demand, and reducing delinquency. The delay in disbursing loans by PROAPE/FONDESA may be a factor in the low demand for second loans.

4.3 Impact Factors

- (1) Employment generation, labor productivity, and income generating effects were higher for larger firms and for those in manufacturing, which dictated ADEMI's decision to continue to serve those firms, and move away from the very small firms who had been involved with its solidarity group lending.
- (2) The percentage of ADEMI's beneficiaries who are women is proportional to the number of economically active women in the labor force. ADEMI has been successful in identifying and overcoming some of the constraints to access credit faced by women.
- (3) Government demand management and regulation were the most important factors in explaining microenterprise success.
- (4) ADEMI's program demonstrates indications of differential impact on employment and perhaps production by its clients.

5. LESSONS LEARNED. IMPLICATIONS FOR FUTURE PROGRAM AND POLICY DIRECTIONS

- (I) Clear institutional objectives provide a measure to evaluate "success." The objectives of an institution should be formed in concert with its comparative advantage to deliver a particular service. Whereas ADEMI has defined a clear institutional objective, and identified a streamlined strategy by which to achieve it, PROAPE/FONDESA has not identified its market niche, nor determined its comparative advantage as successfully.

The structure of an intermediary institution should be compatible with its objectives. ADEMI has the institutional autonomy to establish and pursue its objectives, as compared to PROAPE/FONDESA, which is incorporated into the social welfare orientation and more complex structure of APEDI.

- (2) Credit and technical assistance are two distinct program components, and should be measured as such. It is necessary to evaluate the costs of each activity, and to determine the level of subsidization (if any) necessary to maintain either one.

Credit and technical assistance have different objectives and separate benefits and costs. Credit is needed by certain enterprises who would be able to compete in the market, but are constrained from doing so by their lack of access to financial resources. Technical assistance is required when enterprises are less efficient than they might be because of lack of knowledge about how to run their business efficiently. The knowledge imparted by technical assistance should assist them in increasing their efficiency. Empirically, those enterprises which need one often do not need the other, and the forcing of technical assistance implied by linking it with credit often undermines both the assisted enterprise and the technical assistance process.

The impact of technical assistance and credit cannot be easily compared. Not only is impact data difficult to compile but the objectives and methods of the programs are quite different.

- (3) Microenterprise projects should incorporate project design elements to ensure equal access to project resources by women. Although ADEMI does not target women specifically, it undertook a study to identify the particular constraints faced by women in their access to credit early on its life, and incorporated mechanisms to overcome some of these constraints.
- (4) Microenterprise projects which target larger manufacturing enterprises often exclude women, who are disproportionately concentrated in retail and trade, and operate smaller enterprises. ADEMI has increased its number of women beneficiaries by targeting smaller microenterprises. Projects should diversify their portfolio by lending to various sectors, particularly those in which women are disproportionately represented, in order to ensure women equal access to project resources.
- (5) Financial intermediation can be self-sustaining, as demonstrated by ADEMI. Decentralized organizational structure, flexibility, well trained personnel, and sophisticated management increase operational efficiency and reduce costs of service. Simplified loan application, repayment and disbursement procedures increase lender viability by reducing operating costs and delinquency,

and thus increase the demand for a lender's services. Positive real interest rates, which may still be significantly below the rates charged by money-lenders, should be charged by microenterprise projects.

- (6) The expectation of "graduating" microenterprises to formal credit channels is based on unrealistic assumptions. High transaction costs, rather than the perceived risk, pose the obstacle to banks' lending to the sector. Restricted liquidity in the formal banking system may also raise the opportunity cost of lending to microenterprises. From the institution's point of view, graduating clients is not advisable, since transferring its least risky clients undermines its own financial viability. A more realistic goal for an institution to achieve is its own graduation to formal credit channels.
- (7) Though problems of small sample size and survey methodology may limit the accuracy of the findings, enterprises in the manufacturing sector, at least in the Dominican Republic, generated more employment than servicesector firms, and small enterprises (11-50 employees) increased employment more so than microenterprises (1-10 employees). Income growth in the microenterprises continued at a relatively higher rate than the average for the sectors in which they were located. Labor productivity was higher for the small versus the microenterprises. The small enterprises in the sample were originally microenterprises, who had grown and increased their number of employees during their participation in ADEMI's program.
- (8) A.I.D. should support intermediary institutions through an "incubation" period--ADEMI is now self-sustaining after five years in operation.
- (9) The findings and conclusions of this study are limited by a lack of data on the impact of the projects on the beneficiaries. Proper impact studies which will allow for such analysis should be conducted. Indicators to measure impact or value added should be installed at the time of project inception, and allow for ~before and after,~ and "with and without" comparisons, to determine the proportion of change which can be attributed to the project.

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