HONDURAS: FIDE SPECIAL DEBT RESTRUCTURING FUND EVALUATION

Prepared for:

U.S. Agency for International Development, Honduras

January 1990

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TABLE OF CONTENTS

EXECUTIVE SUMMARY

A. Background

On August 31, 1984, the Government of Honduras and the United States Agency for International Development (USAID), signed Project Agreement No. 522-0207 for the development of non-traditional exports from Honduras. To this end, a US$ 10.0 million and a L 48 million (US$ 24 million equivalent) Revolving Credit Lines were established at the Central Bank of Honduras. They were to be operated as second tier financial mechanisms using the banking system as the financial intermediary. Out of the Lempiras Line a L 10 million Special Debt Restructuring Fund (SDRF) was established to be administered by the Foundation for Investment and Export Development (FIDE). Banco Atlántida was to be the trustee of the fund and other commercial banks were to be the financial intermediaries. This evaluation examines the experiences of two subprojects, amounting to L 2,730,653 that were financed out of SDRF proceeds. Restructuring credit was extended to Maderas Hondureñas Procesadas, S.A. (MAHPROSA) and to Derivados de Maderas S.A. (DERIMASA).

1. Maderas Hondureñas Procesadas S.A.

On August 10, 1988 the FIDE Certificate of Eligibility for MAHPROSA was approved for L 1,605,653 worth of credit for the purpose of debt restructuring. In addition to SDRF, funds were approved (L 526,000 and US$ 312,047) to finance fixed assets through the Central Bank's Revolving Lines. On December 12, 1988 SDRF restructuring funds were disbursed by the Trustee Bank to Banco de Occidente. Unfortunately, as of the time of this evaluation (August 1989), the fixed asset credit to be financed through the Central Bank's Revolving Lines had not yet been requested by Banco de Occidente. This experience highlights two of the problems of non-traditional export financing in Honduras: the two existing mechanisms--the Revolving Fund and SDRF--do not work in a coordinated fashion and the Revolving Line moves very slowly.

2. Derivados de Maderas S.A.

The experience of DERIMASA also illustrates disbursement delays in the Revolving Line mechanism. In September 1985, the FIDE Eligibility Certificate for DERIMASA was approved to provide financing through the Central Bank's Revolving Line in Lempiras. DERIMASA was to receive L 500,000 for working capital and, as an exception, L 1,500,000 to pay 50 percent of the company's debts to German Banks (the balance was written off as agreed). Although the amount originally approved totalled L 2 million, due to a 14 month delay, actual disbursements were only L 1,848,078. Of this, L 340,078 were for working capital.

A few years later, in April 1988, DERIMASA approached FIDE to request use of SDRF in order to restructure a debt of L 2,625,000. In September, 1988 the FIDE Eligibility Certificate was approved for L 1,125,000 and on December 28, 1988 SDRF restructuring funds were disbursed by the Trustee Bank to Banco Continental.

As in the case of MAHPROSA, the experience of DERIMASA illustrates delays with the Revolving Fund and lack of coordination among financing efforts supportive of non-traditional exporters.

B. Conclusions

Based on the experiences cited above, which are presented in greater detail later in this report, this evaluation makes the following conclusions:

- **The SDRF mechanism operates in isolation from the Revolving Line facility.** Ideally, SDRF and the Revolving Fund would provide complementary forms of financial assistance to potentially viable, non-traditional export companies. Instead, because the two mechanisms correspond to different institutions, a coordinated effort has not taken place. This lack of coordination has affected the impact of SDRF operations.

- **The Revolving Line process is very slow.** In the cases of both MAHPROSA and DERIMASA, the fresh financial assistance to be provided under the Central Bank's Revolving Credit Lines (aimed to improve operations rather than revise debt structures) was obtained either with delay or not at all (as of the time of this evaluation). These delays have altered the expected impact of the SDRF in both cases, and in fact, led both companies to find new partners and to implement other financial measures.

- **It is premature to assess the real impact of SDRF and Revolving Fund financing** on production, exports and employment generation, etc. Because SDRF financial assistance was provided at the end of 1988, both companies were only slightly more than mid-way through their first year of operation under the financing, as of the time of this evaluation.

- **SDRF has benefitted the banks more than the companies in need.** For example, Banco de Occidente was MAHPROSA's major creditor (L 1,164,972), yet had no commitment to assist the company. In the case of DERIMASA, several German Banks received due payments equivalent to L 1.5 million through the Central Bank's special restructuring credit provided to the company. In addition, Banco de Londres and BAFFAA benefitted since both shared L 1.0 million out of L 1,125,000 the SDRF credit.

- **The regulations governing SDRF eligibility are vague and inadequate.** Article No. 4 of the SDRF by-laws states as a condition for financing that the eventual beneficiary must have debts in arrears, or be in serious financial trouble. In contrast, the SDRF By-Laws Eligibility Criteria Section sets no parameters to restrict the types of debt that could be subject to restructuring. Such loose and somewhat contradictory criteria have left the SDRF financial facility too open, permitting questionable types of financial restructuring. For example, in the case of MAHPROSA, this led to land acquisition and the consideration of loans whose maturities were scheduled for more than two and three years in the future.

- **The SDRF By-Laws, which regulate selection criteria, are not supported by the SDRF legal structure.** In SDRF operations, the selection of enterprises, application of eligibility parameters, amount of financial assistance, type of debts restructured and considerations to select the overdue debts, were taken under SDRF's By-Laws and procedures--and were not based on the mechanism's legal guidelines.

- **The applications for and approval of credit made in both cases were not supported by adequate or appropriate feasibility studies.** The information reviewed by this evaluator contained no feasibility studies appropriate for the approval of lending to support debt restructuring. While there was financial information provided by appraisal documents, there were no restructuring guidelines for the preparation and evaluation of a rehabilitating or a restructuring subproject. It is important that such guidelines be prepared in order to avoid the misuse of the SDRF's scarce resources.

- **In both operations, too much SDRF financing was assigned to pay bank debts.** If the SDRF were designed differently, some of the fund's resources could have been applied to provide fresh working capital and/or to support the acquisition of key fixed assets. The current scheme does not include any effort from the creditor banks to combine different rehabilitating measures. In both cases under study the creditor banks received payments in advance without any coordinated arrangement for additional and simultaneous financial support.

- **Both companies under study are improving performance.** DERIMASA is fully on its way to consolidate its financial position and to improve its operations. While MAHPROSA's results were negative for the same period (amounting to losses of L 117,377), they are expected to become positive by the end of the year, and a L 101,818 annual profit is projected. It is the observation of this evaluator, however, that while SDRF proceeds were considerable from the monetary viewpoint they had little direct impact on the improvement of operations within the subject enterprises.

- **With regard to the economic and social impact of SDRF financial assistance, the results are mixed.** When comparing the two mechanisms, SDRF seems to be the more efficient vehicle for export expansion while the Revolving Line is more cost effective in generating employment. According to Table 1, 1.91 of credit out of the Revolving Credit Lines was required to generate 1.00 of export, while under SDRF operations the ratio was only 0.75 to 1.00. On the other hand, the cost of creating one job under SDRF operations required L 31,756, which is twice the amount of credit required to generate one job with the Revolving Credit Lines.

Table 1

COMPARATIVE SOCIOECONOMIC ANALYSIS IMPACT

(In Thousands of Lempiras)

I. CREDIT LINES	CREDIT DISBURSED	CHANGE IN EXPORTS	CREDIT/ EXPORTS	CHANGE IN EMPLOYMENT	CREDIT/ EMPLOYMENT
A) WORD PROCESSORS ENTERPRISES FINANCED	3,722.	2,064	1.08:1	50	74.440:1
B) MANUFACTURING ENTERPRISES FINANCED	7,884	3,952	1.99:1	939	8.396:1
COMBINED IMPACT	11,606	6,016	1.91:1	989	11.735:1
II. SDRF's OPERATIONS					
A) MAHPROSA	1,606	1,674	0.95:1	15	107.067:1
B) DERIMASA	1,125	1,984	0.57:1	71	15.845:1
COMBINED IMPACT	2,731	3,658	0.75:1	86	31.756:1

It is important to note that the accuracy of the above Table is limited by the short nature of the assignment and the lack of information to compare projections with real results. Consequently, the referenced comparative analysis must be taken as a limited judgement to decide on SDRF's future.

- **Use of SDRF proceeds fell short of demand.** In spite of the initial L 19.2 million estimated demand for SDRF, very few funds were approved and disbursed. It is the view of this consultant that the process for preparing and approving eligibility certificates was behind the delay. For both MAHPROSA and DERIMASA more than six months transpired between the companies' initial meeting with FIDE and the actual disbursement of SDRF proceeds.

- **Delays hindered FIDE's promotion of the fund, and implicitly, the use of the SDRF by other potential beneficiaries.** Management at FIDE perceived a lack of interest at USAID for SDRF's future. Apparently this concern was not unwarranted as a decision had been made to use L 5.0 million of SDRF's original resources (L 10.0 million) to finance free-zone parks. In addition, USAID planned to eliminate FIDE's role to perform financial analyses and evaluations and to provide certificates of eligibility for both the Central Bank's Revolving Credit Lines and SDRF credit.

- **This evaluation re-estimates demand for SDRF financing to be L 11.3 million.**

- **The SDRF mechanism should be redesigned to provide companies the financial support they require.** A restructuring line of credit or a similar financial facility must exist for the non-traditional export subsector, either with or without FIDE's participation but under an institution as a third party to evaluate the corresponding credits requested.

C. Recommendations

There are two principal recommendations. One concerns the pending loan for MAHPROSA and the second, concerns the creation of a Rehabilitation Financial Facility.

1. MAHPROSA

MAHPROSA should prepare and submit to Banco de Occidente updated market and financial analyses for new financing under the Central Bank's Revolving Credit Lines. This effort should consider financial projections for at least five years and include evaluations of marketing mechanisms and price structures.

2. Rehabilitation Financial Facility

A Rehabilitation Financial Facility should be established to support the non-traditional export sector. This effort should take into account SDRF experiences and this report's main findings. The creation of a new financial facility should be based on the following concepts and parameters:

- **An effective rehabilitation package is one that provides financial and technical measures simultaneously.** All parties, including the financial intermediaries and the beneficiaries, need to move together to rehabilitate the targeted enterprise.

- **Credit decisions should be based on proper ex-ante financial and technical analyses of the enterprise's problems.** These analyses and the design of an appropriate rehabilitation package should be prepared by a special working group assisted, as needed, by experts in order to properly determine the company's problems and their remedies. This working group, would be headed by the second-tier institution and include representatives from the financial institution as well as the ultimate beneficiary. Once a rehabilitation package is approved, all the parties would be committed to fulfill their corresponding financial measures. This new program should be self-sufficient.

- **Various financial measures, operating independently or jointly, should be considered depending on the needs of the individual enterprise.** Among these measures are:

  -- Simple readjusting of debt maturities, carried out simultaneously by the creditor bank and the second-tier institution;

  -- Restructuring past due debts;

  -- Providing fresh credit to the enterprise for working capital estimated on the basis of incremental production needs, or for fixed assets, technical services etc;

  -- Special features to increase capital through debt-equity swaps carried out by the creditor banks (50 percent of past due debt could be capitalized and the balance could be restructured out of the second-tier institution's proceeds), individual credit to current stockholders or new credit to increase a company's capital and to provide liquidity; and

  -- Financial assistance to provide qualified technical assistance to resolve production and marketing problems.

3. Future Program

In order to improve the future program, its purpose and criteria should be clearly stated using the following as guidelines:

- **The purpose of the program is to assist potentially successful non-traditional exporters.** It is important that the restructuring credit truly benefit the companies, rather than the banks. Most of the second-tier's proceeds should be disbursed and transferred to the enterprises involved as new or complementary credit for working capital, fixed assets or capitalization, etc.

- **Eligibility criteria regarding past due debt to be restructured needs to be more clearly stated and better regulated.** There should be limitations set up regarding debts related to land acquisition or the construction of facilities not necessary for the company's operations. In addition, restructured debt should be limited to only past due obligations. Along the same line, accrued interest would not be subject to restructuring with the second-tier's proceeds.

From the institutional point of view, one option to consider is to operate the facility through the Industrial National Development Fund (FONDEI), which is a second-tier mechanism operating under the umbrella of the Central Bank. FONDEI currently manages a rehabilitation program for small and medium-scale enterprises. Both the small and medium enterprise program as well as the non-traditional export program could be managed jointly, as a national rehabilitation financial program for the industrial sector. FIDE could provide specialized services for promotional activities and technical assistance, including the preparation of feasibility studies.

Before proceeding with this plan, it would be necessary, of course, to asses FONDEI's capacity to handle such a program. This new endeavor would include a Specialized Rehabilitation Financial Unit that would draw on outside technical assistance, as needed. This unit would coordinate programs, undertake evaluations, monitor the application of rehabilitation measures, and set up a management information system.

(All these actions were projected to be implemented under the Third World Bank Small- and Medium- Scale Project's Technical Assistance, the implementation of which was interrupted.)

The following evaluation report is organized as follows. Chapter I discusses the background of the assignment, including the evaluation purpose, scope of work, and methodology. In Chapter II there is a presentation of the Foundation for Investment and Export Development (FIDE). The main body of the report lies in Chapter III, which reviews and analyzes SDRF and the experiences of the two companies that had received SDRF assistance at the time of the evaluation. Finally, Chapter IV offers conclusions and recommendations for future operations.

I. INTRODUCTION

A. Background

On August 31, 1984 the Government of Honduras and USAID signed Agreement No. 522-0207 for the development of non-traditional exports from Honduras. The General Directorate for the Promotion of Exports and Investments (DGPEI) was created to implement the project. Under DGPEI two private sector implementing organizations, the Foundation for Investment & Export Development, (FIDE) and the Federation of Exporters of Honduras, (FEPROEXAAH), were formed to assist potential exporters in acquiring knowledge of foreign markets as well as in facilitating access to them.

A credit component was also included. This portion provided financial assistance to companies requiring fixed asset investment and/or working capital. Revolving Credit Lines consisting of US $10 million and L 48 million ($ 24 million equivalent) were established at the Central Bank of Honduras. These lines were to be operated as second tier financial mechanisms using the commercial banking system as the financial intermediary.

Two years into project implementation, on December 18, 1986, USAID and the Government of Honduras reprogrammed L 10.0 million from the Revolving Lempira Line to finance a discrete Special Debt Restructuring Fund (SDRF). Out of this Fund, loans were made to two private exporting companies: Maderas Hondureñas Procesadas S.A. (MAHPROSA) and Derivados de Maderas S.A. (DERIMASA). Both companies process and export wood products, a non-traditional export.

In anticipation of further demand for SDRF, USAID/Honduras requested an evaluation of the two loans. A banking expert was contracted to perform this assessment, which took place in Tegucigalpa during August, 1989.

B. Purpose of this Evaluation

The purpose of the evaluation was to provide an independent assessment of the SDRF and to provide recommendations to improve it. The outside consultant was to determine whether the SDRF is helping the Mission achieve its objective to promote non-traditional exports.

C. Scope of Work

In order to assess the impact of SDRF, the consultant was to address and comment on the following issues:

- **Operations.** Did the operations analyzed meet the required criteria and were the specified procedures followed?

- **Impact.** What was the impact of the SDRF operations in terms of exports, financial viability, and employment generation?

- **Returns on Investment.** How do the benefits realized from SDRF operations compare with the alternative of financing credit-worthy, non-traditional exporters?

- **Credit Availability.** How limited is the availability of medium-term credit for otherwise credit-worthy non-traditional exporters?

- **Recommendations.** What are the lessons learned? What modifications of the SDRF's objectives, procedures and regulations should be made to maximize its efficiency and impact?

D. Methodology

In order to answer the above questions, the consultant read pertinent documents; met with USAID, banking and private sector individuals; and performed qualitative and quantitative analyses of the information gathered. Specifically, the methodology consisted of:

- **Reading** documents pertaining to FIDE and the SDRF. These included evaluations of FIDE, as well as the by-laws and the operating procedures of the SDRF. In addition, he reviewed feasibility studies and information directly related to the financing of SDRF subprojects.

- **Meetings** with officers of the institutions supervising and administering the SDRF. These included personnel at USAID, FIDE, the Central Bank of Honduras, Banco de Occidente, and Banco Atlántida, as well as SDRF beneficiaries, Rodney Thomson (General Manager of MAHPROSA) and Roger Orsoto (Financial Director of DERIMASA).

- **Oral progress reports** to AID officers and FIDE. These meetings kept all parties informed and allowed for feedback and discussion of preliminary findings.

- **Qualitative analysis.** The consultant identified and assessed the SDRF subproject approval process. Specifically, he reviewed the technical and operating procedures that were applied versus SDRF's basic requirements.

- **Quantitative analysis.** This analysis had two foci:

  -- A comparative analysis between projected versus real benefits. The most fundamental economic parameters and financial ratios were taken into consideration, although much information had to be estimated. A proper analysis was impeded by the lack of a Management Information System to provide updated financial and socioeconomic information on the subprojects at the Central Bank, FIDE or the related banking institutions.

-- A comparative analysis of the SDRF versus the Revolving Credit Lines. This analysis applied quantitative parameters to determine if it would be more or less profitable to invest one monetary unit under the SDRF or under the Revolving Credit Lines. This analysis was hindered due to a lack of current information on shadow prices, labor costs and other basic data. For the most part, the consultant calculated the Financial Internal Rate of Return and other quantitative parameters such as export generation, import substitution and employment, etc.

II. THE FOUNDATION FOR INVESTMENT-EXPORT DEVELOPMENT (FIDE)

A. Overview

As mentioned in the Introduction, the Foundation for Investment and Development Export (FIDE), was created in August 1984 under the Export Development and Services Project for the purpose of generating export earnings and investment in Honduras. Specifically, FIDE is to undertake five areas of activity: 1) assist individual Honduran enterprises to increase non-traditional exports; 2) serve as facilitator for foreign investment in Honduras; 3) assist in the development of at least two export processing zones in Honduras; 4) provide technical assistance to existing or new producers' associations, particularly in the wood products groups; and 5) serve as the technical support arm of the private sector to analyze policy issues which affect efforts to increase non-traditional exports.

To meet these objectives, FIDE carries out promotional activities; provides technical assistance; performs feasibility studies and evaluations; conducts orientation in trade and product marketing; and assists in resolving production problems or improving quality to meet foreign market requirements. In addition to the above role, FIDE's Substantive Law and its corresponding By-Laws permit it to set up and manage programs to provide financial assistance to its beneficiaries.

FIDE has a current staff numbering 35 persons, of which 18 are professionals, and the balance are accountants, secretaries and other support personnel. It is organized into functional departments including those for Operations, Industrial Services, External Promotion and Information.

The Industrial Services Department is in charge of feasibility studies and project analysis, primarily to issue eligibility certifications for credit applications. Since its creation, FIDE has carried out 75 feasibility and/or evaluation studies. Out of these, 70 have been approved representing US$ 13.2 million and L 43 million as financial assistance for the non-traditional export subsector. At the present time, one professional and one half time secretary have been assigned to carry out enterprise analyses and evaluations for both SDRF and the revolving lines of credit. This Mini Unit has also received sporadic assistance from other FIDE staff and from consultant services.

Most of FIDE's operations have concentrated on trade promotion activities. This has included technical assistance in administration, financial and production systems, product marketing and in investment promotion, particularly through the creation of industrial free zones.

B. FIDE's Financial Facility Role

In 1985 the Central Bank administered revolving credit lines were established. FIDE was to participate by issuing Certificates of Eligibility for credit approved by the banking system and rediscounted by the Central Bank. FIDE was to and has provided technical judgement and financial assessments for the credit decision making. FIDE's role in the above scheme reflects the banking system's need for technical assistance in project preparation and evaluation.

C. Anticipated Future Operating Mechanism

At the present time, all the institutions involved in managing SDRF and the Revolving Credit Lines are adjusting their operating procedures and FIDE's technical role is being transferred to the banking system. The new scheme will streamline current operational procedures of both credit mechanisms by limiting the lines of credit to two institutions and the execution to three.

The lack of solid credit evaluation skills in the banking system remains a serious problem. Because of this, as well as the fact that the intermediary banks assume the credit risk, the banks continue to require technical assistance in the preparation and evaluation of large development investment subprojects. Until the intermediary banks can develop the capacity to prepare and evaluate large investment subprojects, a third party must carry out (at least) ex-post evaluations and have the authority to reverse those operations that are not approved according to the terms and conditions of the corresponding credit facility. At the present time, these procedures are in the banks' best interests and it also helps to ensure attainment of the Program's expected results.

Providing an example of this gradual transfer of responsibility to the banks is the operation of the Industrial National Development Fund (FONDEI). FONDEI is a second tier credit mechanism operating under the umbrella of the Central Bank and has been implementing the third World Bank Small and Medium-Scale Project for Honduras. This Project includes a technical assistance component to assist FONDEI's financial intermediaries in setting up special units in their Credit Departments to handle not only FONDEI's rediscount operations, but also other rediscount credit lines for development investments, such as the revolving credit lines in reference. The gradual transfer of the subprojects' final approval to the banking system, while leaving the evaluation of the large subprojects to FONDEI, was the strategy behind the technical assistance. A free limit of L 100,000 was initially agreed upon, yet recently has been increased to L 200,000. As a result, special units were installed in Banco de los Trabajadores, Banco de Capitalizadora Hondureña, Banco de las Fuerzas Armadas and Banco del Ahorro Hondureño. Similarly, with the SDRF, the best approach for now would be to provide assistance to the banks in project evaluation with the understanding that these responsibilities should eventually rest entirely with the banks themselves.

III. THE SPECIAL DEBT RESTRUCTURING FUND

A. Introduction

On December 18, 1986, USAID and the Government of Honduras reprogrammed L 10.0 million from the Revolving Lempira Credit Line to finance a discrete SDRF. One year and a half later, on May 13, 1988, the corresponding agreement between USAID and FIDE was signed. The institutional scheme for this complementary credit facility rests on the participation of FIDE's technical support, the banks as financial intermediaries and Banco Atlántida as Trustee of the resources, which were assigned to FIDE.

The objective of the SDRF is to increase non-traditional exports by establishing a mechanism that would allow debt restructuring and the infusion of additional capital to firms which demonstrate a significant export potential but whose current debt structure hinders this potential. Under SDRF's operations there is not a Guaranty Fund facility, consequently, the credit risk is borne by the intermediary bank and the final beneficiaries.

As of the time of this evaluation, subprojects amounting to L 2.730,653 had been financed out of SDRF proceeds. The SDRF facility had assisted two companies, MAHPROSA and DERIMASA, the experiences of which are discussed below.

B. Maderas Hondureñas Procesadas S.A.

1. Background

In March, 1988, MAHPROSA approached FIDE for special financial assistance to restructure a total of L 1,605,653. Five months later, on August 10, the FIDE Certificate of Eligibility was approved for the above amount to be financed out of SDRF proceeds. On November 29, 1988 the restructuring credit agreement between Banco Atlántida and Banco de Occidente as Trustee Bank and Financial Intermediary, respectively, was signed. Two weeks later, on December 12, the restructuring funds were disbursed by the Trustee Bank to Banco de Occidente.

In addition to the restructuring funds, L 526,000.00 plus US$ 312,047 for fixed assets were to be financed through the Central Bank's Revolving Lines. As of the time of this evaluation, however, this credit had not been approved. With regard to this delay, this evaluator interviewed officers of Banco de Occidente who expressed the Bank's intention to present the corresponding application to Central Bank within the following few weeks. Given the amount of time that has transpired, however, Banco de Occidente's action is long overdue. The above experience illustrates the operational problems of a project utilizing two separate credit facilities that are supposed to operate in a coordinated fashion on behalf of a common objective: the increase of non-traditional exports.

2. Eligibility Criteria

As noted above, the experience of MAHPROSA highlights the difficulty of coordinating the provision of credit from two different sources. It also demonstrates the need to follow and adhere to strict eligibility criteria in order to meet program objectives.

The SDRF By-laws, however, are confusing. According to Article No. 4 of the by-laws, the conditions for use of SDRF resources require that a potential beneficiary's debts be in arrears or, alternatively, that the enterprise be in serious financial trouble. The Eligibility Criteria Section of the by-laws, however, does not include these parameters or regulations.

With regard to MAHPROSA, the eligibility study prepared by FIDE shows a restructuring credit breakdown (see Table 2).

According to Table 2, an amount of L 250,000 was the only debt past due at the time of the eligibility approval declaration. In a strict sense, this amount is the only one that should have been considered for restructuring purposes, since this type of financial assistance usually covers past due debts and ostensibly those debts or installments due within the following year. In MAHPROSA's case, however, the analysis included not only past due debt, but also future payments due in more than one and two years, and also a liability of L 184,798, the last installments of which were scheduled to be paid in 1993, representing advance payments of more than four years.

It appears that MAHPROSA's restructuring loan was considered under conditions of both the arrears, and general financial difficulties as delineated in Article No. 4 of the By-laws. MAHPROSA's 1987 Income Statement, however, shows L 162,558 as a net profit, indicating that the enterprise was not in serious financial trouble. In addition, the debt-equity ratio was 3.00 to 1.00, which was satisfactory. Liquidity was negative, indicating that the company, more than a restructuring measure, needed fresh money either by capital increment or through new financial credit. This is, in fact, what was requested in the Eligibility Certificate to be financed under the Central Bank Revolving Credit Lines. It is the observation of this evaluator that the use of SDRF was not necessarily appropriate in the case of MAHPROSA. What MAHPROSA needed was an injection of capital, rather than a restructuring of its debt. As such, SDRF assets might have been used more appropriately elsewhere.

3. Impact of the SDRF Credit

It is the view of this evaluator that the SDRF restructuring credit provided to MAHPROSA, rather than favoring the enterprise and solving its liquidity problem, actually benefitted Banco de Occidente. Banco de Occidente was the major creditor in the amount of L 1,164,972, without any commitment attached to the restructuring credit.

In order to resolve its need for working capital, MAHPROSA increased its capital from L 531,100 to L 760,100 in 1988, which was insufficient to resolve its greater liquidity needs. MAHPROSA has continued solving its working capital shortage, however. Out of the L 565,000 agreed to in the restructuring credit, MAHPROSA has already capitalized

L 440,000, increasing its capital to L 1,200,000 as of June 30, 1989. This has improved its debt-equity ratio from 3.00 to 2.58, which is satisfactory.

Table No. 2

MAHPROSA'S RESTRUCTURING CREDIT BREAKDOWN
(In Lempiras)

BANK	PURPOSE	DEBT	INTEREST RATE	MATURITY
Occidente	Land	250,000	17%	May/19/88
Occidente	Machinery	450,000	17%	March/20/90
Occidente	Land	61,637	17%	March/20/90
Occidente	Inventories	403,335	17%	Revolving
Occidente	Machinery	132,000	17%	March/29/90
Occidente	Machinery	28,049	17%	March/06/90
Occidente	Machinery	95,834	15%	Feb/02/90
Occidente	Machinery	184,798	15%	Feb/06/93
TOTAL		1,605,653		

Aside from the SDRF restructuring credit, MAHPROSA has received no other credit, a factor which indirectly favored its financial position by inducing its stockholders to increase its capital. Assuming that MAHPROSA would have received the funds requested from the Revolving Credit Lines, and at the same time increased its capital to L 565,000 as recommended by FIDE, it could be said that its debt-equity ratio would be less than satisfactory but still acceptable. Table 3 shows the debt-equity ratio situation estimated on the above assumptions.

Table 3 shows that even though the liabilities would have been twice the 1987 level, the debt-equity ratio could have been 2.16:1.00, which would still be satisfactory.

MAHPROSA's main needs were for: 1) working capital (to address a liquidity problem) and 2) new credit to purchase a wood drying oven that would make it possible to increase its production, and hence, its sales.

For MAHPROSA, the SDRF enabled the enterprise to be capitalized. MAHPROSA currently is increasing operations, sales, exports and employment. The above benefits, as well as MAHPROSA's current take-off position must be credited either directly or indirectly to the financial assistance provided by SDRF.

It is possible, however, that the same results could have been achieved with less SDRF financial participation, thus saving SDRF's scarce resources for other enterprises. MAHPROSA's restructuring credit could have been limited to L 250,000 plus some already past due installments, totaling about L 800,000. Parallel to this there should have been a written commitment with both Banco de Occidente and MAHPROSA to maintain the L 403,335 working capital line of credit and to provide new credits for the wood drying oven, as well as for fresh working capital. The commitment should also have included L 565,000 for MAHPROSA's capitalization.

MAHPROSA's total sales, export and employment figures increased compared with 1987 results. While the 1988 financial result was negative, that for 1989 is expected to be positive. Table 4 presents a comparative analysis in this regard.

MAHPROSA's 1988 financial results have been affected by an increase in sales costs. While the value of sales in 1988 increased by 31.8 percent (when compared to 1987 operations), cost of goods sold increased by 35.9 percent. This is due to higher rates of increases for raw materials and production costs vis-a-vis those of its sales price. Even though the financial results projected for 1989 are expected to be positive (L 101,818. as a net profit), there is still a gap between both parameters, that it is anticipated would be greater in 1989 (sales would increase by 50.9%, while cost of goods sold would go up by 56.1%). This situation indicates that MAHPROSA's price structure must be reviewed and probably revised.

With regard to the revolving credit that MAHPROSA has requested and still awaits, the company should update its analyses of prices, costs and break-even point as well as revise its market goals. These analyses should include in-depth reviews of the company's marketing mechanisms as well as the product price structure versus raw material and processing costs. MAHPROSA should calculate these financial projections for the next five years.

Table No. 3

MAHPROSA'S DEBT-EQUITY RATIO SIMULATION EXERCISE
(In Lempiras)

December 31,1987		August 31, 1988	
Equity		Equity	
Initial Capital	708,466	Initial Capital	708,466
Total Liability	2,129,285	Capital Increment	1,272,724
Debt-Equity Ratio:	3.00:1	Total Capital	1,981,190
		Initial Liability	2,129,285
		New-Credit, F-A	1,150,094
		New Working Capital	1,000,000
		Total Liability	4,279,379
		Debt-Equity Ratio	2.16: 1

Table No. 4

MAHPROSA'S ECONOMIC AND SOCIAL RESULTS
(In Lempiras)

	1987	1988	% CHANG	1989	% CHANGE
Total Sales	4,751,286	6,265,111	31.8	9,453,438	50.9
Cost of Goods Sold	4,267,364	5,801,177	35.9	9,055,028	56.1
Net Profit	162,558	(117,377)	(72.2)	101,818	86.7
Exports	3,229,488	4,054,161	35.9	5,728,252	41.3
Employment (# of Jobs)	154	154	None	169	10

MAHPROSA's 1988 operational and financial results were not influenced by the expected financial assistance. SDRF's credit disbursement was made on December 1988 and, as noted above, the Revolving Line of Credit loans requested have not yet been approved. A true evaluation comparing projections and achievements must be carried out on the basis of 1989 results. Table 5 shows a comparative analysis of key financial ratios.

Table No. 5

MAHPROSA'S FINANCIAL RATIOS

DEBT RATIOS	1987	1988	1989
Total Debt/Total Assets	0.75.1	0.76:1	1.47:1
Long Term Debt/Patrimony	0.60:1	2.07:1	1.56:1
Short Term Debt/Patrimony	2.39:1	1.02:1	0.70:1
Long Term Debt/Tot. Debt	20.27:1	66.87:1	69.77:1
Short Term Debt/Tot. Debt	79.73:1	33.13:1	30.23:1
Debt/Equity	3.00:1	3.10:1	2.28:1
PROFITABILITY			
Sales	L.4,751,286	L.6,265,111	L.9,453,438
Profit/Sales	3.42%	(1.87%)	1.08%
Profit/Equity	3.06%	(15.4%)	8.48%
Sales Cost/Sales	89.81%	92.59%	95.87%

As indicated in Table 5, there is an improvement in the debt-equity ratio of 2.28:1 projected for the end of 1989 from 1988's ratio of 3.1:1. In this sense, it could be said that the company required some capitalization and also needed to restructure the composition of some of its debt.

The structure of MAHPROSA's debt was adjusted in 1988 due to the SDRF restructuring assistance, which permitted a reduction of the short-term debt from 79.7 percent of total debt in 1987 to 33.1 percent in 1988. A positive financial result is expected at the end of 1989, which will improve the company's profitability ratios. (It is important, however, to note the incremental tendency of cost of goods sold already mentioned.)

Table No. 6

SDRF'S IMPACT ON MAHPROSA, 1988/89
(In Lempiras)

Restructuring Credit	Sales	% Change	Exports	% Change	Employment Generate	
					No. of Jobs	%
1,605,653	3,188,327	51	1,674,091	41.3	15	10

Based on the above analyses (see Tables 4, 5, and 6), it could be said that from 1.00 of the restructured debt, 1.89 of sales were generated and 1.04 of export value was created. With regard to employment generation, 15 new jobs were created, representing a 10 percent increase. The above means that L 707,043 of restructuring credit was required to create one job, which is not compatible with the L 12,944 estimated cost per new job calculated for wood and textiles enterprises.

Since the SDRF credit was for debt restructuring, its impact cannot be compared to that of other credit lines. Unlike other types of credit, SDRF would not have a direct effect on productions or sales, etc. For example, credit provided under the Revolving Credit Lines has been for fixed assets and working capital, which should have a direct effect on production, sales, exports and employment, etc. Since SDRF would not have such a direct impact, any comparative analysis between it and the Revolving Credit Lines's operations would not be valid. Also, as was mentioned in the Methodology Section of this Report, a cost/benefit socioeconomic analysis is not feasible either.

C. Derivados de Maderas S.A. (DERIMASA)

1. Background

DERIMASA's relationship with FIDE dates back to 1985 when the company was unable to comply with its obligations to two German Banks for a total equivalent of L 3.0 million. With FIDE's aid through the Lempira denominated revolving lines, DERIMASA was to receive L 500,000 for working capital, and as an exception, L 1,500,000 to pay 50 percent of its debt to the German Banks (the balance was written off, as agreed). Even though the total amount approved was L 2.0 million, due to disbursement delays at the Central Bank, the actual amount received was L 1,848,078, out of which L 340,078 was for working capital. Although FIDE's certificate was approved in September 1985, DERIMASA did not receive any funds until December 26, 1986, 14 months later. This delay affected DERIMASA's operational projections, and thus the fulfillment of its financial obligations.

Nevertheless, under the first round of financial assistance provided to DERIMASA through the revolving lines the following was achieved: 1) a reduction of a large company's debt through the writing-off of L 1.5 million, 2) a change in the currency composition of the German Banks' debt from US$ 750,000 to long-term debt in Lempiras, and 3) L 500,000 in credit for working capital to keep alive a company that by then had 124 employees. In general, this assistance rescued an enterprise with export potential generation.

For reasons that related more to the market than to the company's financial health, DERIMASA was unable to take off and to recover its normal working pace. By the end of 1987 it had fallen into financial difficulties once again. This made DERIMASA come to FIDE for further financial assistance. The total non-traditional exports' resources involved in DERIMASA's case totaled L 2,965,077.73.

In April 1988 DERIMASA approached FIDE for SDRF financial assistance in order to restructure a total debt of L 2,625,000. In September 1988 the FIDE Eligibility Certificate was approved for L 1,125,000. Three months later, in December 1988, the restructuring credit agreement between Banco Atlántida and Banco Continental as Trustee and Financial Intermediary, respectively was signed and on December 28, SDRF's restructuring funds were disbursed by the Trustee Bank to Banco Continental.

2. Eligibility Criteria

In DERIMASA's case the eligibility certificate was limited to the past due debt, amounting to L 1,125,000 (see Table 7). (DERIMASA's application included also an obligation with Banco Continental for L 1,500,000, which was not past due and was not approved.) As compared to MAHPROSA, SDRF financing for DERIMASA was more in line with the facility's objectives since it was used to restructure past due debts. As it was mentioned earlier, SDRF by-laws do not go into detail in relation to the types of debt or the maturities of future installments.

Table No. 7

DERIMASA'S RESTRUCTURING CREDIT BREAKDOWN

BANK	PURPOSES	DEBT	INTEREST RATE	MATURITY
Continental	N.A.	L.1,500,000	17%	In 3 Years
BANFFAA	W/Capt:	L.500,000	17+2%	Past Due
Banco de Londres	W/Capt:	L.500,000	17+2%	Past Due
Banco Sogerin	W/Capt:	L.125,000	17+2%	Past Due
TOTAL REQUESTE		L.2,625,000		

3. Impact of SDRF Financing

Since the Company actually received less fresh money than anticipated, (L 340,077 instead of L 500,00) and the disbursement was behind schedule, the amount was insufficient for DERIMASA to resolve its working capital needs. Lack of working capital was not the only problem faced by the company. In addition, DERIMASA was in financial difficulty due to the structure of its debt, which included loans taken out by affiliated companies that were not reflected in its financial statements. Based on the above situation, DERIMASA had to look for new stockholders (COMISA Group). The new partners provided fresh capital in the amount of L 559,000 and L 500,000 as one year non-interest bearing loans, which would be capitalized at the end of the year if required by the company. Table 8 shows historic and projected key financial ratios:

Table No. 8

DERIMASA'S FINANCIAL RATIOS

DEBT RATIOS	1987	1988	As of June 1989
Total Debt/Total Assets	0.55: 1	0.77: 1	0.72: 1
Long Term Debt/Patrimony	0.32: 1	0.32: 1	1:07: 1
Short Term/Debt Patrimony	0.90: 1	3.11: 1	1.51: 1
Long Term Debt/Tot. Debt	0.27: 1	0.09: 1	0.42: 1
Short Term Debt/Tot. Debt	0.73: 1	0.91: 1	0.58: 1
Debt/Equity	1.22: 1	3.43: 1	2.60: 1
PROFITABILITY			
Sales	L.5,585,463	L.6,090,623	L.3,753,719
Profit/Sales	(0.06: 1)	(0.22: 1)	0.11: 1
Profit/Equity	(0.80: 1)	(0.80: 1)	0.15: 1
Cost of Goods Sold	86%	93.9%	83%

As mentioned, the SDRF restructuring credit to DERIMASA, was signed and disbursed on December, 1988. It is logical to assume, therefore, that the effects of the above credit would be noticeable in 1989. The above Table presents the 1987 financial ratios and shows the corresponding ones through June 30, 1989. After four turbulent years it appears that finally the Company is in a comfortable financial position.

As indicated in Table 8, in 1988 DERIMASA's long-term debt represented only 9 percent of its total debt, whereas by June 30, 1989 long-term debt represented 42 percent of the company's total debt. Short-term debt, which stands at 58 percent of total debt, has been reduced considerably from the 1987 figure of 73 percent and the 1988 figure of 91 percent.

The debt/equity ratio as of June, 1989 was 2.60 to 1.00 shows a considerable improvement from its 1988 ratio of 3.43 to 1.00. The composition of DERIMASA's current liabilities along with its actual debt/equity ratio provide a sufficient financial base for the company to increase its operations.

In 1988, DERIMASA experienced losses of L 1,360,824. Added to its 1987 losses, they totaled L 1,692,903. These losses were the result of several problems, among them higher cost of goods sold, uncollectible accounts written-off in 1988, production and fixed costs that increased at a much faster rate than sales, quality problems, market of loss and lower production.

Along with the reorganization of DERIMASA's stockholder composition (COMISA Group as new partnership), the Company changed its product and marketing strategy. As a result, demand has increased and better prices have been attained, as reflected in the positive results obtained as of June 30, 1989. Table 9 shows a profit of L 426,570 at that time.

Table No. 9

DERIMAS'S ECONOMIC AND SOCIAL RESULTS
(In Lempiras)

	1987	1988	% Change	June 1989	Projected Dec. 1989	% Change
Tot. Sales	5,585,463	6,090,623	9.0	3,753,700	8,270,478	35.79
Exports	3,256,934	3,074,300	3.0	2,444,517	5,058,790	64.55
Cost of Goods Sold	4,803,987	5,720,551	19.2	3,101,793	o,895,315	20.53
Net Profit	(332,079)	(1,690,824)	Negat	426,570	1,575,664	115.78
Employment	124	309	149.1	380	380	23.00

DERIMASA is projecting to finish 1989 with sales of L 8,270,478, which would represent an increase of 35.79 percent in current terms. Net profit should approximate L 1,575,664, which would represent a 200 percent increase over the 1988 negative result. At the time of FIDE's second eligibility certificate, 15 new jobs were anticipated and the real employment increment had been the creation of 71 new positions. When DERIMASA approached FIDE for the first eligibility certificate, 124 employees were working permanently compared to the current level of 380 personnel, representing a 206 percent increase.

It cannot be said, however, that the above results are the due directly to the SDRF credit, because it was mostly for debt restructuring, and any liquidity provided went to the intermediary bank rather than to the company.

Table 10 shows that L 1.00 of restructuring credit generated 1.94 of sales and 1.65 of export value. With regard to employment generation the impact was the creation of 71 new jobs, which represents a 23 percent increase from the 309 number of employees in 1988. The above means that L 15,845 of the restructuring credit were required to create a job, which is compatible with L 12,944 estimated cost per job calculated for wood and textiles enterprises. As in MAHPROSA's case, it is important to note that results obtained by DERIMASA cannot be considered as being a direct effect of the SDRF restructuring credit. Therefore any comparative analysis based on the above impact versus Revolving Credit Lines operations will not provide sound comparable parameters.

Table 10

PROJECTED IMPACT OF THE SDRF CREDIT TO DERIMASA
Years 1988 - 1989
(In Lempiras)

Second Restructuring Loan	1,125,000
Projected Change in Sales at end of 1989	2,179,855
Sales Generated by SDRF Restructuring Loan	1.94
Projected Change in Exports at end of 1989	1,984,490
Exports Generated by SDRF Restructuring Loan	1.65
Employment Generated	
Number of Jobs	71
Percent Change	23.0

D. Demand for the SDRF

In October 1988 FIDE identified eleven non-traditional export enterprises as eventual users of SDRF proceeds. Their total restructuring needs amounted to an estimated demand of L 19.2 million. This amount surpassed the initial L 10.0 million assigned to this financial facility. MAHPROSA and DERIMASA were included in the original list of eventual beneficiaries. Under the context of this assignment, an eventual demand has been estimated as shown in Table 11.

Table No. 11

ESTIMATED SDRF'S DEMAND

	COMPANY	ACTIVITY	AMOUNT	EXPORT
1	MADETEX:	Furniture	L.6,000,000	Yes
2	Textiles Maya:	Apparel	L.2,000,000	Yes
3	Marmol de Hond:	Marble Products	L.2,600,000	Yes
4	Blondy S.De R.L.:	Apparel	L.1,000,000	Yes
5	ANA:	Aluminum Products	L.1,600,000	Yes
6	Tabacos de Oriente:	Cigars and Tobacco	L.3,000,000	Yes
7	ARTESANOS:	Furniture	L.550,000	Yes
	TOTAL:		L.11,350,000	

The above demand was estimated based on FIDE's records and it must be re-estimated case by case. It should also consider those companies that have been financed under the Revolving Credit Lines, which could be in financial difficulties and could use SDRF financial assistance.

In addition to the enterprises identified in Table 11, there are others in the non-traditional export subsector that might seek assistance from the restructuring credit facility. In the Recommendations Section of this report there are guidelines to revise SDRF objectives and eligibility criteria. It should be noted, however, that this kind of financial assistance should not be in great demand. Excessive demand for this type of credit would indicate that there are fundamental difficulties with the main credit lines or that the corresponding sector or subsectors are in bad condition.

IV. CONCLUSIONS AND RECOMMENDATIONS

The following conclusions reflect the main findings of this evaluation.

A. Conclusions

- The SDRF is an isolated financial facility which, alone, does not address the needs of the target group. Non-traditional exporters require comprehensive financial assistance, of which debt restructuring is only one component. The SDRF should be part of an integrated financial rehabilitation package that would also include the provision of new credit or other more sophisticated and complementary financial remedies, such as the conversion of part of a company's debt into equity (debt/equity swaps).

- The assistance provided to both enterprises evaluated, MAHPROSA and DERIMASA, was not as effective as it could have been due to the lack of coordination between the two financing mechanisms.

- The SDRF By-Laws do not set up regulations regarding the type of debts to be restructured. In MAHPROSA's case, loans whose maturities were scheduled for more than two and three years in the future, as well as a loan for land acquisition were considered.

- Both SDRF operations favored the banks more than the enterprises. Rather than helping the companies solve their liquidity problems, the schemes benefitted the Intermediary Banks and other financial institutions by enabling them to recover credit in advance. It is important to point out, however, that from a legal standpoint, both referenced operations were carried out in line with SDRF's By-Laws. The problem is that neither the By-Laws nor the operating regulations or guidelines ruled about these matters.

- The SDRF design summary is deficient.

- The SDRF provided indirect financial support during critical moments. Since the fund did not provide working capital or financing for equipment acquisition, there was no direct impact on production, employment generation, or exports. Nevertheless, the evaluation has demonstrated that due to other factors, such as capitalization by the owners and new marketing strategies, there were increases in sales and exports. In the case of MAHPROSA, the restructured credit was expected to lead to the creation of 154 new jobs. In fact, 169 were created, representing a 10 percent increase. With regard to DERIMASA, 71 new positions were created compared to 15 that were expected to result from the second credit. In this respect is important to note that under the first restructuring, DERIMASA was able to create 185 new jobs.

- From a financial standpoint, both MAHPROSA and DERIMASA are on their way to financial recovery. This is particularly significant since last year both were operating in the negative. As of June 30, 1989 MAHPROSA was still showing losses, but a profit was projected for the end of the year. It is important to point out that the major constraint affecting MAHPROSA is its price structure. DERIMASA has experienced better short term results. As of June 30, 1989 it had reported a profit of L 426,570 and the company expects to achieve a profit of L 1,575,664 by the end of the year.

B. Recommendations

The following recommendations are made:

- A financial facility like SDRF should continue to operate to rescue non-traditional exporters that face financial difficulties. In most developing countries the expertise required to become successful exporters is uncommon. It is advisable, therefore, to assign resources to assist exporters, especially given the importance of the foreign currency generated by their operations.

- An integrated financial facility supportive of the non-traditional export sector should be established. The objectives, institutional mechanisms and operating procedures of the SDRF should be redesigned in order to provide a more comprehensive rehabilitation financial tool that will assure positive results.

- Consideration should be given to the mechanism which already exists in FONDEI.

APPENDIX

Scope of Work

USAID/Honduras requires the services of an outside expert consultant to determine whether its objective of promoting non traditional exports is being achieved through a Special Debt Restructure Fund (SDRF) set up by the Mission and the GOH at the Foundation for Investment and Exports Development (FIDE).

The evaluation will consider the adequacy of the current strategy vis-a-vis the alternative uses of the resources programmed for the SDRF within the scope of the Export Development and Services Project.

The consultant will:

- Review all the material available with USAID/Honduras on the SDRF and the recent evaluation of FIDE as well as analyze all of the operations undertaken to date, visiting borrowers and reviewing their books as necessary.

- Interview representative officials of FIDE, AID, and the banking and industrial community in order to analyze the actual and projected impact of the SDRF operations in relation to its objectives.

- Prepare a report acceptable to USAID/Honduras indicating his findings and recommendations to better enable AID and FIDE to maximize their export generation objectives under this activity.

- Answer the following illustrative questions:

  -- Did the operations analyzed follow the specified procedures?

  -- Did the operations analyzed meet the required criteria?

  -- What is the impact of the operations in terms of exports, financial viability and employment creation?

  -- Compare the projections (exports, financial ratios, employment) expected of the firms with restructured debt under the SDRF with the likely trend that could have been expected without the restructuring.

  -- How do the benefits realized from the SDRF operations compare with the alternative of financing credit worthy non traditional exporters? How limited is the availability of medium credit for otherwise credit worthy non traditional exporters?

  -- Based on the findings what are the lessons learned and what specific recommendations can be provided?