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Review of HIAMP as a Vehicle
for Promoting Investment in
Non-Traditional Agricultural
Exports

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

REVIEW OF HIAMP AS A VEHICLE FOR
PROMOTING INVESTMENT IN NON-TRADITIONAL AGRICULTURAL EXPORTS

Bureau for Program and Policy Coordination
Center for Development Information and Evaluation (CDIE)

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EXECUTIVE SUMMARY

Review of HIAMP as a Vehicle for Promoting Investment in Non-Traditional Agricultural Exports PPC/CDIE

The objective of this review is to provide a comparative perspective on the High Impact Agricultural Marketing and Production (HIAMP) Project in light of related project experience of A.I.D. in the area of promoting investment in non-traditional agricultural exports. CDIE recognizes that the conclusions and recommendations of this "desk study" should be assessed, and may need to be revised, in the light of the LAC Bureau's field evaluation of HIAMP and future field assessment.

The HIAMP Project is clearly a high-risk venture in which there are potential large rewards but also potential major pitfalls including the risk of failure (e.g., loss of project funds invested by the Agricultural Venture Trust (AVT)). The greater risk, however, is the significant negative consequence of failing to undertake constructive initiatives in the Eastern Caribbean (EC). The justification is the political, economic, and human importance of supporting development in the EC.

HIAMP proceeded on a largely ad hoc or "rolling design" basis. As a result, there is no longer a clear understanding of how the project's components fit together to achieve the project's goal, purpose, and outputs. In light of how the project has evolved, the rationale for HIAMP as a "cluster" project, combining Quick Response Activities (QRAs), Major Subproject Activities (MSAs), and a Core Contractor (CC), no longer holds. It may be appropriate for RDO/C to formally disaggregate HIAMP into separate, independent projects.

A major concern identified is the question of whether the current arrangements associated with the creation, operation, and oversight of the Agricultural Venture Trust (AVT) raise the possibility that AID, inconsistent with legislation and policy, may in effect be taking on the responsibilities and consequences associated with holding an equity position in private sector enterprises. A firm conclusion on this point requires determination by legal counsel.

Another consideration is the adequacy of the AVT as an equity financing mechanism. Review of venture capital project experience suggests that the institutional prerequisites for a venture capital operation are not present in the AVT as currently implemented. Also, the decentralized management structure of the AVT has been an obstacle to efficient implementation of QRAs, adequate accounting for outputs, and measuring impact. There is a need to reassess the adequacy of the AVT as a financing mechanism and to define an appropriate management structure.

Consideration of constraints in the EC suggests that several obstacles to reducing investment risk were underestimated. The disappointing results of other agricultural export promotion projects in the EC point out that binding constraints, other than financing, frustrated project efforts to develop agribusiness.

Given these high risks and assuming that legislative, policy and structural issues are addressed, RDC/C should view the AVT as a pilot demonstration project and limit its scope and expectations. The level of project resources for the demonstration should be consistent with that required of a pilot activity. Adequate documentation of the experience with the AVT will be necessary if this activity is to help guide future programming on export development.

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Review of HIAMP as a Vehicle for
Promoting Investment in Non-Traditional Agricultural Exports

I. Introduction

A. Objective of Review

The objective of this review of the High Impact Agricultural Marketing and Production (HIAMP) Project is to provide a comparative perspective on HIAMP in light of related project experience of A.I.D. in the area of promoting investment in non-traditional agricultural exports. This experience is reviewed in relation to a number of design and implementation issues identified in the course of learning about HIAMP.

This review was not carried out as a field evaluation of HIAMP, but rather as a basis for providing A.I.D. with a preliminary analysis of the project's design and implementation experience relative to the experience of similar projects. At the time this review was prepared, A.I.D.'s LAC Bureau conducted a field evaluation of HIAMP. It is hoped that the present report will serve as a useful complement to that evaluation.

B. Methodology

The study was conducted as a "desk review" of project documentation, supplemented by interviews with Agency personnel. Documents reviewed included the PID, PP, Project Authorization, Grant Agreements, Implementation Letters, and related cables and memoranda. Additionally, based on a library search to identify related projects and documentation, this review incorporated relevant experience from other projects.

It should be emphasized that CDIE's review of the HIAMP Project was a "desk study" carried out concurrently with a field evaluation of HIAMP conducted by the LAC Bureau. CDIE recognizes that the conclusions and recommendations set forth in this review should be assessed, and may need to be revised, in the light of the LAC Bureau's field evaluation of HIAMP and future field assessment. The present review provides a preliminary assessment of HIAMP based on the information available at the time this CDIE review was conducted.

C. Organization of Report

The report is organized in five sections. After the Introduction (Section I), Section II discusses the rationale for and provides an overview of A.I.D. support for investment promotion in non-traditional agricultural exports. Section III examines the HIAMP Project in terms of key issues surrounding the Agricultural Venture Trust (AVT) and HIAMP's overall project design. Key issues relating to the AVT are: (1) nature and objectives of the AVT as a financial mechanism; (2) consistency of the AVT with legislation and policy; (3) constraints to investment promotion and non-traditional agricultural exports in the Eastern Caribbean; and (4) management, accountability, and benchmarks. Key issues relating to overall project design are: (1) the cluster concept and coherency, and (2) accountability. The study's conclusions are presented in Section IV, followed in Section V by a statement of recommendations.

II. Rationale for and Overview of A.I.D. Support for Investment Promotion in Non-Traditional Agricultural Exports

A.I.D. has placed increased emphasis in recent years on projects that aim to strengthen the capability of developing countries to compete in non-traditional agricultural export markets. One such initiative has been the High Impact Agricultural Marketing and Production (HIAMP) Project of A.I.D.'s Regional Development Office for the Caribbean (RDO/C). The potential importance of HIAMP to the Eastern Caribbean (EC) may be appreciated by a "lesson learned" statement made in the evaluation of two other agribusiness projects in the region: "The most successful agribusiness sub-projects in the Eastern Caribbean...have all been exporting products to market niches in industrialized countries" (L. Berger, Executive Summary, p. 18).

A. Brief Description of HIAMP

The project components of HIAMP include Major Subproject Activities (MSAs), Quick Response Activities (QRAs), and a Core Contractor (CC) that has responsibility for providing technical support for project implementation. According to the PP, the project purpose is:

To increase the contribution of...agricultural enterprises to GDP by improving the investment environment, relieving development constraints to private capital inflows and demonstrating attractive returns on capital at acceptable levels of risk.

A key project activity, the Agricultural Venture Trust (AVT), is being implemented under the project's QRA component.

B. Non-Traditional Agricultural Exports

The impetus for A.I.D.'s concern with non-traditional agricultural exports lies in the Agency's interest in finding new ways to respond to the problems and opportunities facing many developing countries. Limited size of domestic food crop markets in developing countries, decline in traditional agricultural export markets, and the growing need of many developing countries to find new ways to earn foreign exchange have led these countries to seek to develop their potential to compete in non-traditional agricultural export markets.

A.I.D. has supported a number of projects aimed at developing host country or regional capability to market non-traditional agricultural export crops. The HIAMP Project is one such project. Other examples of non-traditional agricultural export projects include:

- Guatemala Agribusiness Development
- Honduras Export Promotion and Services
- Jamaica Agro-Industrial Development Project
- RDO/C Agribusiness Expansion Project
- ROCAP Non-Traditional Agriculture Export Support Project
- Jamaica Agro-Industrial Development Project

A review of some of these projects' experience provides a comparative perspective for analyzing the potential of HIAMP to strengthen non-traditional agricultural export capability.

C. Investment Promotion and Equity Investment

Investment promotion and, to a lesser extent, equity investment have been increasingly important components of A.I.D. projects. One reason is that some types of enterprises, such as agricultural producers, are denied access to loan financing because they lack well-developed business plans or sufficient collateral to satisfy lending institutions or potential investors. The provision of investment promotion services or equity investment would serve to release this constraint. Moreover, there is less long-term loan financing available in many developing countries, given an increasingly competitive financial environment, in which sectors other than agriculture dominate access to credit.

Long-term credit and investment have been in short supply for major start-up or expansion in non-traditional agricultural export crops. Equity investment has been used in a small number of A.I.D. projects as a means to stimulate or "kick start" start-up or expansion of agricultural ventures. Additionally, equity investments may also serve to strengthen the capability of private sector firms to attract financing from other investors.

A.I.D. has supported a number of investment promotion and equity investment projects. In addition to HIAMP, other examples of investment promotion projects have included:

- Belize Export and Investment Promotion
- Caribbean Basin Investment and Trade Promotion (CIPS)
- Dominican Republic Export and Investment Promotion
- Haiti Export and Investment Promotion
- Jamaica Technical Consultations and Training
- Peru Private Sector Agricultural Investment Promotion
- RDO/C Project Development Assistance Program (PDAP) and follow-on Investment Promotion and Export Development

A.I.D.-funded projects with an equity investment component include:

- Regional Agribusiness Development Project
- Costa Rica Private Investment Corporation
- Jamaica Private Development Bank
- Kenya Private Enterprise Development
- Panama Private Export Finance (FIDESIA)
- Sri Lanka Private Sector Development Program
- Thailand Venture Capital Limited

Experience drawn from some of these projects provides a comparative perspective for analyzing the potential of HIAMP's QRA component (including equity investment) to contribute to the strengthening of non-traditional agricultural export capability.

III. Key Issues

Based on CDIE's review of related project experience, a number of issues and questions may be raised about the Agricultural Venture Trust (AVT) in particular and HIAMP's overall project design.

A. The Agricultural Venture Trust (AVT)

1. Nature and Objectives of the AVT as a Financial Mechanism -- Is the AVT a pilot demonstration or an institution-building initiative?

The Agricultural Venture Trust (AVT or Trust) is currently the principal institutional mechanism for financing HIAMP's Quick Response Activities (QRAs). AVT objectives include: administering the Quick Response Fund (QRF); making equity investments in for-profit agricultural enterprises; granting on a reimbursable basis funds for capital goods, management training, and technical assistance to not-for-profit enterprises; granting funds on a non-reimbursable basis; and contracting a financial institution to manage the investment fund and participate on the board of directors of recipient enterprises.

HIAMP conceived of equity investments and grants by the AVT as a means to relax the financial constraints on export-oriented agricultural enterprises in the EC. These investments were aimed at reducing the risks for commercial banks and investors reluctant to make financial commitments to agricultural producers. Over time, the complex logistics of shaping the Trust into an efficient vehicle for equity investment has made "venture capital" a primary focus of HIAMP. To some extent, the effect has been for venture capital concerns to overwhelm the project purpose.

Venture Capital: Recent Project Experience

A.I.D.'s experience with venture capital activities is both recent and experimental, limited principally to project development in Kenya and Thailand. There is considerable confusion throughout A.I.D. as to what actually constitutes "venture capital." As the AVT has been characterized by some as a venture capital initiative, an important question for HIAMP is whether the AVT really constitutes a "venture capital" undertaking?

The term "venture capital" refers to a variety of investment vehicles. The essence of this type of equity financing is high risk for high return (OECD, pp. 27-28). Also, "the main objective of the venture capitalist is to realize capital gains once the venture is more mature" (OECD, p. 28).

Venture capital (VC) is a form of financing which provides risk capital for long-term investment for companies in early stages of development. The major distinction between VC and more conventional forms of financing is that the venture capitalist usually maintains control over his investment by actively participating in the management of the company (Arthur Young, p. 1).

Venture capital project activities of A.I.D. and the International Finance Corporation (IFC) suggest that the AVT has a number of deficiencies as a venture capital initiative relative to other venture capital experiences. Firm conclusions cannot be drawn since none of these activities have gone through the full venture capital cycle (identification, investment, nurturing, divestment, and distribution to shareholders). Nonetheless, certain generalizations from A.I.D. and IFC experience are relevant to HIAMP's experience with equity investment.

Risk Sharing with Local Investors

An important basis for venture capital firms is the mobilization of capital from commercial banks, insurance companies, pension funds, and other financial institutions. Equity from local investors in LDCs is anticipated to be a principal source of capitalization of the equity capital firms supported by A.I.D. in Kenya and Thailand, and by the IFC elsewhere. An IFC review

of its venture capital operations found that no company in which the IFC had invested had a single dominant shareholder (OECD, p. 31). When local investors make an equity investment in a venture capital firm in an LDC, there is a greater incentive for the firm to invest its capital so as to maximize capital gains.

In the case of the AVT, the financial risk for the venture capital firm is not shared with local investors. This risk is assumed principally by A.I.D., even though legal responsibility for the equity investments is transferred to the AVT. The project's original design proposed that the Caribbean Financial Services Corporation (CFSC), a for-profit organization, would manage a so-called "Equity Fund" and would "contribute 15 percent of its annual net profits to the Equity Fund" (PP, p. 34). But the project was subsequently implemented without the participation of CFSC, and the design of the QRA implemented by RDO/C did not provide for any other investor to contribute equity to the AVT. The only contribution made by other investors is that which the firm receiving equity from the AVT makes in its own venture.

Sole grant funding from A.I.D. to a charitable trust responsible for making equity investment does not provide a suitable incentive structure for venture capital activities. Even though the Trustees and the Management Services Contractor (MSC) are legally responsible for executing and managing the equity investments respectively, they assume no financial risk for taking an equity investment in firms.

Operational Basis for Venture Capital

Incipient venture capital operations typically have an operational capacity to generate revenue, either in the form of fees for services rendered, interest on idle cash balances, or long-term capital appreciation. The A.I.D.-supported venture capital company in Thailand anticipates generating revenues from investment banking fees associated with its project development role and from capital gains. In Kenya, the A.I.D.-supported venture capital firm anticipates generating revenue from project development and management fees charged to entrepreneurs and investors, respectively, as well as indirect start-up support from A.I.D. The IFC review found that the venture capital firms in which they have invested "have generally managed to generate sufficient operating revenue to cover their overheads and thus avoid operating losses" (OECD, p. 30).

In contrast, the AVT, a not-for-profit trust, did not have any built-in institutional capacity to generate revenue. A.I.D. covered the project development expenses for the equity investments, through its support to the CC, and covered the management fees for the Trust, by financing the MSC. HIAMP anticipates that the Trust will generate capital gains in the long term, when shareholders of invested firms buy-back the equity at an appreciated value after five years. The Trust will also receive reflows from reimbursable grants.

Structure for Managing Equity Investment Portfolio

Poor performance of equity investments by venture banking operations is often associated with passive involvement in management of these equity investments. A critical ingredient in successful venture capital companies has been adequate technical and managerial support to small businesses (OECD, p. 30, 43).

The AVT's management structure, with multiple institutional actors, complicates the approval process and is a disincentive to providing long-term management support to firms receiving equity investments. At present, four institutional actors currently serve clients: (a) the Core Contractor (CC) assists in the preparation of business plans for equity investments; (b) the RDO/C Mission reviews and, if acceptable, approves individual investment proposals; (c) the MSC reviews the proposals, advises the AVT in its negotiation of equity investments, and subsequently manages equity investments approved by RDO/C and the Trust; and (d) the AVT approves equity investment arrangements.

However, the MSC has little incentive to provide the high level of technical and managerial support required, as its fixed fee income is not directly related to the future appreciated value of the Trust. Further, the Trust is only benefitting from part-time management support from the current MSC, as this firm is not able to devote more than 30 percent of its time to AVT-related work. This seems a convoluted arrangement in which the institutions involved have insufficient financial incentive to manage the equity investments effectively.

Also, the change in institutional vehicles to manage the Trust, from a local financial institution (CFSC) to the newly-created AVT, resulted in a situation in which the financial mechanism for the QRAs (i.e., the Trust) had little, if any, financial and administrative capacity to manage equity investments. The original intent in proposing CFSC as the organization that would manage the QRAs was to have an administrative capacity in development finance and an ability to comply with AID's burdensome administrative requirements. The AVT has Trustees with a high level of professionalism and a strong Caribbean representation. But the Trust is limited by the fact that it has only recently been formed and has to rely on an outside contractor for technical and financial oversight of investment development and followup. Also, unlike a development bank, it is unable to draw on opportunities which arise in the course of loan activity.

Finally, the commercial banker and lawyer composition of the Trustees makes for a highly risk-averse, conservative administrative structure, not conducive to equity risk-taking. The AVT's non-profit status and its access to grant funds reduce the incentives to develop a revenue-generating capacity and to provide effective long-term management support.

In sum, AVT's decentralized institutional structure, the Trustees' conservative orientation, and the Trust's non-profit status do not constitute an adequate institutional basis for managing venture capital activities.

Volume and Quality of Equity Investments

A review of the IFC's venture capital experience found that several factors appear important to successful projects; these factors include a healthy volume of inquiries, a satisfactory volume of investment, and satisfactory quality of investment (OECD, p. 30). Venture capital investments are commonly based on rapid capital appreciation, and agricultural investments have not figured prominently as a high growth area for venture capital operations in developing countries (OECD, p. 31).

This raises a question of whether non-traditional agricultural exports in the EC constitutes a strong basis for an equity investment portfolio with high long-term yields. HIAMP appears to have had high expectations about the number and the capital appreciation potential of investments in non-traditional agricultural exports in the EC. But the slow growth rate of agricultural production in the EC in recent years, coupled with the experience of Latin American Agribusiness Development (LAAD) and the Caribbean Development Bank (CDB), suggest that agriculture production and agribusiness may not constitute a strong basis for a high yield portfolio. (See section on Constraints.)

As of September 1987, ten business plans for AVT equity investment financing had been developed by the CC and submitted to RDO/C for approval; by January 1988, the AVT had made commitments for six equity investments for a total of US\$ 1.26 million. While these investments appear to be in the area with the greatest potential to be successful non-traditional agricultural export ventures (e.g., ornamentals), it is unclear whether this volume and the quality of the investments involved will continue in the future.

Attention to Obstacles to Divestment

A review of venture capital companies in developing countries found that an important factor influencing the success of venture capital investments is the availability of avenues for divestment (OECD, p. 32). Satisfactory divestment experience was found to be a common characteristic of successful venture capital operations reviewed (p. 30). While this is a common problem for venture capital activities in all developing countries, the problem is not insurmountable. However, it does complicate matters for venture capital operations at the time of valuing the initial investment, issuing new stock, and liquidating equity.

Sufficient attention was not given in the design of HIAMP to the potential obstacles for divestment of equity investments. The project design anticipated that the AVT would realize capital gains in five years, as a result of the liquidation of the equity investments, through a shares buy-back by the firms' shareholders or a sale of stock to other investors. However, several potential problems were underestimated.

First, there is the difficulty of valuing and liquidating equity held by the AVT, given that an equity or secondary market does not exist in the EC. Second, family businesses are commonly unwilling to dilute control of the firm through issuing equity to other investors. Third, the anticipated time frame for capital appreciation appears overly optimistic relative to the experience of venture capital operations elsewhere. Two reviews of venture capital operations in developing countries suggest that a minimum timetable for realizing a return on an initial equity investment is six years before reaching the break-even point, and eight years before reaching profitability (OECD, p. 28).

Other A.I.D. Experience with Venture Capital

As A.I.D. is prohibited by legislation from making equity investments in private sector firms, several venture capital projects developed mechanisms for limiting A.I.D.'s potential liability. In Kenya, A.I.D. distanced itself from liability associated with making equity investments by:

- limiting financial involvement to the making of loans to a level that complemented the equity investments made by local investors, and
- developing an independent venture capital institution fully capable of approving and managing its own equity investments.

A.I.D. has little involvement in the approval and portfolio management of the equity investments made by the venture capital companies in Kenya (PP, pp. 21-22).

In Thailand, A.I.D. is protecting itself by requiring, as a condition precedent to disbursement of A.I.D. loan funds, that:

- local investors make an equity investment in the venture capital firm itself,
- that the anticipated amount of A.I.D.'s loan to the venture capital firm will equal the amount of investor equity in the venture capital firm, and
- that the extent of the equity investment made by the venture capital firm could not exceed 25% of the total cash capitalization (equity plus term debt) of the enterprise receiving the equity investment.

While A.I.D. reserves the right to review and approve the shareholder agreement, investment statement, and operating policies, approval and portfolio management are delegated to the board of directors of the venture capital company (PRE proposal, p. 12).

In the case of HIAMP, A.I.D. made no provision to involve local investors in the financing of the AVT; rather, A.I.D. grant funds are the sole financial support for the Trust. In addition, as HIAMP was not conceived as a private sector institution-building project, little attention was paid to developing an independent venture capital firm fully capable of developing and managing its own equity investments. In legal terms, A.I.D. protected itself from potential responsibility and liability vis-a-vis equity investments through a provision in the equity investment agreement between the AVT and each invested firm. In essence, the provision states that AID can not be construed as a party to the agreement or held responsible or liable to those involved. (See Section on Legislation and Policy Implications for AVT.)

Implications for Agricultural Venture Trust

In sum, the AVT should not be considered a venture capital initiative for a number of reasons: lack of risk sharing by local investors, inadequate operational basis for venture capital, inadequate structure for managing equity investment portfolio, anticipated limited volume and quality of equity investments in the long term, and lack of attention to obstacles to divestment.

A Pilot Demonstration or Institution Building?

While one of HIAMP's outputs was anticipated to be "the establishment of an efficiently managed, profitable venture capital fund," it appears that the institutional prerequisites for a venture capital operation are not present in the AVT as currently being implemented.

HIAMP was never intended to be an institution building project. The project design never provided for any one institutional entity staffed, trained, and supported to take over the work of the venture capital fund (QRF). However, the reality of managing equity investments through the AVT has increased the need for the Trust to strengthen its institutional capacity.

While the capacity of the Trust to manage the equity investments effectively should be reinforced, the serious limitations of the AVT as a venture capital initiative should be fully recognized. As a result, it is more appropriate for the AVT to be considered as a pilot demonstration, with limited scope and expectations.

Promoting Greater Private Sector Assumption of Risk or Parastatalizing Non-Traditional Agricultural Exports?

A venture capital initiative is by its nature a long term and high risk undertaking; agribusiness in the small islands of the EC is particularly high risk. A means of reducing the risk for institutions undertaking equity investment is to involve a diversity of private investors. At the start of the implementation of HIAMP, an evaluation of two agribusiness projects in the EC raised an important question for HIAMP:

Will HIAMP hold to an approach in which private investors control subprojects and bear the larger share of equity risks? ...pressures to show project accomplishment and to move RDO/C funds could result in the "parastatalization" of HIAMP in a number of subtle and not-so-subtle ways (L. Berger, Executive Summary, p. 15).

The experience of the AVT to date suggests that the "parastatalization" of the Trust may already be taking place. First, it is the A.I.D.-financed AVT that bears the risk of the equity it has invested in the enterprises involved. There is no other party holding equity investment in the AVT who, thereby, would also share in the risk of the equity investments made by the Trust. Second, A.I.D.'s involvement, via the AVT, may have resulted in the creation of a highly risk-averse institution, which is dependent on A.I.D., and lacks a capacity for generating revenue and for independent financial decisionmaking. In effect, RDO/C is using a financial mechanism dependent on A.I.D. grant funds to carry out its very high risk objective of promoting non-traditional agricultural exports.

2. Legislation and Policy Implications for AVT -- Is the AVT consistent with legislation and policy that prohibit A.I.D. taking equity positions in private sector enterprises?

Problem

A major component of the A.I.D.-funded HIAMP Project is the provision of grant funds used by an Agricultural Venture Trust (AVT or Trust) to make equity investments in EC private sector enterprises. Examining the arrangements associated with the creation, operation, and oversight of the AVT, two questions arise: Have these arrangements in any way compromised or jeopardized A.I.D.'s liability and responsibility? Is A.I.D., inconsistent with FAA legislation and Agency policy, through RDO/C's involvement in equity investments made by the AVT, taking equity positions in private sector enterprises?.

Legislation and Policy

There is a degree of confusion surrounding FAA legislation and A.I.D. policy regarding A.I.D.'s authority to grant funds to a not-for-profit organization that, in turn, uses the grant funds to make equity investments in private sector enterprises. Some of the FAA legislation and A.I.D. policy that appear to be relevant are summarized below.

The A.I.D. Private Enterprise Development Policy Paper states that A.I.D. "will not take an equity position in a private enterprise" (A.I.D., 1985:13). On the other hand, an A.I.D. legal brief of GC/LP, dated August 20, 1981, states that "AID may not directly purchase equity securities." This implies that A.I.D. is not prohibited from indirectly taking an equity position in a private enterprise.

The prohibition against the Agency "directly" purchasing or taking an equity position in a private enterprise is apparently based on Section 635(g)(3) of the Foreign Assistance Act (FAA) of 1961, as amended, which states:

In making loans under this Act, the President -- ...may acquire and dispose of...any property, including any instrument evidencing indebtedness or ownership...provided that equity securities may not be directly purchased....

Two considerations have been mentioned as rationales for this legislation. First, Congress did not want A.I.D. managing private enterprises in developing countries, that is, involved in micro decisions that could expose the Agency to difficult and sensitive political and social problems. In other words, direct involvement in managing a private enterprise could put the Agency in a position of having to make potentially difficult decisions to lay off workers, close plants, etc. Second, A.I.D. involvement in equity ownership would risk Agency exposure to suits brought by shareholders or others involved in that enterprise, thereby compromising or jeopardizing A.I.D. responsibility and liability.

The question arises whether A.I.D. can use a trust as a financial intermediary for making equity investments. The September 10, 1987, draft Financial Markets Development Policy Paper (FMDPP) states that the "provision of a grant to a trust or trust fund that serves as a financial intermediary for...equity investment is not permitted" (Section V.D.1., at 17). However, a legal brief on the use of trusts as financial intermediaries has not been issued. Nevertheless, a draft legal memorandum of GC/PRE, dated October 16, 1986, states: "The FMDPP's blanket prohibition on equity investments by A.I.D. grantees (trusts and not-for profits) should be deleted."

In other words, an A.I.D. grant to a trust making equity investments in private sector firms would be consistent with legislation and policy as long as the arrangements involved did not violate the intent and spirit of the legislation, that is, that A.I.D. responsibility and liability are not compromised or jeopardized. However, would the prohibition apply: (1) if A.I.D. were involved, albeit indirectly via RDO/C's funding and oversight of the CC, the MSC, and the AVT, in managing the Trust's equity investments; and (2) if RDO/C (A.I.D.) could potentially be held responsible for managing assets with sensitive political or social implications, or potentially could become the subject of litigation?

Even if A.I.D. approves the equity investments, writes the check to the firms, and pays for the management support of the investments, these arrangements appear to be consistent with FAA section 635(g)(3) as long as the A.I.D. funds involved are provided to the trust in a way that constitutes a transfer of legal ownership of the funds. However, the arrangements might be inconsistent with the legislation if the original purposes of the prohibition, as outlined above, were compromised or jeopardized. This might occur if A.I.D. were effectively involved in the operational management of the enterprise receiving equity investments and vulnerable to potential litigation by shareholders, workers, etc.

Arrangements Surrounding AVT

The Regional Development Office for the Caribbean (RDO/C) is using the AVT as the means of implementing HIAMP's Quick Response Activity (QRA). The equity investment development and approval process involves RDO/C, the Agricultural Venture Trust (AVT), a Management Services Contractor (MSC), and a Core Contractor (CC).

A.I.D. originally proposed that the QRA would be implemented by the for-profit Caribbean Financial Services Corporation (CFSC). However, during project review, AID/W expressed concern about the legality of A.I.D. granting funds to a for-profit firm. There was also concern about creating a situation in which CFSC would be placed in a conflict of interest position, whereby CFSC would be managing a not-for-profit, A.I.D.-funded trust at the same time that CFSC would be managing its regular assets.

In authorizing HIAMP, AID/W required, as a condition for obligating funds, that RDO/C submit a new QRA design. AID/W provided guidelines for the design of the trust. The guidelines indicated a requirement for a non-profit organization or trust capable of receiving A.I.D. grant funds, using them to make equity investments in private-sector enterprises, and managing the trust's equity investment portfolio. Further, to avoid conflict of interest, AID/W advised that the trust and the arrangements with the CFSC for trust management should be established in such a way that CFSC would maintain an "arm's length" from the trust.

Based on these guidelines, RDO/C established the Agricultural Venture Trust (AVT), a not-for-profit charity under Barbados law. However, the CFSC decided that it would not be in the interest of CFSC to manage the Trust; this created a need for RDO/C to identify an alternate arrangement for managing the Trust. This led to the arrangement of having a Management Services Contractor (MSC) that would provide trust management services for a fixed fee. The MSC selected, based on competitive bidding is the for-profit partnership of Deloitte, Haskins and Sells/SYSTEMS Caribbean International (DHS/SYSTEMS). Trust management services provided by DHS/SYSTEMS are paid on a fixed fee basis by the AVT.

The Core Contractor (CC) is Eastern Caribbean Agribusiness Development (ECAD), a partnership of U.S. private sector firms. Development Alternatives, Inc. (DAI) is the lead partner. The CC works with potential investors to develop, and present to RDO/C, equity investment proposals complying with the conditions for equity investments under HIAMP's QRA component. Upon approval by RDO/C, the proposal is submitted to the AVT. Once the AVT has approved the proposal, and A.I.D. has approved the agreement between the Trust and the investor for investor buy-back of the equity representing the Trust's investment in the investor's enterprise, A.I.D. issues a check to the investor for the Trust's purchase of equity shares in the investor's enterprise.

Consistency of AVT with Legislation and Policy

In view of the arrangements surrounding the creation, operation, and oversight of the AVT, a concern arises whether A.I.D., inconsistent with legislation and policy, may be taking equity positions in private sector firms, thereby compromising or jeopardizing A.I.D.'s liability and responsibility. Whether this is the case depends on how legal counsel would interpret these arrangements in the light of counsel's interpretation of relevant legislation and policy. The arrangements in question may be summarized as follows:

1. The question has been raised as to whether the AVT was created merely to get around FAA legislation and A.I.D. policy prohibiting A.I.D. from making a grant to a private sector firm that uses the grant funds to make equity investments.

AID/W imposed a requirement that the QRA be administered by a non-profit organization that would receive A.I.D. grant funds to make equity investments in private sector firms. RDO/C implemented HIAMP's QRA component, based on the Mission's determination that the requirement would be met by the Agricultural Venture Trust (AVT), a not-for-profit charity under Barbados law, that held a Management Services Contract with the for-profit firm of DHS/SYSTEMS.

The mechanism chosen by RDO/C to implement the QRA was a trust that did not, being the new arrangement that it was, have an established capability to provide and administer the financial services required to manage a trust. Hence the need to involve another party (MSC). However, the viability of the proposal of having a MSC that would manage the Trust may be questioned in view of RDO/C having previously maintained that CFSC was the only organization in the EC having the capability to provide the financial services that would be needed to manage the Trust.

Thus, there is an appearance that the AVT was created in response to the need to find an alternative way of making equity investment in view of AID/W's unwillingness to approve RDO/C making a grant to the for-profit CFSC; and that the MSC was created in response to the need to find an alternative way to manage the AVT when CFSC, the originally proposed MSC, withdrew.

Implementation of HIAMP proceeded not on the basis of a sound, well thought out design but rather on the basis of an ad hoc or "rolling" design that was designed in reaction to the roadblocks to HIAMP startup and implementation that appeared prior to and following project authorization.

2. AID/W may have unwittingly approved and set in motion a project design that may be inconsistent with FAA legislation and A.I.D. policy prohibiting A.I.D. from making equity investments in private sector enterprises.

A.I.D. approval of the design of the QRA component was required by AID/W as a condition for the obligation of HIAMP Project funds. Paragraph 3 of the July 15, 1986, Project Authorization stated: "No Project funds shall be obligated until the design for the QRA component is approved by AID/W." No record could be identified that RDO/C resubmitted a new "design of the QRA component" to AID/W, that AID/W approved the QRA design being implemented by RDO/C, or that AID/W has ruled that the QRA arrangement being implemented by RDO/C (i.e., A.I.D. making grants to the non-profit AVT that is managed by a for-profit MSC) is consistent with FAA legislation and A.I.D. policy.

A.I.D., albeit unintentionally, may have provided RDO/C with a loophole by means of which the Mission could "fulfill" paragraph 3 of the Project Authorization without ever submitting a "design of the QRA component" to AID/W. On that same date, July 15, 1986, item 5 of State cable 221519 stated: "Subject to RDO/C conformance with the terms and conditions of this cable, the condition to obligation of funds established by paragraph three of the project authorization...is hereby fulfilled."

A.I.D., at the Mission (RDO/C) level, and based on the aforementioned cables, proceeded to redesign and implement the QRA component. However, no record could be identified that RDO/C's design for the QRA was found by AID/W to be in "conformance with the terms and conditions" of State cable 221519.

3. If A.I.D., the sole funding source of the AVT, is not building the Trust as an intermediary financial institution and is, for the sake of expediency, using the AVT as a conduit for making equity investments in private sector firms, this may not be consistent with the intent (spirit) of FAA legislation and A.I.D. policy.

A.I.D., at the Mission (RDO/C) level, following its ad hoc or "rolling" redesign of HIAMP's QRA component, approved the AVT, the Trustees, and the MSC. Aside from the Trustees and A.I.D.'s funding of the Trust, there are no other participants in the AVT. Even if it were decided that the AVT is an initiative worthy of development as an institution, neither the AVT nor HIAMP were intended to be institution-building initiatives.

A.I.D. has been the sole source of funds for the AVT; indeed, there is no element of the AVT that is not A.I.D.-funded. Directly or indirectly, A.I.D. pays:

- a. each AVT Trustee an honorarium, in addition to expenses, per diem, and cost of direct travel to attend meetings of the Trustees;
- b. the Management Services Contractor's fixed fee;
- c. the fees of consultants retained to advise the AVT; and
- d. the Core Contractor who develops the equity investment proposals submitted to the AVT.

The viability of the AVT totally depends on A.I.D. While the inherent nature of equity investment requires the presence of an institution that is capable of owning and managing equity in the long term, there never was any intention of building the AVT into an independent, self-sustaining institution that would have this capability. The AVT, as a result, has little independence apart from the funding provided by A.I.D. Further, A.I.D., via its funding of the AVT, the MSC, the consultants to the AVT, and the CC, as well as via A.I.D.'s involvement in approving equity investment proposals and agreements between the Trust and investors, does not maintain an "arm's length" from the equity investments made by the Trust. AID/W found this to be a problem in the original proposal that the for-profit CFSC would manage the equity investments. Is this any less of a problem when A.I.D. is involved in A.I.D.-funded equity investments made by the AVT?

5. If A.I.D. signs the check for investments authorized by the AVT and the AVT does not have independent capability to issue the check, this arrangement may not be consistent with the intent (spirit) of FAA legislation and A.I.D. policy.

Project documentation implies that A.I.D. issues (signs) the check for grant funds authorized by the AVT for equity investment in an enterprise; and that the check is sent by A.I.D. directly to the investor. The AVT cannot independently make an equity investment without A.I.D.'s prior approval of the investment nor without A.I.D.'s approval of the equity investment agreement which A.I.D. may withhold simply by refusing to issue a check to an investor.

6. In view of the arrangements previously discussed, a question arises whether the pro forma AVT Equity Investment Agreement adequately protects A.I.D. from responsibility and liability.

The pro forma Agricultural Venture Trust Equity Investment Agreement contains a provision which appears to protect A.I.D. responsibility and liability vis-a-vis equity investments made by the AVT. This provision states (p. 24):

13.9 The Parties hereto understand, acknowledge and agree that the Agreement of which this is a part has reserved to AID certain rights such as, but not limited to, the right to approve of the terms of this Agreement, documents related to this contract and the Project of which this is a part. The parties hereto further understand, acknowledge and agree that AID, in reserving any or all of the foregoing approval rights, has acted solely as a financial entity to assure the proper use of United States Government funds, and that any decision by AID to exercise or refrain from exercising these approval rights shall be made as a financier in the course of financing this Project and shall not be construed as making AID a party to the said Agreement. The parties hereto understand and agree that AID may, from time to time, exercise the foregoing approval rights, or discuss matters related to these rights and the Project with the parties jointly or separately, without thereby incurring any responsibility or liability to the parties jointly or to any of them. Any approval (or failure to disapprove) by AID shall not bar the Trust from asserting any right, or relieve the agreeing party of any liability which they might otherwise have to the Trust of AID (emphasis added).

If the AVT were to be dissolved, would the protection implied by this provision lapse, leaving A.I.D. responsible for managing the former Trust's assets and subject to liability vis-a-vis the shareholders in the firms in which the former Trust holds equity? For example, if the AVT had dissolved and one of the firms that received equity investment went bankrupt or defaulted, creditors might attempt to litigate against A.I.D. to gain control of remaining real assets (e.g., real estate).

Conclusion

These six arrangements, when viewed in combination, raise three questions:

1. How "directly" involved is A.I.D. (RDO/C) in making equity investments in private sector firms:
2. Have the arrangements surrounding the creation, operation, and oversight of the AVT in any way compromised or jeopardized A.I.D.'s liability and responsibility?
3. Is A.I.D., through RDO/C's involvement in equity investments made by the AVT, and contrary to FAA legislation and Agency policy, taking equity positions in private sector enterprises?.

There is an appearance that A.I.D. is "directly" involved in promoting, developing, approving, implementing, monitoring, and evaluating equity investments in private sector firms. A.I.D.'s association and close involvement with the creation, operation, and oversight of the AVT suggest that A.I.D.'s support of the AVT may be, albeit unwittingly, inconsistent with the spirit and/or the letter of FAA legislation and A.I.D. policy prohibiting A.I.D. from making equity investments in private sector enterprises.

CDIE has neither the complete information nor the legal expertise required to answer these questions. However, there appears to be sufficient cause, in terms of the arrangements cited above, to warrant that A.I.D. turn to legal counsel, and other expertise as may be appropriate, to examine more carefully the nature and implications of the Agency's support of HIAMP (and the AVT), in order to ensure that A.I.D.'s interests are being well served.

The process involved in designing, authorizing, implementing HIAMP has not been neat and tidy, nor has it been well documented. This process needs to be documented and reexamined to ensure that project components such as the AVT are adequate as well as of a nature with which A.I.D. can comfortably live.

3. Constraints -- Will providing equity remove or relax the prime constraint(s) to increasing non-traditional agricultural exports in the Eastern Caribbean?

HIAMP's purpose is "to increase the contribution of the agricultural sector and...enterprises to GDP by improving the investment environment, relieving development constraints to private capital inflows, and demonstrating attractive returns on capital at acceptable levels." The project assumes that money, technology, personnel, and markets exist for agricultural investments in the Eastern Caribbean, and that market imperfections keep them from getting together. A.I.D.'s role of matchmaker was anticipated to be sufficient to reduce the risk for investors in non-traditional agricultural production for export.

Consideration of constraints in the EC suggests that several obstacles to reducing this investment risk may be beyond the capacity of HIAMP to address. The issue of the severity of constraints relative to the project's purpose was discussed at the DAEC review of the PP:

Does the combination of [these] constraints, which include small scale and wide dispersion of potential production units, infrastructure and transportation deficiencies, policy constraints, and competition from better equipped Caribbean countries add up to too many strikes against the prospects for achieving the goal and purpose? In other words, are the Eastern Caribbean states really ready for this project? (DAEC Issues Memorandum)

Capital as a Constraint to Investment in the EC

Recent agribusiness projects in the EC, such as those executed by the Latin American Agribusiness Development Corporation (LAAD) and the Caribbean Development Bank (CDB), have not had much success in increasing investment in agricultural enterprises, with a few exceptions.

LAAD, well known for its lean management style and success with agribusiness equity investments in Central America, had problems initiating and expanding a significant volume of private agribusiness investments in its principal target area, the EC. In the Agribusiness Expansion Project, LAAD was to emphasize investment opportunities involving non-traditional agricultural products for regional and international markets. While the PP targeted 17 potential subprojects in the EC, LAAD placed a small amount of A.I.D. funds, just over \$1 million, in only four projects. Sixty percent of the A.I.D. funds, nearly \$4 million, went to one Central American country, Belize. Moreover, LAAD was unable to place even half of A.I.D.'s authorized funding of \$8

million in the Caribbean. With the limited volume of bankable projects and the high operational and management expense in the EC, LAAD withdrew its EC representative in Barbados.

The CDB's project experience in the EC was even more disheartening. The CDB was to increase investment in agribusiness enterprises through loans and equity investments. Of the five subprojects financed, four are experiencing serious financial difficulties (L. Berger, Executive Summary, pp. 9-10). Two of LAAD's four EC subprojects are in severe financial difficulty.

A principal conclusion of the evaluation of the two previously cited EC agribusiness investment projects challenges the assumption of the QRA component, as executed by the AVT, that equity investment will be the answer for promoting non-traditional agricultural exports:

the underlying assumption of the two projects that the provision of credit for agribusiness would release a key constraint and result in the establishment of significant numbers of new agribusiness ventures (principally engaged in agroprocessing) proved unfounded. Although USAID provided \$12.5 million for agribusiness credit, there are only three new or expanded viable agribusinesses in the Eastern Caribbean, each of which appear to have had the potential for successful solicitation of commercial credit. The disappointing results of the two projects suggest there are binding constraints to agribusiness in the Eastern Caribbean other than credit which frustrated project efforts.... Earlier thorough evaluation of...[the LAAD project]...might have...led to a decision to loosen the RDO/C's commitment to the agribusiness sector..., due to the numerous binding or inherent constraints on the sector which donor agencies are powerless to relieve (L. Berger, p. 12; emphasis added).

Inadequate Transport and Marketing Infrastructure

The project paper mentions costly and irregular transportation as a constraint to private sector-led agricultural development. "The lack of adequate transportation facilities for inter-island shipments of fresh produce has constrained both intra- and extra-regional market development in the region" (PP, p. 12). HIAMP's designers proposed to address this constraint by conducting a study of transportation requirements, which would form the basis for the design of subsequent project activities.

The question that arises is whether local and foreign investors will be prepared to make equity investments in agribusiness ventures in the EC, if transportation is still an obstacle? Several considerations are relevant.

First, experts familiar with and executing similar non-traditional agricultural export projects cite the importance of refrigerated warehouse and transport facilities for firms exporting perishables. Given the scarcity of such facilities in the EC, this requirement may represent a considerable obstacle to investment in the export of perishables (e.g., passion fruit). Transport and marketing infrastructure was critical to the success of the perishable agricultural export firm financed by the LAAD project. "The most successful project addressed the need for collection, storage and distribution facilities" (L. Berger, Executive Summary, p. 11).

Second, infrastructure variables were found to be important considerations for investors in another A.I.D. investment promotion project in the EC. An evaluation of the Project Development Assistance Program (PDAP) found that "investment decisions in the Eastern Caribbean are based largely on investment climate and infrastructure variables and -- at best -- can only usually be 'facilitated' by the kinds of activities PDAP has undertaken" (SRI, pp. 3-4). Specific problem areas mentioned by investors were "poor transportation links...and a dearth of middle management (primarily technical) expertise" (SRI, p. 23). The evaluation concluded that "too much attention was focused on investment promotion activities before basic policy environment and infrastructure questions were addressed" (SRI, p. 3; emphasis added).

Experience from the Caribbean Regional Integrated Agricultural Development Project also suggests that developing marketing channels for non-traditional crops in the EC has greater risks than for traditional crops. An evaluation found that a majority of project loans supported the cultivation of traditional crops (e.g., bananas and sugar cane) for which there are reasonably good arrangements for inputs and marketing. The evaluation noted the difficulties of promoting non-traditional agricultural production, given the potential constraints, and concluded that it is "probably better to...[concentrate] on situations where input availability and marketing arrangements ...[do not hinder]...profitable use of credit" (Pacific Consultants, p. 4).

While RDO/C is addressing these infrastructure constraints through various projects, HIAMP may have underestimated the effect that inadequate transport and marketing infrastructure may have in identifying and developing viable agricultural export-oriented enterprises. A survey of HIAMP clients found that those receiving marketing assistance were "very concerned about spending their investment to diversifying only to find they do not have a dependable market. They want to know who will help them penetrate the overseas market when HIAMP is finished" (Weatherspoon, 1987, pp. 10-11).

Attitudes toward Commercial Agriculture

Negative attitudes toward commercial agriculture and the overall business climate in the EC appears to be a serious obstacle to implementing HIAMP. One of the problems cited in several evaluations is the lack of local interest in developing commercial agriculture (L. Berger, SRI, passim).

First, the declining returns of plantation-based cultivation (e.g., sugar) and the prevalence of subsistence agricultural production in the EC have not made agriculture an attractive investment. Agricultural land and labor are scarce commodities in the EC, given the competition with tourism for these factors of production. Financial returns from import businesses and tourism in the EC are often more attractive than agricultural exports. In addition, some agricultural exporters, having rising costs tied to the US dollar, have ceased harvesting grapefruit for export to Europe because of declining revenue associated with exporting to non-dollar based economies (L. Berger, p. 29).

LAAD found that very few local businessmen in the EC were willing to risk investing in non-traditional agricultural production, and that those who took risk were not willing to share ownership with outside investors (L. Berger, pp. 14-16). "The officials of LAAD cited the lack [of entrepreneurs] as one of the key constraints in finding suitable projects in the Eastern Caribbean and disbursing funds available" (L. Berger, p. 31).

A related factor, the small family-owned character of EC firms, has already emerged in the course of negotiating the terms of the equity investment. Owners of family firms have been unwilling to have investors from the same island represented on their board of directors; others have withdrawn from the negotiation process completely because they were unwilling to share ownership with outside investors. A representative of the Core Contractor for HIAMP recently commented that:

an...intractable problem that may serve to slow down the process of delivering equity financing to investors is the commercial milieu in the EC. Businesses in the region are small-scale and...characterized by little middle management support (HIAMP Quarterly Report, Oct.24, 1987, p. 7).

The negative attitude toward commercial agriculture, coupled with the lack of economies of scale of family businesses in the EC, does not bode well for these new firms' ability to compete with established Caribbean and Central American producers. Thus, it is not surprising that very few producers in the EC currently export extra-regionally.

Some Implications of Constraints for the AVT

The AVT may have a greater potential to develop viable non-traditional agricultural export enterprises than in the projects examined in the earlier cited evaluations. First, the AVT is concentrating on the product area with the greatest potential for success in the EC. Both the LAAD and the CDB projects found that the subprojects with the best success rate were those supporting export of non-traditional agricultural products to industrialized countries (L. Berger, Executive Summary, p. 18). Second, the AVT has a more comprehensive support structure for the promotion of equity investments than previously was the case. Finally, aside from the investors who receive equity investments, the A.I.D.-funded Trust is the only party that is placing funds at risk in equity investments made by the Trust. This was not the case either for LAAD or the CDB who assumed financial risk as external institutional investors.

As a further consideration, the previously-cited evaluation of two agribusiness projects in the EC raised an important question: "Will enough investors come forward to invest in new or expanded agribusiness activities to justify the magnitude of the resources programmed for the [HIAMP] project?" As of September 1987, ten business plans had been developed by the CC and submitted to RDO/C for approval; by January 1988, the AVT had committed six QRF investments for a total of US\$ 1.26 million. While these investments are in product areas having the greatest potential for successful non-traditional agricultural export ventures, it is unclear whether this volume and the quality of these investments will continue in the future.

4. Management, Accountability, and Benchmarks

Three other issues also emerged in reviewing the AVT: management of, accountability of, and benchmarks for the AVT. Based on the documentation reviewed, it becomes clear that:

- With respect to management, the project's decentralized structure for managing the AVT has become an obstacle to efficient implementation of the Quick Response Activities;
- With respect to accountability, the project lacks a clearly designated delegation of authority and responsibility for achieving project outputs, in view of the multiple number of actors involved (e.g., RDO/C, Core Contractor, Management Services Contractor, Agricultural Venture Trust); and
- With respect to benchmarks, that the project, given its track record of implementation via ad hoc or "rolling" design, has not established realistic, clearly-defined benchmarks upon which project progress can be monitored.

Management -- HIAMP's decentralized management structure has proven to be an obstacle to the efficient implementation of the QRA component. At present, four institutional actors currently serve clients: (a) the Core Contractor (CC) assists in the preparation of business plans for equity investments; (b) the RDO/C Mission reviews and, if acceptable, approves individual investment proposals; (c) the MSC reviews the proposals, advises the AVT in its negotiation of equity investments, and subsequently manages equity investments approved by RDO/C and the Trust; and (d) the AVT approves equity investment arrangements.

As a representative of the CC stated recently, "In spite of good intentions, the organization structure encourages delays and iterative charges that "one or the other is not doing their job well enough or too well" (Mickelwait, Oct. 29, 87, p. 2). The issue of HIAMP's decentralized management structure has been recognized by RDO/C and the other parties, and preliminary steps have been taken by the Mission to address the problem (RDO/C Mission Director cable 07717 of 9/18/87 to Karl Schakel of Western Agri-Management Company; 11/3/87 memo from RDO/C Mission Director to AA/AID).

Accountability -- To the extent that the AVT is not fully independent, being financially dependent on A.I.D. grant funds, technically dependent on the CC, and administratively dependent on the MSC, there is confusion regarding who is accountable for achieving project outputs.

For example, who is responsible for managing the equity investment portfolio: the Trustees (or future administrative staff) of the AVT, the employees of the MSC, the technical assistance team of the CC, or even RDO/C? This is especially problematic because the CC is now primarily responsible for the development of the equity investments. The Core Contractor's role vis-a-vis equity investments, as compared with that of the MSC or the Trustees, has been greatly expanded. There is a potential conflict of interest if the CC is assisting the AVT to manage the very same equity investments which the CC is developing. The conflict of interest situation may be aggravated by the fact that the CC has staff on each of the islands, while the AVT does not. Looking down the road, who will manage the portfolio at the end of the project?

Benchmarks -- The manner in which the QRA component is being implemented is significantly different from the design in the PP. Further, there have been significant delays in establishing the AVT and in developing and implementing QRAs. Thus, HIAMP has not moved forward at the rapid ("quick") pace assumed in the PP. This raises a question of benchmarks, of what may reasonably be expected of the AVT in terms of meeting the project's inputs, outputs, purpose, and goal.

For example, the PP anticipated an aggregated internal rate of return of 56% to subprojects (PP, Annex O, p. 3). However, discussions with the LAC evaluation team indicated that the current anticipated rate of return on subprojects visited is in the order of 20%. This suggests that the PP may have made unrealistic projections about anticipated returns. In light of this reduced rate of return and the small number of equity investments financed by other investors in the EC, the benchmarks for the AVT (number of investments per year, rate of return, etc.) may need to be reassessed.

Another concern for the benchmarks issue arose in the light of the experience of the two Caribbean agribusiness projects:

All the sub-projects evaluated had difficulty meeting the targets set for them.... In most cases, the shortfall had less to do with the capabilities of the implementors, and much more to do with inflated forecasts.... ..inflated forecasts [have] plagued many RDO/C private sector projects, and is clearly related to the "selling job" required for donor funding. ... The [sub-project] appraisals lack a fundamental sense of reality, and an understanding of the dangers and opportunities for investors...(L. Berger, Executive Summary, p. 17).

B. Overall Project Design

1. The Cluster Concept and Coherency -- Is HIAMP currently structured as a coherent project?

"The HIAMP project is the centerpiece of the RDO/C's cluster concept" (PP, p. 4). The "cluster concept" approach to project management is that of using a core contractor to manage a group of project activities in the same programmatic area (e.g., non-traditional agricultural exports). HIAMP's design conceived of the Core Contract as a vehicle for contracting out specific project activities (e.g., research activities) to different institutions, while freeing up overburdened RDO/C staff to focus on policy, institutional links, and overall effectiveness. Also, the RDO/C staff limitations, the difficulties of managing project activities in a number of small islands from a Barbados base, and the need for programmatic coherence made the cluster approach appealing.

Problems arising during the project's implementation suggest that HIAMP went beyond the cluster concept. A common thread in these problems is the perception that HIAMP was not conceived as a project but as an open-ended Mission program with the potential to do any number of things in any number of areas. This "basket approach" has both strengths and weaknesses. Previously, AID/W had raised the issue that "the costs and benefits of the core contractor approach were difficult to assess and that procedural and policy problems might arise" during the review of the RDO/C Action Plan for FY86/87 (PP, p. 21).

HIAMP's project implementation experience suggests that the project design may have held unrealistic expectations as to what the CC and RDO/C could effectively manage. Examples include:

- Four Major Subproject Activities (MSAs) were originally envisaged in the project design. Two are on track but the other two are postponed and under discussion (Windward Islands Tropical Fruit and Leeward Islands Crop Diversification Subprojects). The existing MSAs currently operate independently of the CC who no longer has any responsibility for managing design teams for MSAs or doing "reality checks" on the management of MSAs. Now the priority of the CC is to follow through with the equity investment projects that the CC helped to prepare.
- Over time, RDO/C has found that a significant number of A.I.D. staff are still needed to oversee this project. The Mission Director has two direct hire staff assigned full-time to the project, and another part-time. In addition, the Mission Director is closely monitoring performance.

In effect, HIAMP has not been a coherent project. The "project" now consists of activities which are highly unrelated relative to what the PP originally envisaged. Two fundamental questions arise:

First, with respect to the Major Subproject Activities (MSAs), if MSAs now operate independently of the CC, what is the rationale for continuing the MSAs as subprojects of HIAMP?

Second, with respect to the CC, does limiting the role of the CC to that of supporting the QRAs undermine the concept of having an overall CC as the agent for implementing RDO/C's cluster initiative?

As HIAMP is being carried out as a decentralized project, with the MSAs operating independently of the AVT, there is no rationale for the MSAs to continue as part of HIAMP or for the CC to manage HIAMP as a whole. Unlike the AVT, MSAs are primarily commodity-specific technical assistance projects without an equity investment component. Also, they are relatively large-scale projects based on a different project design and a different group of executing institutions in each case. Finally, MSAs operate as shadow projects, essentially independent of the traditional mission tracking system, which increases the potential for lack of accountability.

In light of these various considerations and the evolution of the AVT, there is a need to rethink what the role of the CC is (or should be) relative to the AVT and HIAMP. For example, what are the budget implications of the Core Contractor's new role?

2. Accountability -- Given the lack of coherence in HIAMP's structure, has the project's multi-faceted character resulted in a lack of clear priorities and benchmarks for evaluating project performance?

One of the advantages of a multipurpose project which combines several activities under the charge of a Core Contractor is that the project is sufficiently flexible to respond to opportunities and requirements as they arise. For example, the management implications of bilateral programs in the EC operating independently of regional initiatives is a justification for increasing management flexibility. Managing a regional project requires flexibility to respond to country-specific concerns; this approach can make use of scarce professional resources for a variety of tasks. Also, as HIAMP aims to stimulate equity investments, flexibility in approach may be an essential requirement.

However, a fundamental limitation of this "basket approach" is that these multiple activities have different objectives, which increases the difficulty in developing clear guidelines, particularly indicators for monitoring and evaluating project performance. Evaluators of the PDAP, a similar Caribbean-based, investment promotion project having a central contractor management structure, found that "the disadvantage [of the multipurpose character of the PDAP model] is that the ultimate mission of the project team is mixed, leading to lack of clarity on priorities and evaluation criteria, and an inadequate skill mix for certain assignments" (SRI, p. 9). The evaluation also found that personality conflicts and questions about internal control over the project led to lack of coordination and direction (SRI, p. 13).

Integrated rural development projects, commonly "multi-pronged, coordinated efforts," have suffered similar problems. A review of A.I.D.'s experience with these projects found that

lack of coordination was a major malaise affecting most of the projects. Dispersion of responsibilities and decision making often paralyzed project management, when the centralization of control over project funds in a single lead agency delayed disbursements to appropriate agencies and organizations responsible for completing individual activities (A.I.D., 1987, p. ix).

It may be preferable to rethink accountability in the HIAMP project in terms of separate projects rather than as a project as a whole.

IV. Conclusions

A. General

1. The HIAMP Project is clearly a high-risk venture in which there are potential large rewards but also potential major pitfalls including the risk of failure (e.g., loss of the project funds invested by the AVT in agricultural enterprises). However, the greater risk would be the potentially significant negative consequences of failing to undertake constructive initiatives in the EC.

The justification for supporting a high-risk venture such as HIAMP is the political, economic, and human importance of finding ways to support economic and social development in the EC. A question still open to debate is whether non-traditional agricultural exports is the best way to stimulate development in the EC context.

2. A project can take either a "blueprint" or a "rolling design" approach to implementation. HIAMP proceeded on a largely ad hoc or "rolling design" basis. As a result, there is now some confusion about how the project's components fit together to achieve the project's goal, purpose, and outputs. Consequently, the project now lacks defined benchmarks upon which project progress can be monitored.

There is a lack of documentation (e.g., PP Amendment, Mission Cable to AID/W) that comprehensively sets forth the project's goal, purpose, outputs, and inputs, as well as the key actors and the strategy and operational procedures to be followed in implementing the project. Memos written by the Core Contractor have attempted to set forth a revised strategy and operational procedures to be followed in implementing the project. However, the strategy and procedures to be followed, as well as the actors to be involved, have changed from one memo to the next. This is a continuation of the same problem that occurred during the "rolling design" of the project from the time of the PID, to that of the PP, to that of authorization, and beyond.

B. Agricultural Venture Trust (AVT)

1. A major concern identified in reviewing HIAMP has been the question of whether the Agricultural Venture Trust (AVT) is consistent with FAA legislation and Agency policy that prohibits A.I.D. taking equity positions in private sector enterprises. The current arrangements associated with the creation, operation, and oversight of the AVT raise the possibility that AID may, in effect and inconsistent with legislation and policy, be taking an equity position in private sector enterprises. However, a firm conclusion on this point requires a determination by legal counsel.

2. The AVT is not a venture capital activity. Review of venture capital project experience suggests that the institutional prerequisites for a venture capital operation are not present in the AVT as currently implemented. HIAMP's experience to date suggests that the AID-financed AVT, not local private investors, will bear a large share of the equity risk. Further, the risk-averse character of the mechanism (AVT) created by A.I.D. is inconsistent with the high risk character of RDO/C's non-traditional agricultural export financing objectives for the EC. There is still considerable confusion as to the appropriate mechanism for equity investment in the EC.
3. Consideration of constraints in the EC suggests that several obstacles to reducing investment risk were underestimated. Experience with other agribusiness investment projects in the EC challenges HIAMP's assumption that equity investment will be the answer for promoting non-traditional agricultural exports. The disappointing results of other agricultural export promotion projects in the EC points out that binding constraints, other than financing, have frustrated project efforts to develop agribusiness in the region. Problematic constraints have included inadequate transport and marketing infrastructure, and negative attitudes toward commercial agriculture.
4. Given these high risks, the AVT should be viewed by RDO/C as an experiment or pilot demonstration, with limited scope and expectations.

If RDO/C could first demonstrate, on a small-scale basis, the feasibility of exporting non-traditional agricultural products from the EC, then RDO/C could explore how to institutionalize this export capability. An alternative approach would be to conduct studies to identify and analyze the existing constraints. However, there is a risk that this approach might only yield inconclusive results without practical application. On the other hand, an experiment or pilot demonstration that is closely monitored and evaluated provides a basis for "learning by doing."

5. The decentralized structure for managing the AVT is an obstacle to efficient implementation of ORAs, adequate accounting for project outputs, and measuring impact.
 - a. Management--The problem here is that a multiplicity of actors (RDO/C, Core Contractor, Management Services Contractor, and the AVT) has severely slowed development and approval of equity investments. There is a clear need to rationalize the number of actors involved, to delegate the required authority to make decisions to key actors, and to streamline the operational procedures to be followed.

- b. Accountability--The problem here is the question of who (Management Services Contractor or Core Contractor's Island Advisors) is to be responsible for managing the portfolio of equity investments during the life of the project and beyond.

If the AVT is an experiment or pilot demonstration, there is a question of how long the demonstration must be run in order to show that non-traditional agricultural exports can develop a profit-generating ability that would ultimately enable them to buy back the equity held by the Trust.

- c. Benchmarks--The problem here is the lack of realistic, clearly-stated benchmarks against which to measure the project's implementation progress.

C. Overall Project Design

1. HIAMP does not hold together as a coherent project. In light of how the project has evolved, the rationale for HIAMP as a "cluster" project, combining Quick Response Activities (QRAs), Major Subproject Activities (MSAs), and a Core Contractor (CC), no longer holds. For example, HIAMP includes initiatives (e.g., the Cocoa and Mariculture Subprojects) that would otherwise stand alone as projects, while other MSAs have been cancelled.

As HIAMP is being carried out as a decentralized project, with the MSAs operating independently of the AVT, there is no rationale for the MSAs to continue as part of HIAMP or for the CC to manage HIAMP as a whole.

2. There is considerable confusion regarding which actors are to play which roles in implementing HIAMP. The role of the CC has evolved into something quite different from that envisaged in the PP. Rather than the CC assisting in design and oversight of the MSAs as well as developing QRAs, the CC no longer has any responsibility for the MSAs. Now, the CC's role is limited to developing and following through on the QRAs (i.e., the equity investments made by the AVT).

Yet there are at least two proposals circulating that demonstrate a lack of agreement about who should be doing what. One proposal suggests that the CC work closely with the MSC in the management of the AVT's equity portfolio, while the other suggests that the AVT terminate its contract with the MSC and brief up the Trust's own technical and administrative staff. If these issues are not sorted out, there is a danger that HIAMP, albeit a demonstration, will demonstrate only failure. Or that it will not be clear what it is that has been demonstrated or what project inputs were effective in achieving which project outputs.

3. The reduced number of MSAs, the changed role of the CC, and the delays in implementing QRAs suggest that HIAMP is authorized at a funding level in excess of the level of funds that the project needs to operate at its currently reduced level of activity. If the role of the CC no longer includes providing short-term technical assistance for the design and monitoring of MSAs, there may be a need to reallocate some of the \$10 Million for Core Contractor's budget to ensure that there are adequate funds for short-term technical support for the remaining MSAs.

V. Recommendations

A. Agricultural Venture Trust (AVT)

1. That legal counsel be requested to determine whether the arrangements for the AVT to make equity investments in private sector firms are not inconsistent or contrary to FAA legislation and/or A.I.D. policy prohibiting A.I.D. from taking equity positions in private sector firms.
2. That RDO/C view HIAMP's QRA component, albeit implemented through the AVT or an alternate mechanism, as a high risk experiment or demonstration of the feasibility and profitability of non-traditional agricultural exports.
3. That RDO/C fully define and adequately document the strategy and requirements for conducting the QRA component as a demonstration. Potential requirements include, but are not necessarily limited to, the following: number of equity investments, operational procedures (e.g., making equity investments, equity buy-back from the AVT), staffing, and establishment of realistic benchmarks.
4. That RDO/C obtain specialized technical support:
 - a. to reassess the adequacy of the QRA financing mechanism and to make specific recommendations relevant to designing and implementing a pilot demonstration; and
 - b. to define an appropriate management structure to implement the QRAs, to account for outputs and performance, and to document performance indicators.
5. That the level of project resources for the demonstration should not exceed the level required of a pilot activity.

6. That the AVT (or alternate mechanism), as a pilot demonstration, should be closely monitored, documented, and evaluated by an external review team. Criteria should be developed to assess the lessons learned from the pilot demonstration and, in particular, should include the effect of constraints on non-traditional agricultural exports and the factors which contribute to success of equity investments.

B. Overall Project Design

1. That RDO/C formally disaggregate HIAMP as a "cluster project" into separate, independent projects, including each of the Major Subprojects and the Quick Response Fund currently executed by the AVT.
2. That RDO/C redefine the role of the CC, given the considerable confusion regarding the roles of the actors in implementing the project as a whole and in implementing the QRAs in particular.
3. That a revised funding level for each of the project components of HIAMP be prepared, which reflects the anticipated level of effort of each component.

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