

HEALTHlink

A PROGRAM OF
LOAN FINANCING AND HEALTH TECHNOLOGY TRANSFER TO
THE PRIVATE SECTOR IN INDONESIA AND THAILAND

NEEDS ASSESSMENT: REPORT II

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I. SUMMARY

This "Needs Assessment Report II" completes reporting on the feasibility study carried out for HEALTHlink, a program of health technology transfer, planned for implementation by PATH. This second report provides information on three specific objectives of the needs assessment.

1. To establish procedures for loan development with Bank Niaga and Siam Commercial Bank.

PATH has taken part in the process of identifying alternative methods of financial structuring for the proposed new program and has developed working relationships with the institutions which are expected to be important to the success of HEALTHlink in both Indonesia and Thailand.

2. To establish working procedures for financial feasibility studies with local firms in each country.

PATH has identified potential resources for feasibility studies in Indonesia and Thailand. The identification of these firms and the rapport created will help PATH to launch the HEALTHlink program expeditiously.

3. To determine possible mechanisms by which government officers can assist in local project identification and formulation.

The productive meetings between relevant government organizations and PATH, which are discussed in this report, form the beginning of a process of seeking referrals and other assistance from government officers which will go on throughout the HEALTHlink program. These initial constructive meetings also represent a first step in the important process of creating governmental support for a program which will promote private sector involvement in an area which has a large amount of government involvement and regulation.

II. INTRODUCTION

This is the second of two reports on a Needs Assessment that has been conducted by the Program for Appropriate Technology in Health (PATH) at the request of the USAID Bureau for Private Enterprise (PRE). The assessment is part of the launching of a new effort to transfer appropriate health technologies from the U.S. and other developed countries to the developing world, with particular focus on Indonesia and Thailand. The program, to be called HEALTHlink, would be directed to meeting the health needs of the majority poor.

The assessment has been conducted over a three and one-half month period from January to mid-April 1984. PATH staff in Seattle and the PATH representative in Jakarta have conducted most of the assessment. In addition, consultants in Bangkok were retained.

The assessment has been conducted in the framework of Terms of Reference prepared in advance and submitted to PRE for approval. Report I dealt with five of the eight objectives of the terms of reference. This report (Report II) covers the remaining three:

1. To establish procedures for loan development with Bank Niaga and Siam Commercial Bank.
2. To establish working procedures for financial feasibility studies with local firms in each country.
3. To determine possible mechanisms by which government officers can assist in local project identification and formulation.

These objectives differ from the other five in that they are exclusively concerned with the mechanisms by which the program will operate rather than the substance of the program (e.g., specific products or companies) or communication with various USAID offices (e.g., the Missions in Jakarta and Bangkok). For reference, the five objectives dealt with in Report I are listed:

1. To identify at least two loan possibilities in each of the two countries.
2. To establish working relationships with relevant officers of the USAID Missions in each country.
3. To identify additional local resources such as consultants, trade associations, etc.

4. To identify government regulations, laws and policies that will influence project formulation and implementation.
5. To establish procedures for continuing communication between the program and the Office of Health of USAID/S&T and the Office of Asia Technical Resources of USAID/Asia Bureau.

III. PROCEDURES FOR LOAN DEVELOPMENT

In Thailand, PATH staff met with officers of Thai Farmers Bank. This bank was selected on the basis of the discussions held during the first trip to Asia by PRE staff Robert Parra and Richard Rosenberg and PATH staff Richard Mahoney. Whereas Siam Commercial Bank had evidenced some reluctance to participate in the proposed HEALTHlink program, Thai Farmers Bank had expressed considerable interest.

Mr. Narong Sri Sa-an, Senior Executive Vice President of Thai Farmers Bank, had stated that his bank was involved in financing the health sector and was interested in expanding this involvement because of the relationship of health to national development. We were told of a Thai Farmers Bank program to expand health service delivery to areas outside Bangkok.

Under this program, graduating physicians and pharmacists are provided long-term loans to finance the establishment of their practice or a pharmacy. Special priority is accorded young professionals who wish to establish their place of work outside Bangkok. The extension of health care services beyond Bangkok is a national priority of the Royal Thai Government.

During a subsequent visit, PATH staff met with senior staff of the Business Development Department. The manager of this Department is a qualified pharmacist. She has played a key role in the development of the young professionals' program. She expressed her keen interest in the proposed HEALTHlink program because it would provide an opportunity for Thai Farmers Bank to increase its capability to work in the health field.

PATH was able to discuss both general procedures by which PATH and Thai Farmers Bank could collaborate in loan development as well as specific procedures for a test case that arose.

In general, the procedure is quite straightforward. PATH will conduct its own financial and technical feasibility studies. If, based on these studies, PATH and the project sponsor should conclude that the project merits implementation, a project proposal will be prepared for submission to banks and other investors. In the case of Thai Farmers Bank, the Bank will want to conduct its own feasibility study. Bank staff stated that it conducts its studies using its own staff and perhaps a local consultant. University staff are sometimes used as consultants when the project involves sophisticated technical activities. The Bank's feasibility study is usually completed in one or two weeks and the Bank can usually make a decision on a loan application within two months of submission of the application.

Thai Farmers Bank (as do most banks in Thailand) places a great deal of weight on the character and reputation of the individuals and companies involved. The technical characteristics of a project will not be as important in the Bank's decision as the people involved. If the applicant is known to the Bank and has a good credit standing, the loan will have a much better chance of approval. Thai Farmers Bank noted that in cases where it does not have good documentation of the credit standing of the applicant, the involvement of PATH, both in project development and project execution, will give the Bank the opportunity to make loans it otherwise would not consider.

In the course of our discussions it was made clear that the local project sponsor would be expected to reimburse PATH for all or a portion of the costs that PATH incurs in developing the project. It was agreed that this reimbursement cost could be included in the loan made by the local bank.

It was also explained that any continuing technical assistance required from PATH would be paid for by the sponsor and also could be paid from loan proceeds.

While making it clear that PATH staff was not in a position to represent PRE, it was noted that PRE was considering accepting the credit risk for its portion (50%) of the loans. Thai Farmers Bank staff were enthusiastic and made it clear that assumption of credit risk would make USAID funds quite attractive.

Thai Farmers Bank can offer a loan structuring arrangement that may be of some interest to sponsors. The Bank offers a currency convertibility option. Under this option, the borrower can redenominate the loan (between dollars and Bhat) once every three or six months. It is not known whether other banks offer this same feature.

Thai Farmers Bank staff indicated that its offices in the United States would be available to interact with the headquarters of the U.S. bank which PRE might choose to work with as the central banking institution.

The specific case that PATH and Thai Farmers Bank staff were able to discuss is the establishment of a new company that will undertake the manufacture of raw materials for antibiotics. (This is one of the priority areas identified in Needs Assessment Report I.) The project most likely does not qualify for HEALTHlink since the Royal Thai Government's Government Pharmaceutical Organization (GPO) will be a part owner.

Several Thai banks, including Thai Farmers Bank, have been approached to provide an estimated \$4.5 million in loan financing. This project is of interest to PATH since it would qualify for support under the

Ford Foundation-sponsored ILF program. PATH offered to provide, subject to feasibility assessments, up to \$500,000 in loan financing and up to \$50,000 in technical assistance.

Thai Farmers Bank offered to provide a syndication service to the new company. It would accept a deposit from PATH which it would on-lend to the company. In this particular case, Thai Farmers Bank offered not to charge PATH a fee for managing PATH's portion of the loan. This service may not be generally available.

Thai Farmers Bank would establish a dollar account for PATH. As repayments are received for the loan, PATH's portion of the repayment would be deposited in PATH's account. PATH may withdraw the money at its discretion. In the case of Thailand, PATH would withdraw its funds immediately as dollar time deposits earn substantially less in Thailand than they can in the United States.

Thai Farmers Bank also offered to provide, without charge, documentation services for the loan. This would include not only the drawing up of a legally enforceable loan document, but also the registration of the loan with the Bank of Thailand. Registration with the Bank of Thailand is necessary to assure the availability of dollars (not a major problem at this time) for repatriating loan payments to the United States.

In summary, it is clear that Thai Farmers Bank is prepared to work collaboratively with the program and to make available its banking acumen.

In Indonesia, PATH staff met with officers of Bank Niaga. Discussions were held among PRE staff member, Richard Rosenberg, and Bank Niaga officers Maschli Mohammed and Max Siddhartha. The Bank Niaga/PRE relationship was covered, as was the cost of loan funds. The Bank Niaga stated that the interest rate requested by PRE was quite high. Even at the rate offered, the bank could cover its costs and was interested in participating in the program. In general, the Bank Niaga staff were quite positive with respect to the program.

PATH staff also participated in other meetings to evaluate alternatives in Indonesia. These included a meeting with Philip DeFord of Chase Manhattan Bank. Mr. DeFord suggested the alternative of depositing \$2.5 million with one bank in Indonesia which would then on-lend to all of the PATH-developed projects. The principal bank (probably an international bank) would then make loans or issue letters of credit to the Indonesian firm's own bank (probably a local bank). The local bank would provide the matching funds and accept the credit risk. This structure would have the advantage of allowing the borrowing firm to work with its own bank.

Additional meetings were held with Michael Selby of Data Impact in Jakarta. Mr. Selby had several recommendations for managing and structuring the PRE loan pool. The discussions centered on the idea of assigning a "manager" for the loan funds prior to disbursement for loan projects. The manager would perform the same role as the international bank in Mr. DeFord's suggested arrangement for loan projects. The difference would be that the manager would be able to choose from a range of pre-approved investments such as Asian Currency Units (ACUs) to maximize the earnings on the funds. The possibility of using a "guaranty" facility in the PRE program was also discussed. To establish a guaranty, the manager or international bank controlling the preloan funds would pledge ACUs to open a standby letter of credit (LC) in favor of the client's local bank. This method would avoid the process of bringing funds into the country and the later repatriation. The LC would be for 50% of the loan amount with the balance funded by the local bank. The terms of the LC would establish a scheduled reduction in the amount guaranteed over the life of the loan which matched repayments by the borrower. This is an attractive suggestion, and it is understood that PRE staff are pursuing it further.

At the Bank of America, Richard Yeoman expressed interest in the program. He suggested that the program not limit the loan structure to a guaranty facility, but establish a method that also allowed for direct dollar lending to clients. Mr. Yeoman felt that the cost to the borrower could be reduced by 150 basis points by direct lending. Bank of America would like to participate in the program and Mr. Yeoman said the bank would be willing to make matching funds available for loans as small as \$100,000.

A meeting with Bank Duta Ekonomi offered some information about the choices between Rupiah and dollar lending. Given the uncertainty of the value of the Rupiah against the dollar, it appears that borrowers would almost always prefer to have loans denominated in Rupiah. Unless the firm has some foreign currency earnings from exports, a dollar denominated loan has the risk of increasing in the event of a Rupiah devaluation. Banks have access to dollars through swap, which for about 6% per year will translate dollar financing to Rupiah financing. While swap can act as a hedge against the currency risk of a dollar loan, it is available only in six-month contracts, and it is not always available. Serious concern over the value of the Rupiah at some time in the future could affect the availability of swap facilities and place the long-term borrower in an exposed position. Therefore, from the borrower's perspective, Bank Duta Ekonomi felt that it would be best to guaranty Rupiah loans.

While investigating loan alternatives for ILF loans in Indonesia, PATH staff have met with two leasing companies which may have some potential as participants in the PRE program. Leasing has the advantage of the lessor retaining title to the capital goods. In Indonesia, where perfecting a security interest in assets is hampered by the lack of a central registry for recording secured positions, leasing may become an important financing method. Lessors also generally will deal with smaller transactions (\$50,000 to \$300,000) than banks are willing to work with.

PATH staff met with Mr. Dia of P.T. Orient Bina Usaha Leasing, and with Mr. Dana of Citilease. The meetings provided basic information on the status of leasing in Indonesia. Pass-through lending can be done through both of these institutions, and in the case of Citilease, a deposit in dollars would be attractive, as they have used up their current dollar allocation. Both companies would want to place the lease in the same currency which they were obligated to repay to the depositor of funds. It was difficult to assess the interest rates charged on leases due to various deposit and title transfer charges, but since the leasing companies deal with smaller transactions and sometimes less credit-worthy clients, it can be assumed interest rates will be higher than corresponding bank rates.

In summary, we believe that we have identified a number of attractive mechanisms and organizations with which to implement HEALTHlink in Indonesia.

IV. PROCEDURES FOR FINANCIAL FEASIBILITY STUDIES

During the course of the needs assessment, PATH was able to test procedures for conducting financial feasibility studies. In Indonesia, we were in the process of making a loan to a manufacturer of hospital equipment and worked with a local firm to conduct a feasibility study. In Thailand, we retained a local feasibility study firm to assist the actual conduct of the needs assessment. Since PATH has an office in Indonesia, those staff undertook the needs assessment work. In Thailand, PATH does not have an office and therefore consultants were retained. It is clear that these firms, and certainly others that could be identified, have the technical capability to undertake conventional financial feasibility studies.

As stated in our technical proposal, PATH plans to subcontract with local groups, such as Data Impact in Jakarta, and similar companies in Thailand, to carry out financial feasibility studies. Detailed terms of reference will be agreed to in advance. PATH will provide all required information about U.S.-originated costs, while the local sponsor will provide information about his/her costs of doing business. It is in the analysis of the sponsor-provided information that the abilities and knowledge of the local feasibility study firm will be especially crucial. Financial statements of private companies in developing countries are prepared in a variety of ways and for a variety of purposes. The feasibility firms will analyze these statements and provide a realistic picture of the feasibility of any given project.

In addition to the local firms PATH has worked with, PATH staff recently met with representatives of the SGV Group, an international accounting firm. SGV is the affiliate of PATH's auditor, Ernst & Whinney. They have offices in all of the ASEAN nations, as well as Saudi Arabia, Sri Lanka, Korea, Taiwan, and Hong Kong. SGV offers a wide variety of assistance which could be useful to the PRE program under their "Project Development Services" section. These services include identification of potential joint venture partners, financial feasibility study preparation and analysis, market evaluation, concept pretesting, and assistance in choosing financing structure. With SGV's broad coverage in Asia, they could be useful for projects involving partners from different Asian nations, or US/Asian projects which intend to market throughout the region.

An additional resource for financial feasibility studies in Indonesia is P.T. Panca Bina Esa. It is a consortium of government and private financial institutions that provides financial and management assistance to local firms. Part of this assistance includes specialized services, such as designing information systems and evaluating credit and financial feasibility studies.

It should be noted that financial feasibility studies will have to be confidential and remain proprietary documents of the sponsor and PATH, except to the extent the sponsor should decide to divulge information to the participating banks or others. However, the decision to divulge will rest with the sponsor. PATH's subcontracts will contain confidentiality clauses prohibiting the feasibility firm from divulging any information.

V. GOVERNMENT PARTICIPATION IN PROJECT IDENTIFICATION AND FORMULATION

In implementing HEALTHlink there will be four government agencies of special concern: the board of investment, the government development bank, the ministry of public health, and the food and drug administration. We have been able to identify specific ways in which the participation of these agencies can be obtained.

In Thailand, PATH staff met senior staff of the Board of Investment's Project Development Division. This government office is responsible for identifying opportunities for industrial promotion. Having identified an opportunity, the office will conduct an analysis of the potential market and the financial and technical feasibility of the project. If it concludes that the opportunity merits promotion, it will announce its willingness to make available certain incentives to entrepreneurs willing to pursue the opportunity.

The tax and duty privileges that the Board of Investment is empowered to grant to a promoted project are:

1. Exemption from corporate income tax,
2. Exemption from or reduction of taxes and duties on machinery,
3. Reduction of taxes and duties on raw materials,
4. Reduction of taxes and duties for projects located in an Investment Promotion Zone, and
5. Exemption from and reduction of taxes and duties for export production.

There are specific requirements that a project must meet for each of these privileges to be awarded. For example, exemption from import duties and business taxes on imported machinery will be granted only if there is insufficient or no local production of the same machinery with quality comparable to the import.

The Board of Investment accords high priority to the promotion of projects in the health industry. However, according to BOI staff, few projects have actually been promoted because the BOI lacks the staff capability to develop opportunities in that field.

The proposed HEALTHLINK program was described to BOI staff and discussions were held on the manner in which the two agencies could collaborate. BOI staff expressed willingness to assist HEALTHlink. BOI offered to make available office space to PATH consultants who are visiting Thailand to explore specific project opportunities. In addition, BOI staff would be available to participate in feasibility

studies, with the understanding that the Project Development Division is experiencing a staff shortage. In return for providing its facilities to HEALTHlink, BOI would require access to the feasibility study reports and would want to have the opportunity to pursue the project for promotion, if it met BOI requirements. (The exact conditions for BOI's provision of assistance to HEALTHlink were not discussed. The conversation was to identify possible areas of collaboration.)

PATH believes that this opportunity to collaborate with BOI should be pursued. It can work to the benefit of both organizations. On the one hand, PATH will have access to the considerable resources of BOI; on the other hand, BOI will be able to explore projects which otherwise might not have been brought to its attention.

PATH staff also met with senior staff of the Industrial Finance Corporation of Thailand (IFCT). IFCT is the government agency responsible for providing loan financing at less than commercial interest rates to new enterprises that are considered to contribute to the economic and industrial development of the country. It currently is lending at a rate of approximately Bhat two billion (\$87 million) per year. As of December 31, 1983, its major outstanding loans were in four areas:

1. Non-metallic mineral products (22%),
2. Agro-industries, agribusiness and food processing (17%),
3. Iron and steel products and other metal products (11%), and
4. Services (10%).

As noted in HEALTHlink Needs Assessment Report I, IFCT has not made significant investments into the health industry. In great part this is because the health industry is largely a repackaging undertaking and does not involve manufacture of raw materials or original formulation of products.

IFCT priorities are 1) export orientation, 2) location outside of Bangkok, 3) utilization of local raw materials, and 4) labor-intensive production processes. This does not mean that it does not fund capital-intensive and high technology operations.

The organization is in the process of expanding its activities into two new areas. First, it is planning to provide small-scale financing for projects of less than \$50,000. This is being carried out in cooperation with government efforts to implement the Small Industry Finance Organization. Second, IFCT is considering providing equity financing to selected projects.

Senior IFCT staff expressed considerable enthusiasm for working with PATH in the implementation of HEALTHlink. IFCT would like to identify projects in the health industry which it could finance. IFCT staff named four particular services it could provide to assist in implementing HEALTHlink. First, it would be willing to collaborate on financial feasibility studies, and, in particular, checks on market figures for proposed projects. Second, it could help to find investors to cofinance projects. Third, it could provide financing. Fourth, once a project has been launched, IFCT is in a position to provide industrial management advisory services.

It would appear that there exists the opportunity for close and productive interaction between HEALTHlink and IFCT, while keeping in mind that HEALTHlink projects themselves may not have any government ownership.

Over the last several years PATH (and PIACT) have had numerous interactions with the Ministry of Public Health in Thailand. Collaborative projects have been carried out with the national family planning program. Currently PATH is working with the Diarrheal Disease Control Program to plan for the introduction of the PATHtab ORS tablet to the government's activities. In preparing for HEALTHlink, PATH staff have met with the Deputy Director General for Health and with his subordinates in the Communicable Disease Control Division (responsible for diarrheal diseases, malarial control, dengue hemorrhagic fever, immunization program, helminthic diseases, and zoonotic diseases) and in the Family Health Division (responsible for the national family planning program and for maternal and child health programs).

The Deputy Director General is willing to support the implementation of HEALTHlink in Thailand. During the Bangkok visit of PATH staff, the Deputy Director General assisted in planning for the registration of PATH as a nonprofit, nongovernmental agency in Thailand. He stated the willingness of the Ministry of Public Health to support PATH's registration application during review by the Ministry of Foreign Affairs, the Department of Technical and Economic Cooperation and other government agencies.

Under the Deputy Director General is also the Office of International Health. The resources of this office were made available to PATH in preparing for its registration application.

We are encouraged by these interactions to conclude that there will be a cordial relationship between the Ministry of Public Health and PATH in the implementation of HEALTHlink.

HEALTHlink would interact with the Food and Drug Administration of Thailand only indirectly through the companies that were undertaking

projects to establish production of new products. We have not met with FDA staff specifically to discuss HEALTHlink, but we have met with them to discuss the application of B.L. Hua for approval to distribute the PATHtab ORS tablet. We anticipate no unusual problems in interacting with the FDA. It is a professional organization that provides serious review of applications. PATH will need to provide full and detailed information on any product that is the subject of a HEALTHlink project.

In summary, we feel pleased with the current stage of developing working relationships with critical government organizations in Thailand.

In Indonesia, PATH staff met with personnel of the Board of Investment (BKPN). The new HEALTHlink program was explained and information was gathered on specific health opportunities which are open to foreign investment. BKPN's Promotion Bureau maintains active files on all registered entrepreneurs and companies. These files will be available to PATH personnel for project identification purposes. BKPN will be an important government agency for the HEALTHlink program, especially since it maintains the "Restricted List" that indicates areas closed to foreign investment.

In meetings with the President of the government's industrial development bank (BAPPINDO), PATH staff found that the Project Promotion Department of the bank could help in identifying projects and clients. Several specific projects were mentioned, such as local production of penicillin. There is also the potential for joint financing of private sector ventures with BAPPINDO. It appears that BAPPINDO will be a valuable collaborator for HEALTHlink.

At the Ministry of Public Health (MOPH) PATH staff met senior ministry officials. MOPH priorities were discussed and a general background briefing on HEALTHlink was provided. Several private sector firms in eye care, medical and dental equipment were referred by the MOPH, and interest was expressed in several areas for which PATH staff may seek opportunities.

PATH staff also met with the Director General and the Director for Drug Control of the Food and Drug Administration (POM). Since many of the products HEALTHlink will finance will require POM approval, a constructive relationship with this agency is important. POM's staff provided several suggestions for projects, such as local production of Lipidol or a similar product. They cautioned that future foreign investments in the pharmaceutical industry would be subject to new regulations which require some local production of raw materials. The Director General is a member of the Select Committee which is coordinating the Government of Indonesia's efforts to promote local production of pharmaceutical raw materials. Since the financing of raw

material production is a potential HEALTHlink activity, he will inform the committee of the program. This will result in key governmental personnel becoming aware of HEALTHlink and may lead to project proposals in raw material production. To help further development of close ties with this important government agency, PATH is considering requesting that POM act as sponsor for PATH's official registration in Indonesia.

In addition to these four basic government offices, PATH personnel met with staff of BAPPENAS, the board in charge of overall government planning. The staff interviewed are in the health section of BAPPENAS and were very supportive of the HEALTHlink concept. Project areas that they suggested PATH examine included methods for water purification, oral rehydration salt production, and various methods of delivering iodine to areas where goiter is endemic.

Based on these interactions with critical agencies and our established presence in Indonesia, we are confident we will be able to work effectively with relevant government agencies.