



SHOREBANK INTERNATIONAL

EL SALVADOR:

**QUASI-EQUITY FUND FOR SMALL AND
MEDIUM EXPORTING ENTERPRISES**

PRE-FEASIBILITY ASSESSMENT

Prepared for the U.S. Agency for International Development/EXPRO
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A handwritten signature in black ink that reads "Lauren Moser Counts".

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EXECUTIVE SUMMARY

The United States Agency for International Development (USAID) funded Export Promotion Program (EXPRO) project engaged ShoreBank International Ltd., (SBI), a subsidiary of ShoreBank Corporation a community development bank holding company in Chicago, to do an assessment of the market, legal and regulatory requirements, costs and risks of a small business investment fund in El Salvador (the Fund). Although a previous study was done in 2004¹, an update of the SME landscape in El Salvador was needed along with the possible structure of the Fund. The SBI team consisted of Lauren Moser Counts, Gretta Larson, Oswaldo Mendoza and Manuel Alegre.

Our research and experience in similar environments indicate the current lending norms in El Salvador favor businesses with substantial collateral coverage in the form of real estate or those needing short-term financing for trade purposes. The limitations to capital imposed by the banks on small business provide an opportunity to a non-bank entity such as the Fund.

Results of our work reveal that the Fund should target investments of a size between \$100,000 and \$500,000 with the average investment size of \$300,000. The Fund should have the option to go as high as \$800,000 on an exceptional basis. The Fund will target export companies in exporting areas such as food products, technology, engineering and medical/dental services. Export companies will be targeted because of the high growth potential in this area and the technical assistance these businesses are receiving that will help ensure them to meet the demand and maintain a high quality of product and service. However, investments should not be limited to only export companies. The Fund should be constituted as a mixed fund seeking to provide longer-term (beyond three years) financing in the form of debt, quasi-equity and equity, allowing for flexibility while still obtaining commercial returns on the investments.

The Fund has the opportunity to collaborate with several established organizations to provide the investees with technical assistance prior to and after the investment. This assistance includes managing growth, budgeting and financial controls, business and export plans, and strategic decision making.

The recommended size for the Fund is \$8-10 million and should be committed prior to launching the Fund. Additional sums should be actively explored should the Fund exceed the Base Case projections as seen in the financial projections. Projected returns in the Base Case or most likely scenario for the Fund investors are at 7.51% assuming a mix of equity, quasi-equity and senior debt transactions. The life of the Fund is proposed to be 10 years. The total number of investments/loans closed and exited over the life of the Fund is projected in the Base Case to be a total of 40 investments with an average size of \$300,000.

The primary challenge to the Fund is launching the Fund in a timely manner to take advantage of the built up momentum and interest in the Fund by investors and investees. An additional challenge will be to keep a pipeline full of potential investments, making good use of the referral sources available.

The Fund will help ensure a full complement of financial services for small and medium sized enterprises in El Salvador. It will provide flexible financing for those SMEs that are at a particular point in the life of their business where conventional financing does not meet their needs. While assisting in the development of the SME sector in El Salvador, the Fund will also provide its investors an acceptable rate of return on their investment.

¹A study performed by Jean Pierre Schwartz, Managing Director, Washington International Finance Corporation (WASHFIN) and Alejandro Saravia and Manuel Castro, consultants.

SMES IN EL SALVADOR

Private enterprise in El Salvador covers the full spectrum of businesses, from a sizeable, flourishing micro enterprise sector to the larger, well established enterprises. In between these two we find the small and medium enterprises (SMEs). The SME sector in El Salvador plays an important role in the economic well-being of the country. As in most countries, El Salvador's SMEs are leaders in innovation and entrepreneurial activities, employ a large percentage of the workforce (over 50%) and contribute substantially to the Gross National Product. The Fund's target businesses will be those engaged in export activities as defined below.

Small and medium sized businesses in El Salvador are usually structured as sole proprietorships, partnerships or Sociedades Anonimas (S.A.).

Definition of SME/EXPORT

Although different institutions vary in the definition of small and medium enterprise, the most common definition appears to be:

Small enterprise – 5 to 49 employees and revenue not exceeding \$1,000,000 per year.

Medium enterprise – 50 to 100 employees with revenue not over \$7 million per year.

An export business is defined as any business whose revenue comes at least in part from a source outside of El Salvador. Examples of these include:

- Companies that export goods made in El Salvador to foreign countries.
- Tourism, including health tourism where foreigners come to El Salvador for medical/dental treatment.
- Engineering – local companies provide engineering services to foreign companies.

Size and Depth of Market

It is estimated that as of December 31, 2007, there are 15,344 small businesses in El Salvador². Although they represent only 4% of all businesses in the country, it is estimated these companies employ 39% of the workers. Medium sized enterprises are estimated at 7,823 and contribute 11.9% of the employment. The small and medium businesses fall into one of the three major economic sectors of:

	Small	Medium	Total ³
Industrial	21.6%	11.0%	20.5%
Commerce	33.3%	62.0%	36.8%
Services	45.1%	27.0%	43.3%

Commerce includes both export and import. Although imports exceed exports, the deficit is offset by external aid and remittances. Implementation in 2006 of the Central America-Dominican Republic Free Trade Agreement (CAFTA-DR), which El Salvador was the first to ratify, has strengthened an already positive export trend. Increases in non-traditional exports have offset the decreases in maquila⁴ exports. The increase in exports in 2007 grew to \$3,965 million, up 7.4% from 2006.

² Information from USAID program -Servicios Financieros para las PyME-report based on numbers from CONAMYPE.

³ A Fund Proposal study performed in Feb. 2007 for FUSADES/PROPEMI by Victor Manuel Serrato P., consultant IDB/MIF

⁴ A maquiladora or maquila is a factory that imports materials and equipment on a duty-free and tariff-free basis for assembly or manufacturing and then re-exports the assembled product, usually back to the originating country.

Based on information obtained from Garantias y Servicios, SGR, S.A. de C.V., the majority of the non-agriculture businesses are located in the urban areas of El Salvador, with the greatest number in San Salvador. Other areas are Santa Ana and San Miguel.

Current Programs Targeting SMEs

Since the beginning of the 1990s, El Salvador has endeavored to restructure and modernize institutions in order to support micro, small and medium enterprises. The Ministry of Economy has played an important role in this initiative by developing institutions and support programs designed to serve this sector. A five year plan was adopted (2004-2009) that included addressing issues of financial support and technical assistance. The Salvadoran Foundation for Economic and Social Development (FUSADES) and the National Commission for Micro and Small Enterprises (CONAMYPE) are both examples of successful programs serving the Micro, Small and Medium Enterprises.

In addition to the national government initiatives, foreign government agencies and non-governmental organizations have implemented programs to strengthen the micro, small and medium business sectors. These organizations offer small and medium enterprises management training, technical assistance in planning, competitiveness and marketing. For purposes of this report, below we will look at those organizations that focus on assistance to export enterprises (non- financial). Financial assistance will be discussed later in the report.

INSTITUTION	CREATED BY	FOCUS
EXPORTA	Vice Presidency of the Republic	Export policy coordination and one-stop shop services where exporters can receive assistance in a number of areas.
TRADEPOINT	Exporta	Devoted to web-based Internet research.
CENTROMYPE	BMI	Assists SMEs in identifying export possibilities and developing business with larger industrial companies.
CAMARA DE COMERCIO Y INDUSTRIA	Members	Includes members from all sizes of businesses, with the majority from the SME sector and in particular commerce. Have programs to enhance management and export plans.
COEXPORT	Members	A business association founded by major exporters to improve export opportunities through efficiency and quality.
USAID/EXPRO	USAID	Promotion of SME exports from El Salvador by providing technical assistance and other services.
CONAMYPE	Economic Ministry	Assistance for Micro and Small Businesses
FUSADES	Private	Think tank and research center for sustainable economic development.
JICA	Japanese Agency	Helping SMEs find new export markets in Japan and providing consulting activities.

Financial Sector Serving SMEs

The El Salvador banking system is a multi-tiered system which includes the Central Reserve Bank (BCR) in charge of the development of the financial systems, consolidation of the monetary integration and the generation and disclosure of economic information. The Superintendencia del Sistema Financiero (SSF) supervises the financial institutions, including authorizing the constitution, operation and closure of banks and other financial entities.

Banco Multisectorial de Inversiones (BMI) is a second tier bank created in 1994, to promote the development of private sector development projects by means of granting loans, under market conditions, to financial institutions who then on-lend to viable businesses.

It is estimated that there are more than 170 financial institutions in El Salvador, including banks, credit unions and non-bank financial institutions.⁵

Commercial Banks - The banking system comprises 13 banks. Eleven of the banks are privately held and two (highlighted by an asterisk below) are government owned. During the past couple of years there have been some significant mergers and purchases of local banks by international banks, which has resulted in all 11 private banks being foreign owned⁶.

As of December 31, 2007

Position	Banks	Assets	Loans	Deposits	Equity	Profits
1	Banco Agrícola	\$3652.8	2,468.5	2563.1	427.7	71.0
2	Banco Cuscatlán	2624.2	1756.8	1750.2	339.3	11.0
3	HSBC	2115.3	1499.0	1457.5	256.4	26.8
4	Scotiabank	1948.1	1399.4	1335.1	221.7	15.8
5	Banco de America Central	874.0	620.5	575.1	88.9	13.4
6	Banco UNO	427.2	318.6	282.2	44.2	1.1
7	Banco Promerica	353.8	226.9	281.8	28.1	3.2
8	*Banco Hipotecario	329.8	224.4	218.1	31.1	2.1
9	Banco ProCredit	231.7	168.2	154.5	20.9	2.3
10	*BFA (Banco de Fomento Agropecuario)	193.7	99.0	134.4	22.1	1.1
11	Citibank	163.8	40.8	89.2	19.1	0.7
12	Banco G&T Continental	128.8	82.5	78.2	25.1	0.2
13	Banco First Commercial	17.2	6.0	2.4	14.7	0.4

Total loans for 2007 reached \$7932 million or up 12.3% over 2006. The largest growth was seen in real estate loans at 23.5%, followed by consumer loans – 22.8% and commercial loans – 16.3% (\$1476 million). The level of arrears represents only 2.1% of the portfolio.

Over 80% of all loans are in the top two risk categories.⁷ Interest rates too have declined during the last quarter of 2007, following the international markets. Total deposits also grew in 2007 by 17% over 2006.⁸

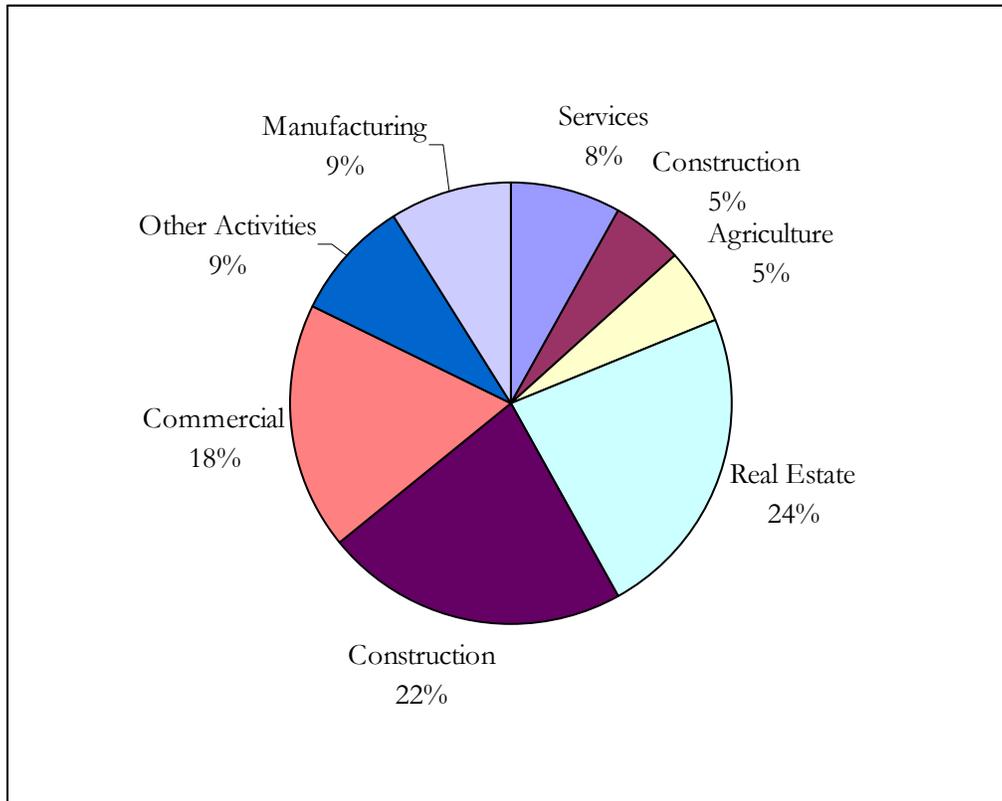
⁵ Information received in an interview with Banco Agrícola.

⁶ For example, Citibank has purchased Banco Cuscatlan, Ban Colombia has purchased Banco Agrícola, and HSBC owns Banco Salvadoreño.

⁷ December 31, 2007 report from the Bankers Association of El Salvador (ABANSA).

⁸ Ibid.

The following chart shows the breakdown in loans.



According to parties interviewed, interest rates on loans average in the range of 9% to 12%. The banks may charge more, but rarely charge above the 12% rate. In addition, fees are charged for appraisals, closing, monitoring, etc.

Typically, banks find it difficult to lend to small and medium size enterprises for some of the following reasons:

- Inadequate or poorly present financial information – rarely are there audited statements.
- Financial information prepared to reduce tax consequences.
- No credit history.
- No long term business strategy.
- Insufficient collateral - most banks base the loan on the value of the collateral as opposed to the needs of the business.
- High debt to worth.
- Historical cash flow will not support future debt.
- The high cost of monitoring vs. the size of the loan.

Banks that are most successful in growing the SME area of their customer base are banks that have a department dedicated to SMEs or the bank itself has a mission to serve this sector.

Pro-Active Initiatives

As stated above, pro-active initiatives in providing financial assistance to SMEs have been instituted by internal and external sources.

BMI. In 2004, spearheaded by BMI, a program was formed, under the oversight of the Superintendent of Financial Systems (**SSF**), Garantias Y Servicios, SGR, S.A. de C.V. The **SGR** (Sociedad de Garantias Reciprocas) provides a 100% guaranty on a loan to a micro, small or medium sized business, provided it meets the SGR's qualifications. To obtain a loan, a business must first be a member of SGR (about \$40 for one share). SGR then analyzes the business, structures the loan, including collateral requirements, interest rate and terms. SGR prepares all documentation and then submits the loan to a bank for funding. Should there be problems with a loan, SGR handles the monitoring and work-out. SGR has over 600 members and \$18 million in guaranties outstanding. Seventy percent are revolving credit lines of one year and the remainder are loans up to three years. Loan losses are less than 2%.

USAID-DCA is a loan guaranty program for private sector banks that loan to SMEs. Banks involved in the program are able to receive a guaranty of up to 50% of the loan amount. The aim is to help stimulate development by encouraging banks to loan to this sector. As of December 2007, DCA has seventy-one loans for \$2.8 million in its program in El Salvador.

CASEIF was established in 2000, sponsored by MIF and Norfund (Norwegian Investment Fund for Developing Countries). It is a private equity fund targeting MSMEs in Central America, Panama and the Dominican Republic. It is managed by LAFISE Investment Management, Ltd., with offices in several Central American countries including El Salvador. The fund has made 10 investments and exited six, with two years left to go. The target size was \$800,000, with an average size of \$750,000. Two investments were to Salvadoran companies. In 2007, \$35 million was raised to start a second fund, **CAESIF II**. Seventy percent of the investments will target companies with up to 100 employees or \$5 million in annual revenue or assets. The target investments range between \$250,000 and \$1.5 million, looking for an average size of \$1 million. Thirty percent of the investments will target larger companies with up to 300 employees and \$10 million in revenue or assets. Investments could be as high as \$3 million. CASEIF II is tied to a grant facility of technical assistance funds for investees, provided by Norfund, BIO and SECO.

CAGF – The Central American Growth Fund is in its initial stages. The Fund has a maximum capitalization set at USD 25 mm. It will provide equity and quasi-equity financing, financial and technical advisory, and value-added governance to approximately 15 SMEs in the target countries. The technical assistance will be provided by a Facility set up by donor organizations, independent from the Fund. CAGF will be managed by Aureos Central American Management Company, with offices in Costa Rica and El Salvador.

USAID- Financial Services for SMEs in El Salvador implemented by CHEMONICS International. Another USAID program geared to SME finance is one currently managed by Chemonics International. The project is training banks in SME lending “best practices”, giving the banks the tools to provide a greater comfort level in their ability to make loans to this sector. All but 3 of the banks in El Salvador have received training from Chemonics and they are currently working closely with six banks. This training provides practical, efficient lending practices. The additional “know-how” provided by this program is leading to increased focus in lending to SME market by participating banks.

CONAMYPE. A new partnership between CONAMYPE and Banco Agrícola has recently been concluded. CONAMYPE is an incubator and investor “angel” of micro and small enterprises. Once

the businesses operating successfully, Banco Agrícola could become the businesses' main source of financing.

FUSADES. A private organization created in 1983 for the promotion of economic, social and intellectual development. FUSADES/PROPEMI operated a micro and small credit program for 20 years. In 2007, the entire portfolio was sold to the Banco de América Central (BAC). In February, 2007, FUSADES invited IDB/MIF to complete a study on establishing an SME investment fund, which has been reviewed by the SBI Team.

A SMALL BUSINESS EXPORT INVESTMENT FUND

Why a Small Business Export Investment Fund?

A small business investment fund is one of the financing vehicles that meets the financing needs of businesses that are at a certain point in their evolution. Although there appears to be nearly a full range of financing options in El Salvador, from self-financing to investment funds, the SBI team has observed a segment of small and medium businesses that do not qualify for traditional bank loans and are often too small for the investment funds. These are businesses that are at a place in their company's life-cycle where medium to longer term financial support is required, but is not provided by the banks. This type of financing is best suited to equity or quasi-equity investment, and is limited to those businesses that have a record of quality management and strong, rapid growth potential. An investment Fund targeting this segment of growth companies should seek commercial returns while having the benefit of greater flexibility than a bank in structuring its investments.

Potential Investors and Expectations

Three of the potential investors were interviewed and all expressed interest in investing in the Fund (assuming positive outcome of vetting the market opportunities and viability of the Fund):

- Banco Multisectorial de Inversiones (BMI)
- The Multilateral Investment Fund of the Inter-American Development Bank (MIF)
- FUSADES

Similar expectations were expressed during the interviews:

- Capitalization of the Fund should be \$8 million but could go up to \$15 million if deal flow could support it.
- The Fund would have a life of 10 years
- The Fund would target export companies
- Expected rate of returns range from 9% - 15%
- Investments in export businesses from \$100,000 to \$800,000.
- Investments only in the formal SME sector.

Once a "core" group of investors have committed, in principal, additional investors should be pursued. Based on knowledge of existing SME Funds, the minimum amount of \$8 million should be committed before launching the Fund. Bringing additional investors into the fund after it has been closed and operational can be complicated.

Target institutional investors, other than those above, may include DEG, KfW, IFC, IIC, Norfund and FMO. Some of these organizations have been previously approached and expressed interest subject to further structuring and due diligence. Private investors or foundations should also be sought with a minimum investment of \$500,000. Examples of private investors are some of the large companies in El Salvador that recently sold their bank holdings and have excess liquidity. Also, successful El Salvadorans in the United

States might be candidates, although U.S.-based individual investors would need to be qualified and vetted in accordance with U.S. regulations.

The appeal of the Fund to investors would be that it will be a fund operating on a commercial basis, which provides a vehicle for investing in growing export businesses that due to their smaller size would not normally be considered by traditional investors. The Fund will add to the range of financial vehicles that provides opportunity for the development of a strong economic base in El Salvador.

Market Demand

In accordance with ShoreBank’s experience in SME finance, companies or entrepreneurs will approach the Fund for financing for a variety of purposes. The following table outlines the different stages of enterprise development, which will in part determine the financing product and structure.

Stage of Development	Financing Need	Risk Level
Seed	A company or entrepreneur needs “seed” financing to prove a product concept. This could be a completely new venture or a new idea for an existing company. The funding is not for marketing the concept, which occurs at a later stage.	Very High
Start-ups	A company that has been in existence for 1 year or less. Financing needs could vary.	Very High
1 st Stage	Funding is needed to commercialize the manufacturing and sale of a product	High
2 nd Stage	The company needs working capital for initial expansion, but is already in business and shipping product. Could still be operating at a loss.	Moderately High
3 rd Stage	The company is undergoing major growth and is breaking even or turning a profit. Use of funds could include a plant expansion, marketing, or new product development including product branding, positioning and other intangible assets that add value to products.	Moderate
Bridge	The company expects to go public within 6 months to a year and requires financing to “bridge” to the IPO.	Moderately High
Leveraged Buyouts (LBOs)	Funding is needed to enable management to acquire a product line or business (at any stage of development) with management holding a share of equity.	Moderately High

The Fund should target companies in the 2nd and 3rd stage of development in accordance with the level of risk associated with this stage of growth and the appropriate financing mechanism. The Fund could consider start-ups or companies in the 1st stage of development, but should finance only those with the strongest management teams and growth potential, in which the principals have invested or will invest together with the Fund at least 30% of the project cost in-kind or in cash.

The export market continues to grow and this includes the growth of small and medium export companies that are found in the 2nd and 3rd stage of development (above). CAFTA is assisting in this growth as are the technical support organizations that provide these businesses with information and training in how to become more competitive, reach international markets and management skills.

The SBI team had an opportunity to meet with organizations, lenders and business support providers that work closely with small and medium sized businesses (*Annex V*). The team conducted a focus group meeting with seven exporting entrepreneurs to understand their financing needs and concerns (*Annex III*). We also

had access to several reports pertaining to this sector. The data obtained from these sources has assisted us to confirm the demand for an investment fund as proposed, which further supports the overall viability of the Fund.

To conduct the market assessment, the SBI team obtained a list of the top 123 companies that have worked with USAID-EXPRO. EXPRO provided input on fifty of these businesses, which they believed could be candidates for an investment by the Fund. The export sales of these companies currently range from \$6,000 to \$1,000,000 per annum⁹ The companies represent a wide range of businesses, of which the largest group is food products (sweets, salsas, meat products, honey, etc.) and food supplements, followed by artisans, beauty products and medical services and equipment.

In an additional survey of twenty three small exporting business EXPRO clients¹⁰, twenty indicated the need and interest in an investment for at total of \$8.9 million or an average of \$445,000. The focus group with which the SBI team met (*Annex III*) expressed an interest in the Fund, but stated they would require more information. Their needs vary from investment in intangibles, such as trademarks or packaging design, to equipment and real estate. These businesses are in a growth cycle where their collateral does not support additional loans. Often long term assets are tied up by short term loans, which restrict the firms' borrowing capacity. The Fund with flexible investment instruments would be better positioned to meet these long-term financing needs.

Other organizations interviewed, such as FUSADES and SGR, indicated they would be able to refer clients to the Fund.

Competition/Synergy

Competitors

The banks could be considered both potential competitors and potential partners of the Fund. As competitors, the banks make loans to small and medium sized businesses. Several of the banks target specifically SME customers. According to Chemonics, the six banks they have been working with have launched or will be launching, during the first half of 2008, SME pilot projects. These SME pilot projects are a result of the systems put into place to better serve the SME sector. However, as noted above, they are not always able to meet the needs of the businesses and the businesses then have limited and often extremely costly options, such as family or "loan sharks". At the same time, it will be important for all Fund investees to have a banking relationship and the Fund should look for ways to collaborate with banks for financing packages for portfolio companies, especially for short-term financing needs of the investee.

Two investment funds described above could also be considered potential competitors, CASEIF II and CAGF. Both of these funds serve the broader Central American market as opposed to targeting El Salvador specifically. While they have the ability to invest smaller sums of money, they generally look for investments of \$1,000,000 or more.

Synergies

The competitors listed above - banks, the two Central American funds, SGR and other supportive organizations would most likely welcome collaboration with the Fund providing co-investing and/or technical assistance. There could be opportunities for joint projects. These organizations could also be good referral sources.

⁹ Due to client confidentiality this list has not been included in the report.

¹⁰ See footnote #8.

SCOPE OF THE FUND

Mission

The objective of the Small Business Export Fund is to support the development of small and medium-sized export businesses in El Salvador. The primary goal of the Fund is to increase entrepreneurial access to medium to long-term risk capital to finance enterprise growth. SBI believes the dual objective of financial and development objectives can be achieved with proper structuring of the Fund, use of appropriate investment instruments which provide returns superior to straight debt, and experienced fund management.

Investment Objectives

Investments should be structured to generate current revenue streams to the Fund, yet accommodate the growth and working capital needs of the investee business. While capital appreciation should not be the primary focus of the Fund, it should nevertheless target export companies with substantial growth potential throughout the duration of the investment. The Fund should seek to participate in revenues or profits through revenue share agreements and dividends.

Investment Strategies

Each investment should be reviewed and tailored to a particular customer. Future cash flow should be a determining factor in structuring the appropriate term of the investment. Management, market and competition are among the major points analyzed, regardless of the size of the deal. The selection of the investment structure should include senior or subordinated debt, quasi-equity and equity* instruments. These instruments should be structured to account for the projected cash needs of the Investee Company while creating a sense of discipline and provide the Fund a gauge of the investee's commitment and performance. The selection of the investment structure should depend on the perceived potential risk and return of the investment as well as the stage of development of the enterprise. All investments should be comprised in such a way as to reduce the Fund's risk, generate a moderate operating income and accommodate the growth and working capital needs of the businesses. With all investments, the Fund should build in a timely, successful exit strategy, optimally, through self-liquidating investments.

*Straight equity investments would be the exception and should be in conjunction with other investment products.

Investment Parameters

Investments would target export businesses from \$100,000 to \$800,000 (or 10% of the Fund's equity, whichever is lower), with an average size of \$300,000. Existing established small to medium-sized businesses, focused on but not limited to export businesses. Targeting local businesses whose revenue is not derived from exports will provide the Fund additional flexibility and deal flow. It is assumed these businesses would have verifiable revenue streams which can be adequately monitored and tied to repayment structures to ensure portfolio performance.

- The Fund should anticipate from 3 – 5 years as the duration of an investment depending on the stage of development of the company. Occasionally, a longer-term investment might be more appropriate for maximizing a company's potential but should be no more than 7 years and thus would have to be made within the first 2 years.
- Only as a complement to longer term investment in a company should the Fund provide any short-term financing (less than 3 years).
- The Fund should seek to avoid investing in enterprises whose activities may be in direct competition with existing investments within the portfolio.

- The Fund should not invest in enterprises that are prohibited as investees by any of the Fund's investors.
- Should the Fund invest in a start-up or early stage development business the Owner's equity participation should be a minimum of 30% of project costs. Such participation could be in the form of cash or in-kind contribution. It is expected that such investments would be a small percentage of the portfolio as they entail higher risk.
- Investments should be made only in businesses operating in the formal sector, with all appropriate legal documentation.
- The Fund should attempt to collateralize its position as best possible, without basing the investment decision on collateral. The Entrepreneur must also be at risk.
- The Fund should seek entrepreneurs whose motivation, training, experience and management ability indicate that the financing will enable the applicant to develop a more successful business.
- Investee businesses must show a strong future positive cash flow.
- Investee businesses will have a competitive advantage and potential growth in market share.

Investment Instruments

SBI recommended Investment Instruments include debt, quasi-equity and equity instruments. The benefit of quasi-equity investment instruments is the current return they provide through loan, income sharing, or fixed dividend payments with the inclusion of collateral as a means to recuperate the investment under a worst case scenario. The exit is built into the structure and generally has a finite date. A typical company would be relatively young exporting company in the process of moderate to high growth (2nd or 3rd stage of development).

Loan Instruments

- Senior debt – This is a traditional bank loan typically collateralized with assets of the company, owner or third party and personal guaranties. The term may be short or long depending on the purpose of the loan. Debt could be used alone or in combination with other instruments

Quasi-equity Instruments

- Subordinated debt – This debt is subordinate to other claims on the company and generally has a longer term than senior debt. The pricing for these loans would typically be higher than senior debt, to reflect the risk of the loan. The collateral position on these loans is weak (subordinated to primary creditors) or non-existent. Often subordinated debt is combined with warrants for equity or conversions to equity to provide the investor some additional reward for the added risk (see below). Without an equity stake, lenders do not have a board seat or participate in the management of the company.
- Convertible debt – Convertible debt is a loan that is convertible into equity ownership in the company in accordance with terms of the loan agreement. Such conversion could be triggered by the company achieving certain sales or net profit goals. Upon conversion, the company would issue new shares to the Fund for the amount of outstanding debt at an agreed-upon conversion ratio.
- Revenue Sharing Loan Agreement – This structure is a type of convertible instrument, but in this case it is a profit-share with an option to convert to debt. The Fund makes a loan to the company and in exchange receives a fixed percentage of the company's gross sales. This share can increase as sales grow and eventually the company "buys out" the Fund (or the Fund's claim to a share of profits) at a negotiated amount. The structure of the Revenue Sharing Agreement provides an incentive to the entrepreneur to buy out the Fund as soon as is possible, because as the company becomes more successful, he or she has to part with a growing percentage of sales. If investees fail to perform as agreed, the profit share converts to a loan with strict terms.

- Preferred stock – The Fund can purchase different categories of preferred stock as opposed to common stock. Preferred stock typically provides the Fund with a fixed dividend to be paid regardless of the company’s financial performance, with limited or no voting rights for the investors. Some types of preferred stock provide no fixed dividend, but preferential payment over other stockholders and preferential voting or veto rights over key areas of company management. The advantages of the fixed dividend type of preferred stock are the current returns to the investors. However, the company must make payments to preferred stockholders out of profit, and the investor’s ability to influence the company may be more limited. A combination of preferred and common stock can be used to achieve voting rights and current returns.
- Convertible preferred stock – Like debt, preferred stock can be structured as a convertible instrument, giving the investors the right to convert their preferred shares into common stock. The shares may or may not be converted at a 1:1 ratio; depending on the valuation, preferred stockholders may have to pay a premium for common stock (receive fewer shares of common stock in exchange for their preferred shares).

Equity Instruments

- Purchase of common stock – The company issues new shares of common stock, which are purchased at an agreed-upon price. Returns come from a combination of dividends, management fees, and exit. The bulk of the returns are expected from the exit than from current income, however. This type of structure would suit a company that currently lacks the cash flow to service principal and interest payments for the entire project amount, has weak net worth, and offers high potential for growth and return to the investors. Given that returns are typically “back-loaded” on the exit, this structure is higher risk than quasi-equity structures. Yet since the investors have common stock and are risking along with the company owners, they have a claim to their share of the net profits of the firm.
- As a means to bypass the legal obstacles of a share buy back by the company, SBI used a “sinking fund” in an environment similar to El Salvador. A trust account in which both the fund and principal(s) of the company have signing authority is created at reliable institution that acts as the fiduciary (usually a bank). An agreed percentage of the salary and/or dividends received by the principal(s) are deposited into the account. These resources can only be used to buy back the shares from the fund so when the time comes to implement the exit strategy they are purchased by the principal(s) (which is legal) and the fund has the security that the resources for the share buy back are available.
- Reverse Mergers – The definition of a Reverse Merger is “the acquisition of a public company by a private company, allowing the private company to bypass the usually lengthy and complex process of going public”. In the context of the Fund, with this instrument, a foreign company can acquire control of a Salvadoran company, while simultaneously the Salvadoran company becomes a shareholder of the foreign company. All equity contributions made by the investors in the offshore/foreign company would be channeled to the Salvadoran company as shareholder contribution that would be used for working capital or investment. The Salvadoran company is now owned by the foreign company (which is owned by the investors and the Salvadoran company owners). The reverse merger would take the place of purchase of Common Stock, as the exit in this type of investment is very difficult and can only be done to a third party. The existing owners or company cannot repurchase the shares. With a reverse merger the ownership of the Salvadoran company would not change upon exit, only that of the foreign company. SBI has never used this instrument so cannot comment on its use in practice. The Reverse Merger might be a bit complicated and costly for the average investee, but could possibly be used with larger investments,

Additional information on the Reverse Merger can be found in the paper received from Mr. Luis Medina (*Annex IV–Section II*). The paper also includes Conditions, Representations, Warranties and Covenants to be

covered in loan documentation (*Annex IV- Section III*). It is SBI's understanding that all of the above instruments are viable in El Salvador.

Advantages & Disadvantages of Products

The following table summarizes some of the advantages and disadvantages of each of the above equity and quasi-equity instruments from the perspective of the Fund and the investee enterprise:

Investment Instrument	Advantages		Disadvantages	
	For the Fund	For the Entrepreneur	For the Fund	For the Entrepreneur
Senior Debt	Provides current return in form of principal and interest payments. Senior position in collateral.	Do not have to share "upside" with investor.	Limits potential returns.	Drain on cash flow during growth period.
Subordinated debt	Provides current return in form of principal and interest payments.	Do not have to share "upside" with the investor.	Limits potential returns; collateral position weaker than with senior debt.	Interest rate higher than a senior loan; drain on cash flow during growth period.
Convertible debt	Provides current return; allows investor to participate in "upside" with conversion.	Interest tax deductible; could be more palatable to company than parting with common stock at outset.	Conversion rate could be a contentious subject; may not be able to convert at an advantageous time.	Drain on cash flow during growth period; conversion results in sharing the control and "upside" of the company with the investor.
Revenue Sharing Agreement	Allows lender to participate in the profits of the company; fairly simple to document and close.	Does not drain the cash flow until profits reach certain levels; not parting with equity	Lender does not sit on the board or otherwise influence co. mgmt.;	Percentage of royalty payments to the lender increase as revenues grow (sharing of "upside");
Preferred stock	Provides current return in form of fixed dividends; can provide some preferential rights in managing the company.	Gain equity partner with value added, which does not have a claim on the complete upside.	Upside participation limited by the fixed dividend; some forms of preferred may not allow for board seat.	Fixed dividend must be paid out of profit (no tax advantage).
Convertible Preferred Stock	Same as above, and option to participate in upside	Gain equity partner, with conversion limit the drain on the cash flow.	Conversion rate may be disadvantageous, initial preferred ownership may have limited impact on mgmt. of company	Same as above, and company will have to eventually share the upside with the investor; conversion may be disadvantageous for the company.

Investment Instrument	Advantages		Disadvantages	
	For the Fund	For the Entrepreneur	For the Fund	For the Entrepreneur
Reverse Mergers/ Common Stock Purchase	Allows investor to fully participate in the “upside” of the company’s success	Allows the company to grow without drains on the cash flow of interest and principal payments, etc.	The bulk of returns are frequently dependent on a successful “exit” from the company. Payment of dividends could come late in the life of the investment.	Must share the “upside” of the success of the company with the investor.

The primary considerations for which investment instrument to choose should depend on the financial situation of the company, its potential for growth, its valuation, and the current ownership and capital structure. These factors should indicate the level of risk of a particular deal and the appropriate structure and return for that risk. Structuring an equity or quasi-equity deal that is profitable for both the investor and the entrepreneur is key to the success of any risk capital fund.

Evaluation Guidelines

Although the average investment size is not large, as investment funds go, it is still important to evaluate all aspects of the applicant investee. Since as noted above, small and medium sized businesses lack the sophistication of larger businesses, this will take time and require the Fund personnel to work closely with the investee in order to obtain a true and accurate picture of business and its needs.

The Fund should ensure the following analyses are completed and the risk factors are considered and evaluated prior to a financing decision:

Non Financial Analysis:

Legal/Organization Structure
 Environmental
 Principals and Management
 Markets/Sales
 Marketing Strategy
 Product/ Production/Operation
 Reputation

SWOT Analysis:

The Investment Officer should determine the Strengths, Weaknesses, Opportunities and Threats (SWOT) of the company as a whole.

Financial Analysis:

General Financial Data
 Balance Sheet
 Income and Expense Statement
 Cash Flow
 Margins/Ratios
 Ratios and Relationships
 Forecasting

Risk Assessment

In any investment there is a level of risk. It is the responsibility of the Investment Officer to initially assess this level of risk and to determine if the benefits outweigh the risks prior to presenting the investment to the investment committee, where the final decision is made. The structure and pricing of an investment is determined in part by the amount of risk the Fund will be undertaking.

The Risks include:

- Industry
- Political
- Marketplace
- Inflation
- Interest Rate
- Concentrations
- Liquidity
- Default
- Technological, and
- Regulatory

Technical Assistance

Optimally, there would be a technical assistance component to the Fund for their investees. Should this not be the case, then the Fund should seek out technical assistance organizations to provide assistance to their investees when needed. Many of the potential investees will be referred by organizations that are providing technical assistance to the client they refer. The amount and type of assistance should be disclosed in the referral information and whether the organization would be willing to provide assistance in the future. In the cases where a company needs a different type of assistance than currently receiving or is not getting any technical assistance, it would behoove the Fund to have agreements in place with several technical assistance organizations. Fees for this assistance, if any are required, would be paid for by the investee and the Fund, perhaps on a 70/30 basis. The financial projections prepared by SBI for the Fund include a \$500 monthly expense for technical assistance. The Fund staff would, also, provide technical assistance when appropriate and within their sphere of knowledge.

Portfolio Management

In SBI's experience, the most important time in the life of an investment is after the closing following through to the exit. Once an investment has closed, the file should remain with the originating Investment Officer and analyst. It is the responsibility of the Investment Officer to monitor the investment and work closely with investees to implement a strategic plan. Monitoring and managing the portfolio can often be last on "the list" of things to do when there are investments in the pipeline that need to be worked on and funded. Especially, if everything seems to be going alright with the investee, meaning they are meeting the financial obligations to the Fund. However, because one does not hear about problems does not mean there are none. A good monitoring policy and follow-through is essential to the success of any Fund. If the Fund reaches a size in terms of number of investments in the portfolio that the Investment Officer and Manager are unable to do both the incoming work load and the portfolio management it would be advisable to hire a Portfolio Officer.

Exit Strategy

It is recommended the fund exit an investment within 5 to 7 years of investing, or sooner, depending on the growth trajectory of the company. An exit strategy needs to be considered prior to investing and exit provisions must be included from the beginning of the process (in the term sheet).

The surest exit from investments is the self liquidating investment. Otherwise the most promising exits appear to be strategic sales to foreign companies, or sales to other investment funds or investors. As a rule, Management Buy Outs (MBOs) seldom occur in SME investment funds, however, if this is the strategy to be

taken, it must be clear in the beginning of the investment how this would happen and appropriate steps taken to ensure this possibility.

Part of the strategy for the Fund should be to structure in current return in the investment through the use of alternative investment vehicles describe above, and not rely on huge gains upon exit. The Fund should certainly build value in its companies and seek merger and third party strategic sales of its equity holdings whenever possible. The selection of companies in growth industries is therefore vital, as is structuring in some form of current payment on the investment, whether it be in the form of fees, such as monitoring fees or profit share.

FUND STRUCTURE

Capitalization

The minimum capitalization for the Fund should be \$8 million, given the costs of starting up and managing such a fund in El Salvador. Market demand appears to be sufficient to absorb at least this amount.

Investors and Commitments

The targeted “core” group (MIF, BMI and FUSADES) should commit no less than \$6 million in a preliminary agreement and then look to additional investors to provide up to a total of \$15 million, assuming deal flow can support this amount, but no less than \$8 million. It is assumed investors would take equity stakes in the Fund. It would be less desirable to have a significant amount of termed debt financing in the Fund’s capital structure. The Fund would have a life of 10 years, with a target rate of annual return of 8.0%

Board of Directors /Advisory Board

The highest governing body of the Fund would be the Board of Directors consisting of representatives of the investors who would hold authority to approve the selection and remuneration of the Fund Manager and the Investment Policy.

The Fund could form an Advisory Board comprised of representatives from the business community, who would be a source of potential deals as well as assist in the due diligence process on specific investments. Some members of the Advisory Board could also participate in the Fund’s Investment Committee.

Investment Committee

In addition to the financial commitments, the investors should be represented on the Investment Committee. The Investment Committee is an important element in the success of the Fund and will have the sole authority to approve an investment. The accumulated experience of the committee members will give a greater breadth of knowledge and appreciation of the projects submitted. To ensure effectiveness, the investment committee should have the following characteristics:

- It should be small enough that it could meet frequently (between 5 and 7 members including the Fund management team member);
- Members should be able to review a project rapidly;
- A minimum number of members for a quorum with a majority for approval.

Fund Type and Domicile

There are several options to the type of entity the Fund can use. Luis Medina of Resconi, Valdez, Medina & Associates Central-Law, was consulted regarding the proposed Fund. He has provided information for several options and potential costs in the type of Fund and where it might be located (*Annex IV-Section I*) It is his opinion that an off-shore vehicle would offer the greatest tax advantage to the investors.

- a. Trust (Fideicomiso) – Domiciled in El Salvador

Although this is a viable option, it appears to have some drawbacks. Mainly, the Trust would be subject to taxation and a complicated liquidation and dissolution process.

- b. Sociedad Anonima (S.A.) Domiciled in El Salvador
This vehicle is relatively easy and inexpensive to establish. Through the Foreign Investment Protection Law, the investors can obtain special protection for their investment by registering its capital at the National Investment Office. This registry guarantees special legal protections such as free repatriation of capital and profits.
- c. Off-Shore Entity – Limited Liability Partnership or Trust
Set up of this structure could be more complicated and costly compared to the two above. Depending on the jurisdiction of the off-shore entity, there could be some tax advantages for the investors.

Fund Management – Terms of Reference

The Fund Manager is responsible to oversee every aspect of the investment process, from deal origination, due diligence, presentation of deals to the investment committee, closing and disbursement, monitoring, and exit. For this reason it is essential that the selected Fund Manager have the necessary experience and track record to ensure the ultimate successful running of the Fund and providing positive returns to the investors. The term Fund Manager is assumed to be a legal entity in this case made up of a team of individuals who jointly fulfill the tasks of running the Fund.

Note: It is assumed that the Fund sponsors (in this case EXPRO and other stakeholders) would lead the establishment of the Fund vehicle until the Fund is closed and investors have made their first capital commitments. The Fund Manager would be hired after the Fund is closed. The responsibilities of the Fund Manager following the initial closing of the Fund would include:

1. Establishment of Fund offices in El Salvador, including hiring of a local investment team, outfitting of offices, identification and coordination with legal counsel and the Fund Investors on commencement of operations.
2. Set up of the Fund's administrative and operating system, including financial accounting, management information systems (MIS) for loan and investment tracking, human resource policies and procedures, and general office set-up.
3. Coordinate with Investors to establish Fund's Investment Policy, Investment Committee Guidelines, and other operational documents;
4. Establish Operations Manuals and Policies for the Fund's administration, including due diligence and investment analysis guidelines for staff;
5. Coordinate with local legal counsel to establish set of general closing documents for common debt and investment structures (such as those highlighted in this report)
6. Promotion and marketing of the Fund to potential investees and clients;
7. Coordinate with local organizations to generate a pipeline of investments;
8. Perform due diligence on potential investees;
9. Structure and negotiate individual transactions;
10. Presentation of deals to the Investment Committee;
11. Closing and disbursement of individual transactions, including coordinating with legal counsel (outsourced) to generate closing documents.
12. Preparation of quarterly performance reports including fund pipeline, disbursements, monitoring, problem asset and portfolio grading;
13. Monitoring of outstanding investments, including attending board meetings, collection and analysis of periodic financials, budgeting and projections for investee companies;
14. Oversee the identification and facilitation of provision of technical assistance to investee companies.
15. Negotiation of exits in accordance with investment agreements

16. Oversee any problem assets and workouts that arise proactively in coordination with local legal counsel.

Fund Operation

Several different proposals have been suggested for expediting the flow of investments and possible cost reduction in the operation of the Fund. They include:

1. Outsourcing the analysis of the potential investee. The outsourcing company would do the gathering of documentation, spread the financial information and perform an analysis. Once this was completed it and appeared to meet the criteria of the Fund, the project would be sent to the Fund for review and approval.
2. Outsource of only the initial project review and documentation gathering, prior to being sent to the Fund.
3. Outsource the project monitoring once it funded. Only when there appeared to be a problem would the Fund management take over the monitoring.

At first glance, the above proposals appear as though they could meet the objectives they are trying to attain, however it is worth considering the following risks and logistical challenges to these proposals:

1. Too many people involved in the review of a project. Although the initial review would be done by the Outsourcing company, the Fund investment officer and Fund manager would also want to review the project. The investee would end up repeating and clarifying information at multiple levels. It could be confusing for the investee and in the end take more time and staff resources than if the company went directly to the Fund.
2. In most circumstances the investee wants to know how the project would be structured, prior to getting too far into the due diligence process. This could only be done by the staff of the Fund.
3. During the initial process of the review, the investment officer gets a “feel” for the company, the management, the business acumen and in doing so builds a rapport with the investee. This would not happen if this part of the process was outsourced.
4. Outsourcing the monitoring when the investee knows and trusts the investment officer would be difficult. Building the trust and a partnership with an investee, by the Fund, will be important to the success of the investment. Monitoring the investment on an ongoing, regular basis will enable the Fund to respond to potential problems in a timely manner.

SBI believes, however, in developing reliable referral sources. A number of the technical assistance organizations provide services to companies that are in need of alternative forms of financing. It is recommended that the Fund provide these organizations referral forms that provide the Fund with sufficient information to know whether to pursue a project. The organizations can receive a short training on what the Fund is looking for in its investees and thereby enable the organizations to better “vet” their clients. It is also recommended that the referral source receive Referral Fees; a small amount for the initial referral and a larger amount upon the funding of a project. The projections include a \$250 referral fee and \$750 if the project is funded for 50% of the projects. The other 50% will most likely be referred to the fund by institutions that do not accept referral fees (government agencies and fund investors for example).

SBI recommends for the above reasons that the Fund not outsource the initial analysis or monitoring of investments and rely instead on in-house staff. Development of marketing and referral channels will be a more reliable way to boost pipeline and deal flow. This will maintain the initial and ongoing relationship of the investment officer with the investee, which in SBI’s experience has proven to benefit the investee and portfolio performance overall.

Deal Flow

The following is a brief process flow recommended by SBI from origination, to closing and monitoring, and exit of the investment:

1. Referral with pre-evaluation - this would be done by one of the organizations trained in pre-screening potential projects. Proper documentation would accompany the referral.
2. Investment officer reviews referral information.
3. Investment Officer meets with the client who completes the application.
4. Due diligence.
5. Site visit.
6. Preliminary non-binding proposal.
7. Preparation of investment memorandum.
8. Investment committee presentation and approval.
9. Term sheet.
10. Documentation and disbursement.
11. Monitoring.
12. Exit.

Marketing

The Fund should develop a network of referral sources that will assist in maintaining a healthy pipeline of deals. These include export technical assistance organizations, export business groups, accounting and legal firms, government agencies, small business consultants, banks and the Fund's investors. In addition, the Fund should develop promotional materials. The promotional material should be clear in the type of businesses eligible for investments and the application requirement.

Marketing of the Fund's investments will require constant effort on the part of the management of the Fund and each investment officer. Marketing should focus on both existing and potential new clients. The Fund should develop a comprehensive, yet flexible Marketing Plan.

Operations

If we are to assume the core investment functions are carried out by the Fund Manager (without outsourcing of initial due diligence and monitoring) SBI recommends a core investment team of a Fund Manager, one seasoned Investment Officer, and two investment analysts. The Fund would also require administrative support (office manager and help). The Fund could use outside legal counsel for the closing of investments and other legal advice as needed as well as outside accounting services for the Fund accounting, and other professional services as needed for marketing and promotions.

We are assuming the Fund will rent an office and operate separately from other institutions to maintain an independent identity. However, it will partner and collaborate with local institutions, in particular USAID-EXPRO and technical assistance providers mentioned above.

Financial Projections

In preparing the financial projections, the SBI team considered the information noted above in market demand on the list of potential investees, the percentage of those that apply that actually get funded (10-15%) and the average number of transactions of similar investment funds in the region. We are presenting a Base Case, a Pessimistic Case and Optimistic Case as seen in the Financial Projections document, a separate Excel spreadsheet, and described below.

The following assumptions were made in construction of the financial projections, which are presented in Excel format under separate cover.

- Shareholders Investments. These are projected on an "As Needed Basis" regarding the number of expected deals according to the chosen Fund's deal flow scenario. Every shareholder investment is projected in the amount of \$2 million dollars; the Fund will always start with \$2 million dollars that will cover the initial establishment costs, the ongoing administrative expenses while the Fund generates its own operative cash flow, and the initial expected deals. The shareholders' investments

will change according to the Fund's deal flow scenario chosen, as well as the overall fund's size (\$10 millions in the Optimistic Scenario, \$8 million in the Base Case Scenario, and \$4 million in the Pessimistic Scenario).

- Fund's Payback Scenario. There are two possible scenarios for payback to investors, either to repay the investors at Fund's closing in year 10, or start repaying them starting year 6, when fewer new deals will be funded. The Fund's model default scenario will always start paying back in year 6.
- One Time Acquisitions and Expenses. These are the expenses required to legally set up the Fund (\$15,000 USD), establish its manuals and formats (\$15,000 USD) and acquire its fixed assets (\$65,000 USD, 46% for the office furniture and equipment, 23% for computer equipment and 31% for a service vehicle); as well as to legally close the Fund at year 10 (\$10,000 USD).
- Staff Expenses. Based on experience, SBI estimated the number and type of personnel necessary to manage a fund of the proposed size. The salary costs are based on information obtained while in El Salvador. It will require a Fund Manager that earns an average gross monthly salary of \$5,000 dollars, a Portfolio Manager at \$4,000 dollars, an Investment Officer at \$3,000 dollars, two Financial Analysts at \$1,500 dollars each, an Office Manager at \$800 dollars, and a Cleaning Person at \$450 dollars. Fund's staff should be awarded a yearly bonus according to the Fund's performance that ranges from half a gross monthly salary up to two gross monthly salaries; the projected bonus of the model has been set at one gross monthly salary. The Social and Pension cost are projected according to San Salvador's fiscal requirements.
- Ongoing Administrative Expenses. The Fund will face the following ongoing monthly expenses in US dollars:

Monthly Fund's Trust Administration Fee	2,500
Ongoing Legal Fees	500
Outsourced Accounting Services	500
Technical Assistance for Clients	500
Office Rent	2,000
Utilities: Electricity	600
Utilities: Water	35
Fixed Telephone Line	400
Cell Phones	300
Internet Service	300
Office Supplies	250
Equipment Maintenance	150
Outsourced Security	800
Wire/Bank Fees	100
Promotion / Hospitality	100
Marketing - Advertising Expenses	400
Car Maintenance and Gas	300
Travel Expenses for Pipeline Development	150
Miscellaneous	739

The Fund will also have the following yearly expenses: a) \$12,000 dollars for the administrative and fiscal audits of its financials and b) \$3,500 dollars for the private medical insurance policy of its staff, at \$500 dollars per employee.

- Overall Fund Manager Costs. Based on the assumptions, overall costs of the Fund Manager are expected to run approximately \$370,000 per year, or 4.6% of total committed capital for the Base Case Scenario.
- Carried Interest. It is assumed that the Fund Manager receives additional performance based compensation in the form of a Carried Interest of 20% of the fund returns following a minimum payout of 8% IRR to the Investors. This only occurs in the current projections in the Optimistic Case Scenario.
- Earnings on Idle Funds. Idle cash flows are expected to generate at least 1 month LIBOR as interests. The projected interest rate of 1 month LIBOR is 3.22% in the fund's model.
- General Deal's Assumptions. A 10 to 1 evaluation rate per deal approved is projected, and it is also expected that 1 out of 2 approved deals will be referred by institutions that will be paid a "Referral

Fee” of \$250 dollars per deal at the time of referral and \$750 dollars when funded. It is also projected that 7.5% of the Fund’s portfolio will not be recovered.

- Standard Deal during Round 1. These are Quasi-equity type deals made during months 1 through 30 of the life of the Fund. They are projected to generate an average 20% IRR over a 6 year term including a 1 year grace period. The repayment schedule is projected on a monthly basis. These deals include a 1.5% structuring fee charged at approval and a 1.0% annual monitoring fee.
- Standard Deal during Round 2. These are also Quasi-equity type deals made during months 31 through 60 of the life of the Fund. They are projected to generate an average 20% IRR over a 5 year term including a 1 year grace period. The repayment schedule of these deals is projected on a monthly basis. They include a 1.5% structuring fee charged at approval and a 1.0% annual monitoring fee.
- Standard Deal during Round 3. These deals are Loans made during months 61 through 84 of the life of the Fund. They are projected to generate an average 15% IRR over a 3 year term including a half year grace period. The repayment schedule is projected on a monthly basis. The loans also include a 1.5% structuring fee charged at approval and a 1.0% annual monitoring fee.
- Deal’s Flow Scenarios. There are three automatic Deal’s flow scenarios to choose from: a) Base Case, 40 deals during the first 5 years of the life of the Fund, b) Optimistic, 60 deals during the same period, and c) Pessimistic, 20 deals. The breakdown of deals per Round of deals is projected as follows:

	Base Case Scenario	Optimistic Scenario	Pesimistic Scenario
Deals Round 1	20	30	10
Deals Round 2	12	18	6
Deals Round 3	8	12	4
Total Deals	40	60	20

The overall performance of the Fund is determined by the Internal Rate of Return (IRR) that the Fund’s Investors will obtain on their original investments given the cumulated cash flow generated by the Fund before any Tax Obligations it may encounter once the investment vehicle is chosen. The projected IRR given the 3 different scenarios automatically inputted into the model are as follows:

- Base Case Scenario: 7.51% IRR
- Optimistic Case Scenario: 9.93% IRR
- Pessimistic Case Scenario: 0.61% IRR

Risks and Mitigants

In reviewing the viability of a Small Business Export Fund, the SBI team has noted the following risks, which need to be thoroughly weighed and examined in the course of structuring and closing of the Fund.

Risk	Mitigant
Limiting the fund to export companies only: While there is good indication there are numerous exporting companies that would meet the criteria of the Fund, possible other investment worthy companies would be excluded, limiting the Fund and the businesses in opportunities.	The Fund could target export companies but not limit investments strictly to export companies
A number of the export companies reviewed by the SBI team are closely tied together in brand names. In addition, these	Research on the investee’s customer plus written assurance from the customer

<p>companies' exports are currently to a single customer and have the potential to be controlled by the customer. This would be an investment committee decision, but could limit the potential number of investees.</p>	<p>could lessen this concern along with the potential of new markets.</p>
<p>The companies reviewed are receiving significant assistance from USAID-EXPRO, which has only one and a half years or less of funding (project is scheduled to run through June 2009). What will happen to this project and their clients will be important to consider if the investee is receiving assistance from them. This would be true of any investee that is dependent upon outside technical assistance.</p>	<p>There is a possibility the program could be extended or that a technical assistance fund be established in conjunction with the Investment Fund. If EXPRO is not extended clients would have the opportunity to work with other existing organizations such as FOEX, EXPORT or COEXPORT.</p> <p>These deals should also be shorter in term. Knowing that many of the skills have been transferred from the assisting organizations to the trading companies should also reduce the risk</p>
<p>A good strong pipeline of deals is important to the fund. Using referral sources can be the most efficient and effective way to build the pipeline. The referral sources will have to be clear as to what the Fund is looking for as an investee. Referral fees should be established based on quality of referrals (perhaps a small upfront fee at the time of referral and a larger fee at funding, based on the amount of the investment). Caution should be used in developing a pipeline too early as expectations could be raised among the referral sources and potential investees with no immediate results and possibly hurting the credibility of the Fund.</p>	<p>Referral forms should be developed and training/marketing sessions given to referral sources so neither the referral source, client nor the Fund wastes time with an inappropriate referral.</p>
<p>Technical assistance is important to small and medium sized businesses, especially those experiencing high growth. It is important to the business and the Fund for the investment to be successful.</p>	<p>A technical assistance fund and/or plan (agreements with providers) should be in place at the time the Fund is launched.</p>
<p>The strategic interested parties to this fund and "core" investors should act quickly in order to establish the fund, with firm commitments of money, so as to "sell" others on the opportunity to invest, while the momentum is strong. The next year, 2009, is election year in El Salvador and if the Fund is not established by the end of 2008, attention of the interested parties could be diverted and thus delay the establishment.</p>	<p>The interest is high among the key investors and other sponsors of the Fund. SBI would be willing to provide any "next step" assistance to help launch the Fund during 2008.</p>

SUMMARY

A Small Business Investment Fund will complement and enhance the existing array of financial services now available to the small and medium enterprise sector. It will fill a gap in financing that often SMEs face when they are in a state of high growth. The Fund should target investments of \$100,000 to \$500,000, generally higher amounts and more flexible terms than these businesses can obtain through traditional banking instruments, yet too small for the existing investment funds. Because of the costs involved in “booking” the investment, the Fund should look for medium to longer term investments with self-liquidating exits.

The “core” group of investors should act with resolve to have the Fund launched in 2008, while the interest is high among the advocates of such a Fund and prior to the Presidential elections in 2009, which could have a distracting effect. Decisions including the minimum size of fund, type of fund, and selection of the Fund Manager will need to be made. Risks and how to mitigate them need to be understood.

Marketing materials should be developed and a marketing strategy set up, which would include investor organizations, other potential referral sources and referral fees and forms to be used.

Technical assistance should be required for all investees. This could be on a shared basis by the Fund and the investee and/or involve a third party sponsorship. Discussions with organizations that might be able to provide technical assistance for investees or possibly a sponsor that would provide funding for investee technical assistance should be found.

Cash flow projections contain three scenarios – base case, optimistic case and pessimistic case. Based on experience of SBI managed funds and other SME funds around the world, SBI believes the base case projections reflect the most likely situation. In this scenario, the Fund would require an \$8 million investment by investors and would close 40 investments over the life of the Fund. Approximately 7.5% of the amount funded would not be recovered. The IRR for the base case is projected at 7.51%.

There are always risks associated with financing small and medium sized businesses, but with appropriate due diligence up front, proper structuring and close monitoring of the investments, the risks should be manageable. Constant marketing, in order to keep the pipeline full, should allow the Fund to meet its target in number of investments.

ANNEX I: Establishment of a Local Trust Fund

Details on establishing a Local Trust Fund in El Salvador as provided by Mr. Luis Medina of Rusconi, Valdez, Medina & Associates, Central Law

We have conducted an interview with representatives of the BMI “Banco Multisectorial de Inversiones” about the feasibility of establishing a local trust fund. BMI representatives explained to us that in order to form a trust fund, in general, the following steps must be completed:

1. Define the purposes of the trust fund; this will help to choose the type of trust fund that will be established i.e. managing trust or security trust.
2. According to the type of trust fund chosen BMI can perform the following tasks depending on the preferences of the client: a) Management of the Fund; b) Establishment of the fund and granting credits; c) Management of the treasury; d) Management of Guarantees or Securities of loans.
3. BMI elaborates a document that contains the responsibilities that each of the parties will acquired and the rules under which the trust fund will operate. This document can be called “Bylaws of the Trust Fund”
4. BMI representatives present the Bylaws of the Trust Fund to the Board of Directors of the BMI.
5. The Board of Directors of the BMI approves the establishment of the trust fund and its bylaws.
6. Once the approval is issued the BMI can establish the trust fund and receive the amount of money projected for the fund.

This is preliminary information since we are still waiting for the evaluation on the cost that the representative of the BMI will give us.

ANNEX II: Survey Results

YEARS ESTABLISHED	TYPE OF BUSINESS	FEELINGS TOWARDS BANKS	WHAT IT LOOKS IN A FINANCING	CURRENT CONDITIONS FROM PREVIOUS LOANS	IDEAL CONDITIONS	FINANCING NEEDS
> 1 year	Medical Services to Foreigners	High Interest Rates Little Grace Period	1. Interest Rate 2. Amount 3. Term 4. Service & Speed 5. Collateral	Bank 1. Int. Rate: 11% - 23% 2. Term: 15 years 3. Amount: \$200K 4. Collateral: Mortgage	1. Int. Rate: 3% 2. Term: 10 years 3. Amount: \$500K 4. Collateral: Mortgage	Working Capital Real State Acquisition
5 years	Honey and Pharmaceutical Products Exporter	Don't meet needs / no specific mentions	1. Interest Rate 2. Term 3. Amount 4. Collateral 5. Reliability	N/A	1. Int. Rate: Lower than Banks	Working Capital Equipment
3 years	Pesto and Vinaigrette Exporter	Do not grant financing based on projected cash flows or with little or no track record Financing granted less than required	1. Interest Rate 2. Amount 3. Collateral 4. Term 5. Service & Speed	Bank 1. Int. Rate: 20% 2. Term: 1 years 3. Amount: \$100K	1. Int. Rate: 7% 2. Term: 5 years 3. Amount: \$200K 4. Collateral: Account Receivables 5. Response Days: 20 days	Working Capital Equipment Construction Real State Acquisition
15 years	Ceramic Exporter	Don't meet needs / no specific mentions	1. Service & Speed 2. Reliability 3. Amount 4. Collateral 5. Term	N/A	1. Int. Rate: 2. Term: 90-120 days 3. Amount: \$250K 4. Collateral: Finished Product & Buying Orders	Factoring
14 years	Orthodontist	Don't meet needs / no specific mentions	1. Interest Rate 2. Term 3. Collateral 4. Service & Speed 5. Technical Assistance	Bank 1. Int. Rate: 7.9% 2. Term: 15 years 3. Amount: \$130K 4. Collateral: Mortgage	1. Int. Rate: 6% 2. Term: 10 years 3. Amount: \$400K 4. Response Days: 5	Equipment Construction Real State Acquisition
5 years	Frozen Food Exporter	Banks don't match risk with collateral	1. Collateral 2. Amount 3. Term 4. Reliability 5. Service & Speed	N/A	1. Int. Rate: 2. Term: 7-10 years 3. Amount: 4. Collateral: Project	Working Capital Equipment Construction
1 year	Medical Services to Foreigners	Do not grant financing to new business	1. Term 2. Interest Rate 3. Reliability 4. Collateral 5. Service & Speed	N/A	1. Int. Rate: 3% 2. Term: 15 years 3. Amount: \$300K	Working Capital Equipment Construction Real State Acquisition

ANNEX III: Focus Group Results

San Salvador
USAID-EXPRO Offices
February 7th. 2008

Focus Group with Salvadorian Exporting SMEs

SBI's Consultants working in San Salvador at the Pre-feasibility Assessment of a Quasi-Equity Fund for Exporting SMEs held a reunion with 7 owners of exporting SMEs at USAID-EXPRO offices that are currently being helped by USAID-EXPRO.

The purpose of the Focus Group was to gather direct information from potential users of the Quasi-Equity Fund regarding the general conditions of current financing offered by Salvadorian Banks to SMEs in case such exist and their feelings towards the opening of a Quasi-Equity Fund in the region, such as expectations or concerns.

There is a general feeling among SMEs in El Salvador that banks are not easily granting financing, even though all SMEs participating in the Focus Group acknowledge that new collateral-backup programs granted by the government were at place and beginning to work, however many SMEs still can't access such programs and lack enough collateral to access bank's financing. On the other hand, bank's current approval guidelines are not really based on the collateral offered as it used to be. Overall, current bank's financing has the following perception among SMEs:

- a) There is no available financing from banks to businesses that has less than two years of establishment; these types of businesses must rely on equity financing from family and friends, credit unions or informal loans at very high interest rates.
- b) Bank's financing is not easy to access and is perceived as expensive. Its cost never reduces even if the debtor shows good history and behavior over the term of the loan.
- c) There is a big concern among businesses regarding confidentiality from banks and financial institutions since it is common that projects presented to them in request of financing end up being developed by other entities.
- d) Bank's financing is not flexible, sometimes the financing obtained is nor enough to cover the whole project cost and the repayment schedule is not paired with its cash flow generation.

The idea of a Quasi-Equity Fund among SMEs is perceived as positive if the financing it grants is flexible in terms of adequacy to meet the needs of the projects being financed by it regarding amount, term and repayment schedule needed. Even though cost financing is mentioned as a main concern among SMEs, they will be willing to share their profit and pay an adequate IRR to a financing institution if the financing obtained meets their needs as mentioned, the sharing of the profit is paired to the cash flow generation of the project and the financing institution provides Administrative and Financial Technical Assistance to the business it funds while leaving the operation and know-how of the business to it debtors.

ANNEX IV: Legal Opinion on Fund Structure and Investment Instruments

The following information was provided by Mr. Luis Medina of Rusconi, Valdez, Medina & Associates, Central Law

I. FUND STRUCTURE:

Description of Alternatives:

1. INCORPORATION OF A STOCK CORPORATION IN EL SALVADOR

General Requirements.

To incorporate a stock corporation (SOCIEDAD ANONIMA), Salvadoran law requires the minimum capital stock to be of ¢100.000.00 (COLONES) equivalent to US\$11,428.57; at least 25% of this amount has to be paid at the moment of incorporation of the new corporation.

According to El Salvador's Commercial Code, the initial capital contributions shall be certified by public Notary during the elaboration of the Articles of Incorporation "Escritura Pública de Constitución", usually this is done through the presentation before the Public Notary of a certified check, issued by a Salvadoran bank, on behalf of and in the name of the corporation that will be formed.

In order to prepare the Articles of Incorporation it is necessary to determine the following aspects:

- a) Name of the corporation: The chosen name must first be checked at the Registry of Commerce to determine its availability.
- b) Domicile of the corporation: Generally, is recommended to be the city where the main offices of the company will be settled.
- c) The initial capital.
- d) Given that our law requires at least two shareholders in order to incorporate a corporation, it is necessary to provide these two names and their respective percentages of distribution of capital stock subscription. The law allows one of the shareholders to subscribe only one share, if needed. Any shareholders can be of a foreign nationality.
- e) Corporation Management: The management of the corporation can be performed by a Board of Directors or by a Single Administrator "Administración Unica". The President and Secretary, or the Single Administrator, are usually the Legal Representatives of the Corporation.

In the event that the definitive shareholders can not be present to execute the Articles of Incorporation, third people can appear on their behalf through a means of a Power of Attorney.

The estimated time to register the Articles of Incorporation at the Registry of Commerce takes between 5 to 7 working days.

After registering the corporation at the Registry of Commerce it is necessary to file for the company's tax identification number and the tax-payer number before the Ministry of the Treasury. Additionally and upon the recording of the opening balance sheet, the corporation must request a

business and commercial license “matricula de comercio y establecimiento” at the Registry of Commerce; this certificate allows for the corporation to perform commercial activities.

In order for the corporation to obtain the qualification of employer, and to allow the Company to make the correspondent discounts to its employees in El Salvador, it has to be registered before the Ministry of Labor and at the Social Security Institute “Insituto Salvadoreño del Seguro Social”.

The commercial and corporate books have to be authorized by an external auditor, duly appointed by the Shareholders. This authorization might take approximately three to five working days.

Other important fact is that through the Foreign Investment Protection Law “Ley de Protección a la Inversión Extranjera” the investors can obtain special protection for their investment by registering its capital at the National Investment Office “Oficina Nacional de Inversiones”; this registry guarantees special legal protections such as free repatriation of profits. Although El Salvador, at the moment, does not have any restrictions to the movement of capitals, it is a wise decision to obtain protection for the investment offered by said law.

2. INCORPORATION OF AN OFFSHORE COMPANY

In order to incorporate an offshore company, the person or corporation who wants to create a new offshore corporation must provide some basic and initial information. The specific requirements to be met depend upon the jurisdiction on which the company will be chartered. However, in general the following is a list of what is typically needed.

In case that the initial shareholder of the corporation is an institutional entity, the following internal documents of the shareholder are needed: a) Articles of Incorporation; b) Incorporation Certificate or Chartering issued by the respective Registrar; c) A list of the names and addresses of the shareholders, directors and officials or any person authorized as its legal representatives; d) Copies of the passports of the person who acts as Legal Representative; e) Copy of auditor’s most recent report; f) Copy of the Director’s appointment resolution; g) Resolution that authorizes the institutional entity to incorporate an offshore company.

Additionally, the following reference letters are also needed: a) two letters of reference issued by a bank, in which it declares the date since the corporation who is requesting the incorporation of the foreign corporation, has been their client; b) One letter of reference issued by a lawyer, certified public accountant or a financial advisor, or a business reference in which they declare the date since they have known or initiated business with the person or corporation requesting the incorporation; and c) Brief curriculum that includes relevant information such as complete address, education, principal businesses, profession, etc.

Once these requirements have been fulfilled, it is necessary to decide on some matters that shall be incorporated on the Articles of Incorporation such as the followings:

- a) Jurisdiction of the new corporation: For example, Panama, Sychelles, Bahamas, BVI among others.
- b) Name of the corporation: This has to be checked prior to the determination of its availability.

- c) Authorized capital: The minimum authorized capital varies in each jurisdiction as follows: For Panama the authorized capital of the corporation has to be of at least US\$10,000 distributed in 100 shares of a nominal value of US\$100 each. The directors shall be duly empowered to issue nominative or bearer shares whatever works best for the corporation; for BVI and Bahamas the authorized capital has to be of at least US\$50,000 distributed into 50,000 shares of a nominal value of US\$1 each. The directors will have to be duly authorized to issue nominative shares; for Seychelles and Samoa the authorized capital has to be of at least US\$50,000 distributed into 50,000 shares of a nominal value of US\$1 each. The directors will have to be duly authorized to issue nominative or bearer shares; however it is possible to incorporate any corporation with an amount of capital superior from the ones established above.
- d) Name and number of the corporation's directors: In Panamá it is required to have at least three directors and three officers (President, Treasurer and Secretary. These three directors can be appointed as officers as well). The Directors and Officers can be either corporations or a person. It is mandatory to register at the Public Registry the initial appointments of Directors and Officers as well as its amendments.
- In BVI and Samoa it is possible to appoint only one director, who can be a person or a corporation, and there is no need to register the initial appointments of directors at the Public Registry; however a copy of the director's registry must be kept at the registered office.
- Additionally BVI does not require by law to appoint any officers, but it is recommended to appoint a Secretary. In Samoa it is necessary and mandatory to appoint a Secretary.
- In Seychelles and Bahamas it is possible to appoint only one director who can be a person or a corporation. The law of both jurisdictions does not obligate to appoint any officers but it is recommended to appoint a secretary.
- Under the regulations of Seychelles Law there is no need to register the initial appointments of directors at the Public Registry; however under the laws of Bahamas it is mandatory to register at the Public Registry a copy of the Directors registry or any amendment.

In addition to these requirements if the corporation belongs to the jurisdiction of BVI or Bahamas it is necessary to file for a corporate seal.

Once the corporation's articles of incorporation have been executed they have to be registered at the Public Registry of the chosen jurisdiction.

II. LEGAL VEHICLES FOR INVESTMENT.

Description and legal feasibility of Alternatives:

1. PURCHASE OF PREFERRED SHARES.

El Salvador's Commercial Code allows the stock corporations to represent and divide its capital into different classes of shares, as well as to establish the rights and obligations that each class of shares will bear and incorporate; however it is not allowed to establish a class of share that would exclude its holders from receiving corporation's profits.

Generally, each shareholder is entitled to one vote at the Shareholders General Assembly, however the corporation's articles of incorporation can establish the issuance of preferred shares with limited vote, by which the preferred shareholders are limited to vote uniquely and exclusively at Shareholders' Extraordinary Assemblies, and not at the Shareholders' Ordinary Assemblies. This means that a holder of a preferred stock will have no voting rights to approve the financial statements of the company, among other matters.

Although the above represents in itself a limitation, the law privileges the preferred stockholders. Regarding the distribution of dividends the law establishes that those Shareholders with preferred shares with limited vote will be entitled to receive the dividends before the common stock shareholders receive them; furthermore, the law also establishes that the dividends for the preferred shares with limited vote cannot be less than six percent of the nominal value of the shares. If at the end of the fiscal year the dividends are inferior to the six percent, the shareholders will be covered and paid in the upcoming years with preference to the common shareholders.

The Salvadoran law also allows to stipulate in the Articles of Incorporation the possibility to assign to the preferred shares with limited vote a dividend superior from the one assigned for the common shares.

In the event that the corporation ceases to distribute for two or more fiscal periods, consecutives or not, preferred dividends to the preferred shares with limited vote, its holders will acquire the right to vote in the Ordinary General Assembly, and all the other rights that the common shareholders are entitled to. These rights will be kept by the shareholders of preferred shares until the unpaid dividends are distributed to them.

The preferred shareholders with limited vote shall have the same rights that the Commercial Code grants to the minority shareholders regarding to the right to review the balance sheets of each fiscal year, as well the right to review the commercial and corporate books of the company. More importantly, they also have the right to challenge at a Court level, any decision taken in General Assembly that could affect their rights. This action can be used by the preferred shareholders with limited vote as long as these two requirements are fulfilled:

a) The reason for challenging must be found in a breach of the law or a breach to the Company's Articles of Incorporation; and, b) The challenged resolutions cannot be about changing the administrators' responsibility.

The law further establishes that any restriction made to the voting right of the shareholders will enable them to have the above mentioned rights.

The Salvadoran Commercial Code does not establish a limitation on the rights that can be granted or assigned to a preferred share; therefore under our legislation it is feasible to establish preferred shares with preferred dividends rights, as a result the holders of the preferred shares will be entitled to be paid first than the common shareholders. In the particular case of Small and Medium Enterprises "SMEs", whose commercial activity is centered in the exporting of good or services, the SMEs can establish preferred shares that hold the right to preferred dividends that result from the exporting activity.

The purchasing of preferred shares with preferred dividends rights is understood as a mechanism for investors to recover the investment made in SMEs business, since by the purchase of the preferred shares they will acquire the right to be paid first with the earnings made from the exporting business, regardless if there is not enough earnings to pay or distribute to the common shareholders.

In order for the investors to make available this alternative, they have to enter into an agreement with the SMEs where the investors agree to provide “x” amount of investment and the SMEs agree to secure their obligation of payment by selling to the investors preferred shares with preferred dividends; additionally, an agreement to make the necessary amendments to the Articles of Incorporation in order to incorporate the said preferred shares must be reached.

2. IMPLEMENTATION OF A “REVERSE MERGER” PROCEDURE.

By this mechanism a foreign company can acquire control of a Salvadoran company, which simultaneously allow for the shareholders of the Salvadoran company to become a shareholder of the foreign corporation. This mechanism also requires a reorganization of capitalization of the offshore company .

One simple mechanism to achieve a reverse merger would be through a capital increase. The offshore resolves an increase of capital, and authorizes that such increase be paid with the stock of the Salvadoran corporation. At the end, the offshore company would become the majority shareholder of the Salvadoran corporation.

By authorizing the payment of its newly issued stock to be made in kind, the offshore company facilitates the investment of new shareholders (those of the Salvadoran corporation) into the foreign corporation.

The implementation of the reverse merger would allow for the foreign corporation to become shareholder of the Salvadoran corporation, and all equity contributions to be made by the investors in the offshore company will be channeled to the Salvadoran company as shareholder contribution that would be used for working capital.

The reverse merger is not expressly or particularly considered in the law; however it is not prohibited, since our law has not established any limitation regarding the percentage of participation that a foreign corporation can have in the capital stock of a Salvadoran corporation.

Although family businesses have legal existence under the Salvadoran law (Sociedades de Personas o Registros de Empresas Individuales), we are of the opinion that they do not constitute an appropriate legal vehicle to place or recover an investment, given that their legal treatment differ from the one given to shareholders in stock corporations. More importantly, they have very limited options regarding the transfer of stock since the law establishes that the partners of a family business cannot transfer their participations without the previous authorization from the other partners; therefore we recommend to consider either the establishment of a new corporation with preferred shares or a reverse merger to be made with a stock corporation.

3. CONVERTIBLE DEBT.

This is the mechanism by which a debt obligation, that has result from a credit agreement, can be turned into equity, generally upon the occurrence of future financing.

In this mechanism the debtor issues securities that might be converted at the option of the owner into shares of the issuer, the conversion of these securities is usually made at a pre-determined rate.

According to financial sources, the convertible securities (bonds, promissory notes, etc) are safer than preferred or common shares for the investor, since they could provide certain asset protection. At the same time, convertible securities can provide the possibility of high equity-like returns, and are usually less volatile than regular shares.

In Salvadoran legislation the option to convert debt into equity would imply that the holder of a security be a shareholder in the corporation. Upon the exercise of the option, the holder of the security would become a shareholder with a higher equity participation.

In order to make the convertible debt feasible for the investor as well as for the debtor we recommend that both parties previously discuss the terms under which the convertible debt will apply (i.e. the financial circumstances under the debt can be converted, the conversion ratio, etc) and the terms of credit agreement with convertible debt as a collateral to secure the payment obligation.

In our opinion the parties must incorporate into the credit agreement a clause which regulates the right of the creditor to convert a debt into equity. The decision of converting an obligation implies that the investor can decide whether to convert all or part of the unpaid debt, furthermore once the financial event set for the conversion of debt is reached, the investor has to decide whether to convert its debt or keep the convertible security.

III. CONDITIONS PRECEDENT, REPS & WARRANTIES, COVENANTS TO PROTECT AND EVENTS OF DEFAULT (FORECLOSURE OF LOANS)

If a decision to invest through a credit agreement is made, we recommend taking into consideration the following (and any other as typical to credit agreements):

Conditions Precedent to any disbursements:

- (a) The lenders shall have a valid and perfected first-priority security interest in the collateral before any disbursement is made. We recommend as collaterals to consider mortgage over the corporation; pledge over shares, and corporation's intellectual property.
- (b) The lenders shall be satisfied with the corporate and legal structure and capitalization of each loan party.
- (c) The lenders shall be satisfied that all existing debt of the borrowers has been prepaid, redeemed or defeased in full or otherwise satisfied and extinguished.
- (d) The lenders shall have completed a due diligence investigation of the company of the borrowers.
- (e) There shall have occurred no event or circumstance that i) could result in a material adverse change (to be defined), ii) could have a material adverse effect (to be defined) on the ability of any borrower to meet its respective obligations under any loan document or material

contract to which the borrower it is a party, or iii) in the sole opinion of the lender is likely to be materially adverse to the international or Salvadoran economy.

- (f) The representations and warranties of each party to any loan document shall be true and correct as of the effective date and no event of default shall have occurred or would occur upon the consummation of the Borrowing.
- (g) The lenders shall have received each of the following in form and substance satisfactory to the Lenders: i) the audited consolidated financial statement of the Salvadoran loan parties, certified by the Chief Financial Officer of each Salvadoran Parent Company; and ii) pro forma consolidated financial statements, business plan and forecasts of each of the Salvadoran loan parties, including balance sheets, income statements and cash flow statements prepared on an annual basis.
- (h) There shall exist no action, suit, investigation, litigation or proceeding pending or threatened in any court or before any arbitrator or governmental instrumentality that i) could reasonably be expected to have a Material Adverse Effect or ii) purports to affect in a manner adverse to the lenders the legality, validity or enforceability of any loan document or the consummation of the transactions contemplated thereby.
- (i) The lenders shall have received on or before the effective date the following:
 - (i) Notes of documents of said nature.
 - (ii) Corporate authorizations.
 - (iii) Copies of the organizational documents.
 - (iv) The Guaranty, duly executed by each of the Guarantors.
 - (v) The Mortgages duly executed by the Borrowers.
 - (vi) The Pledge Agreements duly executed.
 - (vii) A favorable opinion of the counsel of the Loan parties as to such matters as any Lender may reasonably request.

Representation and warranties to be made by Borrowers:

- a) That the Borrower i) is a corporation duly organized, validly existing and in good standing under the laws of El Salvador, iii) has all requisite corporate power and authority (including, without limitation, all governmental licenses, permits and other approvals) to own or lease and operate its properties and to carry on its business as now conducted and as proposed to be conducted. All of the outstanding capital stock of such Borrower has been validly issued, is fully paid and non-assessable and is owned in the amounts that their shareholder registry shows. That the outstanding capital stock of such Borrower is free and clears of all liens.
- b) The execution, delivery and performance by such Borrower of each loan Document to which it is or is to be a party, and the consummation of the transactions are within such Borrower's corporate powers, have been duly authorized by all necessary corporate action,

and do not contravene such Borrower's organizational documents, violate any law, rule, regulation, order, writ, judgment, injunction, decree, determination or award, conflict with or result in the breach of, or constitute a default under, any contract, loan agreement, indenture, mortgage, deed of trust, lease or other instrument binding on or affecting such Borrower or any of its properties

- c) The credit agreement is, and each of the Term Notes and each other Loan Document to which such Borrower is a party when delivered will be, the legal, valid and binding obligation of such Borrower, enforceable against such Borrower in accordance with its terms;
- d) No information, exhibit or report furnished by such Borrower to any Lender in connection with the negotiation of the loan documents or pursuant to the terms of the loan documents contained any untrue statement of a material fact or omitted to state a material fact necessary to make the statements made therein not misleading.
- e) There is no action, suit, investigation, litigation or proceeding, including any Environmental Action, pending or threatened before any court, governmental agency or arbitrator that could reasonably be expected to have a Material Adverse Effect or purports to materially affect the legality, validity or enforceability of the credit agreement, any Note (if issued), or any other loan document.
- f) The operations and properties of such Borrower comply in all material respects with all applicable Environmental Laws and Environmental Permits, all past material non-compliance with such Environmental Laws and Environmental Permits has been resolved without ongoing obligations or costs, and no circumstances exist that could form the basis of an Environmental Action against such Borrower or any of its properties that could have a Material Adverse Effect or cause any such property to be subject to any material restrictions on ownership, occupancy, use or transferability under any Environmental Law.
- g) Such Borrower is not a party to any indenture, loan or credit agreement or any lease or other agreement or instrument or subject to any charter or corporate restriction that, in each case, could have a Material Adverse Effect.
- h) The Collateral Documents create a valid and perfected first priority security interest in the Collateral, securing the payment of the Obligations owing to the Lenders under the Loan Documents, and all filings and other actions necessary or desirable to perfect and protect such security interest set forth therein have been duly taken. Such Borrower is the legal and beneficial owner of the Collateral pledged by it under the Collateral Documents free and clear of any Lien.
- i) Such Borrower has filed, has caused to be filed or has been included in all tax returns (national, departmental, local, municipal and foreign) required to be filed and has paid all taxes shown thereon to be due, together with applicable interest and penalties except for taxes contested in good faith by appropriate proceedings and as to which appropriate reserves have been made on its books.
- j) Neither the business nor the properties of such Borrower are affected by any fire, flood, explosion, accident, strike, lockout or other labor dispute, drought, storm, hail, earthquake, embargo, act of war, act of God or other casualty (whether or not covered by insurance) that could have a Material Adverse Effect.
- k) Such Borrower has obtained insurance with responsible and reputable insurance companies or associations in such amounts and covering such risks as is usually carried by companies of similar size engaged in similar businesses and owning similar properties in the same general areas in which such Borrower operates and as otherwise contemplated in the Collateral Documents.

- l) None of the Loan Parties nor any of their respective property has any immunity from jurisdiction of any court.
- m) The credit agreement, the Notes and the Salvadoran Collateral Documents are in proper legal form under the law of El Salvador for the enforcement thereof against such Borrower under the law of El Salvador, and to ensure the legality, validity, enforceability or admissibility in evidence of the credit agreement, the Notes, and the Salvadoran Collateral Documents in El Salvador. Except for the recordation of the Mortgages at the Registry of Real Property, the recordation of the Salvadoran Pledge Agreements in the Shareholders' or Partners' Registry Books, and the recordation of the Salvadoran Pledges of Borrowers' Assets in the Registry of Commerce, it is not necessary that the credit agreement, the Notes or any Salvadoran Collateral Document or any other document be filed or recorded at this time with any court or other authority in El Salvador or that any stamp or similar tax be paid.
- n) The Borrowers' obligations under the credit agreement and the Notes constitute direct, unconditional, unsubordinated and secured obligations of the Borrowers and do rank and will rank *pari passu* in priority of payment.

Finally, in our opinion the following positive and negative covenants have to be incorporated in the credit agreement:

1. Affirmative Covenants

So long as any Loan shall remain unpaid and outstanding, the Borrowers shall cause each of the Loan Parties to:

- a) Compliance.
 - i) Comply with all applicable laws, rules, regulations and orders, such compliance to include, without limitation, all pension laws and Environmental Laws,
 - ii) obtain and maintain all necessary permits, licenses, authorizations and approvals from any governmental authority or regulatory body or any other third party required in connection with the performance by such Loan Party under any Loan Document or any Material Contract and
 - iii) keep all Material Contracts in full force and effect and comply in all material respects with all of the covenants contained in all such Material Contracts.
- b) Payment of Taxes, Etc. Pay and discharge before the same shall become delinquent and maintain appropriate reserves for
 - i) all taxes, assessments and governmental charges or levies imposed upon it or upon its property and
 - ii) all lawful claims that, if unpaid, might by law become a Lien upon its property; provided, however, that the Loan Parties shall not be required to pay or discharge any such tax, assessment, charge or claim that is being contested in good faith and by proper proceedings and as to which appropriate reserves are being maintained, unless and until any Lien resulting there from attaches to its property and becomes enforceable against its other creditors.
- c) Maintenance of Insurance. Maintain insurance with responsible and reputable insurance companies or associations in such amounts and covering such risks as is usually carried by companies of similar size engaged in similar businesses and owning similar properties in the same general areas in which each Loan Party operates and as otherwise contemplated in the Collateral Documents.
- d) Maintenance of Properties, Etc. Maintain and preserve all of its properties that are used or useful in the conduct of its business in good working order and condition, ordinary wear and tear excepted, and pay or cause to be paid all costs and expenses incurred in connection therewith in a timely manner.

- e) Preservation of Corporate Existence, Etc. Preserve and maintain its existence, legal structure, legal name, rights (charter and statutory), permits, licenses, approvals, privileges and franchises and conduct its business in accordance with prudent business practices.
- f) Inspection Rights. During normal business hours and from time to time, with reasonable notice, permit any of the Lenders or any agents or representatives thereof, to examine the records and books of account of, and inspect the properties of, such Loan Party and to discuss the affairs, finances and accounts of such Loan Party with any of its officers or directors and with its independent certified public accountants.
- g) Keeping of Books. Keep proper books of record and accounts, in which full and correct entries shall be made of all financial transactions and the assets and business of each Loan Party in accordance with Salvadoran or US GAAP.
- h) Compliance with Terms of Real Property Leaseholds. Make all payments and otherwise perform all obligations in respect of all leases of real property to which such Loan Party, as applicable, is a party, keep such leases in full force and effect and not allow such leases to lapse or be terminated or any rights to renew such leases to be forfeited or canceled, notify the Administrative Agent (if such an entity is to be created) of any default by any party with respect to such leases and cooperate with the Administrative Agent in all respects to cure any such default.
- i) Transactions with Affiliates. Conduct all transactions including, without limitation, any purchase, sale, lease or exchange of property or the rendering of any service with any Affiliate of any Loan Party on terms that are fair and reasonable and no less favorable to such Loan Party than it would obtain in a comparable arm's-length transaction with a Person not an Affiliate.
- j) Perfection of Security Interests. Maintain the recording, priority and perfection of the Liens on the Collateral created by the Collateral Documents and keep all collateral free and clear of Liens except for the Liens created under Collateral Documents.
- k) Maintenance of Payment Accounts. Transfer periodically, but in no event fewer once per two calendar weeks, all funds collected from customer receivables to the Salvadoran Payment Account. Maintain at all times during each Interest Calculation Period sufficient funds in the Salvadoran Payment Accounts to make each payment (including scheduled prepayments) under the credit agreement and under the Notes, whether on account of principal, interest, fees or otherwise, to be made by the Borrowers as and when due.
- l) Payment of Fees. Pay all fees set forth in the Fee Letter, in the amounts and on the dates specified therein.
- m) Use of Proceeds. Use the proceeds of the Term Loan solely in the manner and for the purposes established in the loan agreement.
- n) Further Assurances. From time to time, do and perform any and all acts and execute any and all documents as may be necessary or as reasonably requested by any Lender or the insurers in order to effect the purposes of this Agreement or to protect the rights or interests of the Lenders, in the Term Note(s) or under the Loan Documents.

Negative Covenants

. So long as any Term Loan shall remain unpaid, or any Lender shall have any Commitment hereunder, the Borrowers shall not permit any Loan Party to, at any time:

- (viii) Liens, Etc. Create, incur, assume or suffer any Lien on or with respect to any of its properties of any character (including, without limitation, accounts) whether now owned or hereafter acquired, or assign any right to receive income.

(ix) Debt. Create, incur, assume or suffer to exist any Debt, other than:

Debt under the Loan Documents;

Debt outstanding on the effective date of the credit agreement constituting Surviving Debt or Subordinated Debt;

Debt incurred to refinance the Debt under the Loan Documents so long as such refinancing shall be paid in full and effected simultaneous with the incurrence of such Debt;

Trade or other account payables incurred in the ordinary course of business;

The endorsement of negotiable instruments for deposit or collection or similar transactions in the ordinary course of business consistent with prior practice; and

Unsecured Debt incurred in the ordinary course of business for borrowed money, maturing within one year and in aggregate principal amount not to exceed \$?????, at any time.

(iii) Contingent Obligations. Create, incur, assume or suffer to exist any Contingent Obligation except the Contingent Obligations created pursuant to this Agreement.

(iv) Lease Obligations. Create, incur, assume or suffer to exist any obligations as lessee i) for the rental or hire of real or personal property in connection with any sale and leaseback transaction, or ii) for the rental or hire of other real or personal property of any kind under leases or agreements to lease including capitalized leases having an original term of one year or more, that would cause the direct and contingent liabilities of such Loan Party in respect of all such obligations to exceed US\$??? payable in any period of twelve (12) consecutive months, excluding lease obligations reflected on the financial statements of the Loan Parties delivered to the Administrative Agent.

(v) Mergers, Etc. Merge into or consolidate with any Person or permit any Person to merge into it or acquire all or substantially all of the assets of another entity, provided that so long as no Default or Event of Default then exists or would exist after giving effect to such acquisition, such Borrower may acquire all or substantially all of the assets of another entity provided that i) the assets to be acquired are related to the Borrowers' Business and, concurrently with such acquisition, are pledged as Collateral in accordance with the Collateral Documents, ii) such acquisition would not cause the aggregate amount invested by the Borrowers in all such permitted acquisitions made in accordance herewith to exceed US\$????? and iii) such Borrower shall be the surviving legal entity in such acquisition.

(vi) Sales, Etc. of Assets. Sell, lease, transfer or otherwise dispose of any Collateral or any part of its assets other than Collateral (including any capital stock of any Loan Party or any Affiliate of any Loan Party), or grant any option or other right to purchase, lease or otherwise acquire any Collateral or any part of its assets other than Collateral (including any capital stock of any Loan Party or any Affiliate of any Loan Party), other than i) assets no longer used or useful in its operations, (ii) sales of inventory in the ordinary course of the business of the Loan Parties.

(vii) Change in Nature of Business. Make any material change in the nature of the Borrowers' Business as carried on at the date hereof.

(viii) Accounting Changes. Make or permit any change in accounting policies or reporting practices, except as required to comply with GAAP.

(ix) Prepayments, Etc. of Debt. Prepay, redeem, purchase, defease or otherwise satisfy prior to the scheduled maturity thereof in any manner, or make any payment in violation of any subordination terms of, any Debt.

(x) Partnerships. Become a general partner in any general or limited partnership, other than through a limited liability special-purpose vehicle, without the express written consent of the Required Lenders.

(xi) Investments in Other Persons. Make or hold any Investment in any Person, except as provided in the credit agreement.

(xii) Subsidiaries. Create or suffer to exist any Subsidiary, except Subsidiaries listed on the Loan Agreement, or Subsidiaries who will become Guarantors pursuant to the Guaranty.

(xiii) Charter Amendments. Make any amendment or modification of its corporate organizational documents in a manner that could be materially adverse to the rights, remedies or interests of the Lenders or the ability of any Borrower to perform under any Loan Document, or impair the value of the Collateral.

(xiv) Negative Pledge. Enter into or suffer to exist any agreement prohibiting or conditioning the creation or assumption of any Lien upon any of its property or assets other than in favor of the Secured Parties, without the prior written consent of the Lenders, in their sole discretion.

(o) Reporting Requirements

So long as any Term Loans shall remain unpaid or outstanding, the Borrowers (or any Parent Company, as applicable) will furnish, to the Administrative Agent, for distribution to the Lenders:

- i) Default Notice. As soon as possible and in any event no later than five Business Days after the General Manager or the Chief Financial Officer of a Borrower or any Parent Company obtains knowledge of the occurrence of any Default or Event of Default, a material default under any other Material Contract of any Borrower or any event, development or occurrence reasonably expected to cause a Material Adverse Change continuing on the date of such statement, a statement of a senior officer of such Borrower or such Parent Company, as the case may be, setting forth details of such Default, Event of Default, other "default" or Material Adverse Change and the action that such Borrower has taken and proposes to take with respect thereto.
- ii) Quarterly Financials. As soon as available and in any event within forty-five (45) days after the end of each of the first three quarters of each Fiscal Year, a consolidated balance sheet of the Salvadoran Loan Parties .

- iii) Annual Financials. As soon as available and in any event within one hundred twenty (120) days after the end of each Fiscal Year, a copy of the annual audit report for such year for the Salvadoran Loan Parties, including a consolidated balance sheet of the Salvadoran Loan Parties as of the end of such Fiscal Year and consolidated statements of income and cash flows of the Salvadoran Loan Parties for such Fiscal Year as of the end of such Fiscal Year accompanied by a report acceptable to the Lenders of an independent public accountants of recognized standing acceptable to the Lenders
- iv) Capital Expenditure Budget. As soon as available and in any event within forty-five (45) days after the end of each fiscal quarter, a copy of the annual capital expenditure budget of the Borrowers as in effect for such Fiscal Year, including a quarterly detailed capital expenditure report comparing actual capital expenditures against amounts budgeted therefore, together with a certificate from the Chief Financial Officer of the Parent Companies certifying the accuracy and completeness of such report.
- v) Litigation. Promptly after the commencement thereof, notice of all actions, suits, investigations, litigation and proceedings before any court or governmental department, commission, board, bureau, agency or instrumentality, domestic or foreign, which could have a Material Adverse Effect or which could have a material adverse effect on the business, condition (financial or otherwise), operations, performance, properties or prospects of either Borrower.
- vi) Material Adverse Effect. Promptly upon the occurrence thereof, notice of (A) a material adverse change in the business, condition (financial or otherwise), operations, performance, properties or prospects of either Borrower or (B) any event that could have a Material Adverse Effect.

3. Financial Covenants

So long as any Term Loan shall remain unpaid and outstanding:

Debt Service Coverage Ratio. The Salvadoran Loan Parties, shall maintain, on a consolidated basis, for each Rolling Period, a Debt Service Coverage Ratio of not less than_____.

Leverage Ratio. The Salvadoran Loan Parties, shall maintain, on a consolidated basis for each Rolling Period, a Leverage Ratio of not more than_____.

Interest Coverage Ratio. The Salvadoran Loan Parties shall maintain, on a consolidated basis, for each Rolling Period, an Interest Coverage Ratio of not less than _____

Dividends, Etc. The Parent Companies shall cause the Loan Parties not to declare or make any dividend payment or other distribution of assets, properties, cash, rights, obligations or securities on account of any shares of any class of capital stock of the Loan Parties, or purchase, redeem or otherwise acquire for value any shares of any class of capital stock of such Loan Parties or any warrants, rights or options to acquire any such shares, now or hereafter outstanding, or return any capital to the stockholders as such (collectively, "Restricted Payments") which would i) otherwise result in the failure of the Borrowers or the Loan Parties to observe any term, covenant or agreement set forth in this Agreement or any Loan Document or ii) cause the aggregate of all such Restricted Payments of the Loan Parties to exceed [fifty percent (50%)] of net income for such previous Fiscal Year.

Capital Expenditures. The Parent Companies shall cause the Loan Parties not to make any Capital Expenditures that would cause the aggregate of all such Capital Expenditures made by the Loan Parties in El Salvador, in any Fiscal Year to exceed \$500,000 (\$500,000) in the aggregate.

EXECUTION OF COLLATERALS

In order for the Lender parties to execute the collaterals agreed upon in the credit agreement (i.e. mortgage on the corporation, pledge over company's shares and intellectual property, etc), we recommend taking into consideration the following "Events of Default":

- a. any Borrower shall fail to pay any principal or interest of any Term Loan or Term Note or any fees established on the Loan Agreement within five calendar days of when the same shall become due and payable or ii) any Borrower shall fail to make any other payment due from it under any Loan Document within five calendar days of when the same becomes due and payable; provided that the Default Interest shall be due and payable by such Borrower for period established; or
- b. any representation or warranty made by any Borrower or the Parent Companies (or any of their officers) in any Loan Document or any certificate or other document delivered in connection with any Loan Documents shall prove to have been incorrect in any material respect when made or confirmed; or
- c. any Loan Party shall fail to perform any other term, covenant or agreement contained in any Loan Document on its part to be performed or observed if such failure shall remain unremedied for thirty (30) days after written notice thereof shall have been given to such Loan Party by any Lender; or
- d. any Borrower shall fail to pay any principal of, premium or interest on or any other amount payable in respect of any Debt that is outstanding in a principal amount in excess of the equivalent of US\$500,000 either individually or in the aggregate (other than any Debt outstanding under the Loan Documents), when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall remain unremedied for a period of fifteen (15) days; or ii) any other event shall occur or condition shall exist under any agreement or instrument relating to any such Debt.
- e. any Borrower shall generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by or against such Borrower seeking to adjudicate it a bankrupt or an insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, trustee, or other similar official for it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it) that is being diligently contested by it in good faith, either such proceeding shall remain undismissed or unstayed for a period of ninety (90) days or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for, it or any substantial part of its property) shall occur; or
- f. one or more judgments or orders for the payment of money aggregating in excess of the equivalent of US\$500,000 shall be rendered against any Borrower and i) such judgment or order shall remain unsatisfied or unstayed after the date such judgment or order was entered for

thirty (30) consecutive days or other arrangements satisfactory to the Required Lenders shall not have been made, ii) an enforcement action shall have been commenced by any creditor upon such judgment or order or (iii) no Contingent Contribution has been made to such Borrower; or

- g. one or more non-monetary judgments or orders shall be rendered against any Borrower or to refrain from taking any action or inaction, either individually or in the aggregate, that could have a Material Adverse Effect, and after the date such judgment(s) or order(s) was entered there shall be any period of forty-five (45) consecutive days during which a stay of enforcement of such judgment or order shall not be in effect; or
- h. any material provision of any Loan Document shall for any reason cease to be valid and binding on or enforceable against any Borrower, or any Borrower shall so state in writing; or
- i. any Collateral Document shall for any reason (except as permitted pursuant to the terms thereof) cease to create a valid and perfected first priority lien on and security interest in any significant portion of the Collateral purported to be covered thereby; or
- j. Either i) any authority asserting or exercising governmental or police powers in El Salvador shall take an action, including a general moratorium, canceling, suspending or deferring the obligation of the Borrowers to pay any amount of principal or interest payable under this Agreement or the Term Notes or preventing or hindering the fulfillment by either Borrower of its obligations under this Agreement or the Term Notes or having any effect on the currency in which a Borrower may pay its obligations under this Agreement or the Term Notes or on the availability of foreign currencies, if applicable, in El Salvador (including any requirement for the approval to exchange foreign currencies) or otherwise or ii) either Borrower shall, voluntarily or involuntarily, participate or take any action to participate in any facility or exercise involving the rescheduling of such Borrower's debts or the restructuring of the currency in which such Borrower may pay its obligations.
- k. any governmental authority having jurisdiction to do so shall revoke any material licenses or permits of either of the Borrowers (or such material licenses or permits shall otherwise expire) or shall revoke any required consent to pledge any of the Collateral, or shall assert in writing that such licenses, permits or consents are no longer binding or in full force and effect; or
- l. any material License shall i) at any time or for any reason be suspended, revoked or terminated prior to its scheduled expiration date or shall otherwise cease to be in full force and effect and not replaced by a substitute acceptable to the Required Lenders within thirty (30) days of such revocation or termination (or such later date as may be mutually agreed by the applicable Borrower and the Lenders provided that such Borrower provides satisfactory evidence that it is diligently conducting negotiations in respect of such substitute contract) or ii) shall be modified, amended or changed in any manner (or shall otherwise have any term, condition, default or breach thereunder waived) that could have a Material Adverse Effect, without the prior written approval of the Lenders; or
- m. there shall occur in the reasonable judgment of the Required Lenders any Material Adverse Change; or
- n. the beneficial ownership of 50% or more of the outstanding Voting Stock of any Loan Party shall be acquired by another Person, then, at any time thereafter during the continuance of any such event, the Administrative Agent i) shall, at the request, or may with the consent, of the Required Lenders, by notice to the Borrowers, declare the obligation of each Lender to make Term Loans to be terminated, whereupon the same shall forthwith terminate, and ii) shall, at the request, or may with the consent, of the Required Lenders, by notice to the Borrowers, declare the Term Notes and all interest thereon and all other amounts payable

under this Agreement to be forthwith due and payable, whereupon the Term Notes, all such interest and all such amounts shall become and be forthwith due and payable, without presentment, demand, protest or further notice of any kind, all of which are hereby expressly waived by the Borrowers; provided, however, that in the event of an actual or deemed entry of an order for relief or similar proceeding under the laws of El Salvador, the Term Notes, all such interest and all such amounts shall automatically become and be due and payable, without presentment, demand, protest or any notice of any kind, all of which are hereby expressly waived by each Borrower.

FORECLOSURE

Whenever any of the Events of Default occur, the Salvadoran law establishes the foreclosure process as a way to enforce payment of the debt. To start the foreclosure process the Lender has to demand the borrower in a commercial court at San Salvador, then the Court formally admits the lawsuit and appoints an “interventor”, this process could take from one month to six months.

Once the interventor is appointed the Court issues an order of attachment on the collaterals mentioned in the lawsuit, this process might take approximately one month, depending upon the Court, after that a Court employee serves notice to Borrowers, who can file their reply.

When the borrowers reply has been admitted, the Court orders a discovery process, during which both parties can present to the Court the evidences that support their actions, after that the Court issues its final judgment.

Under the Salvadoran law, the Court’s final judgment can be appealed twice, the first appeal is filed before a Second Instance Court and a second appeal can be filed at the Supreme Court level. If this Court confirms the final judgment issued by the first instance Court the case is returned to this court in order to begin the enforcement procedure. Please be advice that these appeals can take up to three years in the respective Courts.

To begin the enforcement procedure the fist instance Court appoints accounting experts to conduct a valuation on the collaterals presented, then the Court publishes notice for a public- bid auction and the asset sale takes place on the established date. The buyer of the assets pays the purchase price to the Court and these funds are temporarily transfer to the Ministry of Treasure and once the Court has completed all the administrative paperwork this funds are awarded to the Lender.

Due to the accumulated amount of work in the Commercial Courts the finalization of a foreclose procedure can take approximately 2 years. Please take into account the information prepared in the DOING BUSINESS REPORT of WORLD BANK

ANNEX V: Interview List

Organization	Name	Title
USAID Export Promotion Program (EXPRO)	Phillip Rourk	Program Director
Banco Multisectorial de Inversiones (BMI)	Roger Rafael Alfaro Araujo	Dir. of Investment & Development Banking
BMI	Alfredo Alfaro	Mgr. of Development Banking
USAID-EXPRO	Mario Stanley Caceres	Deputy Director – Training Program
G&S - Garantias & Servicios, SGR, S.A. de C.V.	Victoria Gutierrez de Mejia	General Manager
Inter-American Development Bank (IDB)–Multilateral Investment Fund (MIF)	Guillermo Villacorta	Specialist
IDB – MIF	Carlos Alberto Moreno	Specialist
Rusconi, Valdez, Medina & Associates Central-Law	Luis Medina	Attorney, Partner
SiConsulta S.A.	Claudio de Rosa	Former head of the Nat'l Bankers Association (ABANSA)
Banco Agricola	Ernesto Magana	Manager External Business
Banco Agricola	Lic. Silvia Herrera de Gutierrez	Manager Commercial Banking
FUSADES	Alvaro Guatemala	Executive Director
Chemonics	Anne Bordonaro Spahr	
Chemonics	Michael McNerty	Project Mgr. USAID – Financial Services for SMEs
Chemonics	Alfredo Otero Montero	Finance Specialist
Moran, Mendez & Associates	Luis Alonso Moran	Socio - Accountant
USAID-EXPRO	Federico Aguilar	Deputy Director - Competitiveness
Local Businesses:		
Golden Homes		
Healthco Products		
Olga Gourmet/Cocina Maya		
Basic Glasses/Bello Hogar		
DM Supplies		
Pahnas		
Solumed		