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ARIES

Assistance to
Resource Institutions
for Enterprise Support

Evaluation of the
Small Business Development Project
Honduras

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Submitted to:

USAID/Honduras

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*The views and interpretations in this publication are those
of the author(s) and should not be attributed to the U.S.
Agency for International Development.*

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ARIES

Assistance to Resource Institutions for Enterprise Support

The ARIES project is designed to strengthen the capabilities of support organizations in developing countries to implement small-scale and micro-enterprise development programs. ARIES builds on the work of the Agency for International Development's former Program for Investment in the Small Capital Enterprise Sector (PISCES) and Small Business Capacity Development projects. It works with intermediary support organizations that provide services to small and micro-businesses and industries, such as private voluntary organizations (PVOs), banks, chambers of commerce, management training centers, business people's organizations, and other developing country government and non-governmental organizations (NGOs).

The contract for this five-year project has been awarded to Robert R. Nathan Associates, Inc. (RRNA) with subcontractors Harvard Institute for International Development (HIID), Control Data Corporation (CDC) and Appropriate Technology International (ATI).

ARIES is core funded by the Bureau for Science and Technology's Office of Rural and Institutional Development (S&T/RD) and the Bureau for Food for Peace and Voluntary Assistance's Office of Private and Voluntary Cooperation (FVA/PVC). Mission funded technical assistance represents \$3.8 million, or almost three-fifths of the five-year budget of \$6.8 million.

The ARIES project has three major components -- research, training, and technical assistance -- designed to cross-fertilize each other. The applied research component focuses on economic, social, and organizational issues surrounding intermediary support organizations to inform AID missions and host country actions in this subsector. The training component includes design, testing, conduct and follow-up of training programs in such areas as finance, management and evaluation for PVO and NGO personnel. The technical assistance component provides short-term technical assistance to AID missions and intermediary organizations to assist small and micro-enterprise development.

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LIST OF ACRONYMS

AITEC	Accion Internacional Tecnica
ANDI	Asociacion Nacional de Industriales/National Association of Industrialists
ANMPI	Asociacion Nacional de Mediana y Pequena Industria/ National Association of Medium and Small Industries
ARIES	Assistance to Resource Institutions in Enterprise Support
BANADESA	Honduran Development Bank
BANHCASA	Banco Capitalizador Hondureno Sociedad Anonima
BAS	Business Assistance System
CBI	Caribbean Basin Initiative
CDSS	Country Development Strategy Statement
FEHCIL	Honduran Federation of Industrial Cooperatives
FEHCOVIL	Honduran Federation of Housing Cooperatives
FIA	Financiera Industrial y Agropecuaria
FIDE	Foundation for Export Research and Development
FONDEI	Central Bank's Industrial Development Fund
FOPRIDEH	Federacion de Organizaciones Privadas de Desarrollo de Honduras
FUNADEH	Honduran National Development Foundation

INCAE Central American Institute of Business
Administration

INFOP National Institute for Professional Training

PADF Pan-American Development Foundation

PVO Private Voluntary Organization

PYME Pequeña y Mediana Empresa/Small and Medium
Enterprise Program

RRNA Robert R. Nathan Associates, Inc.

SBD Small Business Development Project

SME Small- and Medium-Scale Enterprise

WID Women in Development

EXECUTIVE SUMMARY

Introduction

USAID/Honduras provides support to the Small Business Development (SBD) Project, which is implemented by two Honduran private organizations -- the Financiera Industrial y Agropecuario (FIA) and the National Association of Industrialists (ANDI). This report evaluates these two organizations.

Chapter I outlines the context in which the SBD Project operates and provides a project description. Chapter II evaluates the SBD Project, presenting the team's major findings on project design, implementation, and impact. The final chapter presents conclusions and recommendations.

Project Background

The Small Business Development Project (SBD) (No. 522-0205) was designed by USAID/Honduras to expand financial and technical assistance to a segment of the private sector that had no access to the banking system. The project seeks to develop a source of technical and financial assistance for Honduras' small- and medium-scale enterprises, thereby increasing production and employment in these businesses. To ensure this purpose, the project anticipated establishing a well-managed, development-oriented business finance company,

Financiera Industrial y Agropecuario (FIA) and a complementary business assistance system (BAS).

The goals of the project over an eight-year period are:

- . To create approximately 2,000 jobs
- . To generate US\$25 million in value added to production

Employment and production goals are to be achieved by providing 170 loans to small- and medium-size enterprises (SMEs) and technical assistance to 525 enterprises.

The project agreement was signed in June 1984 and is currently expected to end on May 31, 1987. Total project resources over the three-year period were estimated at US\$8.2 million. This included a US\$600,000 AID grant, \$4.4 million equivalent in local currency through Government of Honduras (GOH) counterpart funding, \$2 million in loans, \$500,000 in capital from five private banks, and US\$700,000 interest income on loans. Financial support for the technical assistance component was to be generated by a 10.25 percent interest spread on the total interest charged FIA (11 percent) by the GOH.

Project Description

FIA, a private, development-oriented, financial institution is owned by five commercial banks that also serve on its Board of Directors. In March 1985, almost a full year after the start of the project, FIA opened its doors to the public. Since that time, FIA has provided non-bank commercial sources of credit to 35 SMEs.

ANDI, the coordinator of the BAS, was to provide technical assistance to management assistance organizations specializing in SME support; assist SME clients in developing loan applications to be financed subsequently by FIA; and provide courses and arrange for direct technical assistance for both FIA clients and other SMEs. A PADF technical advisor was contracted to assist ANDI in developing the program. ANDI initiated program efforts in June 1985 by establishing the Pequena y Mediana Empresa (PYME) program. While the PYME program has funded grants to management assistance organizations and arranges training courses to address SMEs' needs, the technical assistance component for FIA clients did not develop as expected. Only 15 FIA clients were provided technical assistance financed by the PYME program. To date, four SME clients have been generated for FIA.

A review of the SBD project in March 1985 identified several bottlenecks in project design and implementation. As a result, USAID/H held discussions with ANDI and FIA, negotiated and signed the first tri-partite agreement in September 1985, and formed a project coordinating committee. A technical assistance unit was initiated within FIA, and a loan loss reserve fund was established with the interest earned on GOH counterpart funds deposited in the FIA owner banks. The interest differential between the current Central Bank/FONDEI discount rate of 9 percent, minus the 0.75 percent FONDEI fee, or 8.25 percent, is channeled to ANDI to support the PYME program.

Evaluation Purpose

This evaluation, conducted during November 1986, 2½ years into the three-year project, is the first formal evaluation of

the SBD project. A formal review of the project was carried out in March 1985, and internal memoranda and status reports have documented progress and changes in program operations. This evaluation seeks to:

- . Provide USAID/H with an objective analysis of the role and performance of FIA and ANDI and their impact on project success
- . Assist the Mission in deciding whether to extend the SBD project, and on planning new activities

Project Accomplishments

From mid-1985 to November 1985, the SBD project has accomplished the following:

- . FIA has extended credit to 35 SMEs with a total portfolio of L.3.5 million (US\$1.75 million equivalent).
- . Fifty percent of FIA clients are small enterprises and 50 percent are medium-sized enterprises.
- . Forty percent of FIA loans supported the establishment of new enterprises.
- . Sixty percent of approved loans were for working capital, the most difficult category of credit to obtain from commercial lenders.
- . Forty-eight percent of the loans were for amounts under L.100,000 and 29 percent for amounts over L.200,000.
- . The PYME program has approved 20 small business development grants with 13 management assistance organizations.
- . FIDE and private firms provided technical assistance to 15 FIA clients. This was financed under the PYME program.

- . PYME has generated four clients for FIA credit and three clients for other outside sources of credit.
- . Fifty-one courses benefitting 1,085 participants were sponsored by the PYME program. The majority of the courses have been provided by INFOP and the management assistance organizations that received grant financing.
- . Training has been delivered to 199 SMEs through INFOP and to 772 SME owners and employees through projects financed by PYME.

Project Impact

Both FIA and PYME have been operating for less than two years. However, there are early indications that both organizations are positively affecting employment generation, income generation, and the strengthening of small and medium enterprises. Through ANDI, the project can also improve the institutional and financial leverage of the small business sector as a whole.

Credit and technical assistance have strengthened the FIA-financed firms. Many of these firms have improved their financial position and profitability. Technical assistance and credit through both PYME and FIA programs have also enabled several firms to expand employment opportunities for previously unemployed and unskilled workers, including women heads of households.

Specific effects attributable to the SBD project include the following:

- . Employment gains projected by FIA for the ten enterprises studied amounted to 140 new jobs.

- . The cost per job generated is L.10,202 or US\$5,101.
- . Value-added projections of FIA-supported firms during the first year of operation amount to L.2.1 million for the ten FIA clients studied, and L.5 million for the overall portfolio of 35 clients.
- . FIA-financed companies appear to be financially viable. Seven out of the ten FIA-financed companies studied are able to cover their short-term liabilities with liquid assets, but only three stand out with comfortable margins above the industry average of 2.5. These same seven firms have good to excellent profit margins. The asset base of the enterprises has also changed as a result of credit; fixed assets increased by 16 percent.
- . Preliminary calculations indicate that most of the ten enterprises studied should experience positive rates of economic return. Financial returns are high and secondary economic and social impacts are positive. This is due to the facts that nearly 60 percent of the work force in these firms was previously unemployed, almost 70 percent of the raw materials are local inputs, and nearly 100 percent of the production output is derived from, or sold to, local markets. These purchases (backward linkages) and sales (forward linkages) are considered benefits to the local economy to the extent that goods and services are produced within the country and are new production rather than sales diverted from other customers.
- . Although there are some problems with the validity and consistency of data, PYME program reports indicate that 891 jobs have been generated through program grant funding and technical assistance. The majority of these appear to be jobs maintained as a result of program funding. However, there are several instances where jobs have been created for previously unskilled and unemployed people as a result of providing technical assistance.

The FIA/PYME Relationship

Technical assistance for FIA clients has been only marginally successful. The PYME program is working with a number of NGOs to improve their ability to deliver services to SMEs. The orientation of the PYME program work has been heavily weighted in favor of the needs of micro and small enterprises, too small to fit FIA's small to medium-size business clientele. With FIA's own technical assistance department, there is little reason to expect a continuation of a direct relationship between FIA and PYME. FIA can independently contract technical services, such as feasibility studies, which are best provided outside of FIA, as PYME has done in the past.

There is no need for an intermediary organization such as PYME to become involved in the operation. In the past, this functional relationship between PYME and FIA led to an additional bureaucratic layering and an unnecessarily burdensome coordination and management task for both organizations. FIA is in a better position to evaluate the services of its own staff and/or independent contractors and hold them accountable for services rendered.

Client Coverage

FIA clients tend to be medium-size and larger small-size enterprises, while the clients of the organizations supported by the PYME program tend to be small-size and micro enterprises. Although both FIA and PYME reach the target population in the SME sector, their clients fall on opposite ends of the spectrum.

The technical assistance and credit needs of women entrepreneurs were not taken into account during the SBD project design phase. Many design components, such as the priority given to medium-size enterprises, and choice of management assistance organizations, inhibited women's participation in the project. During the project implementation phase, development occurred which enhanced the SBD project's ability to reach women, such as PYME's support of organizations that benefit women entrepreneurs. While it is unlikely that FIA will benefit many women entrepreneurs directly as borrowers, FIA is enabling larger firms to generate more employment for the female labor force. The PYME program is already providing access to credit and technical assistance for women entrepreneurs, and as it expands into the rural industrial sector, it is likely to do more in that area.

FIA

FIA is a sound financial institution which has operated in a financially responsible and conservative manner. It has performed well considering the complexity of its goals, the difficulty of the local economic climate, and some inappropriate financial and decision-making structures.

Management

FIA management is sound. After working out important project design and start-up problems, FIA is operating efficiently with a reasonably healthy, albeit limited, portfolio. Turn-around time for decisions has become excessive and has discouraged potential clients.

Coverage

FIA needs to expand its portfolio and coverage of small industry, especially outside Tegucigalpa and San Pedro Sula. For example, FIA supports only one production cooperative and needs to be apprised of the economic and financial viability of the numerous rural cooperatives. FIA support in this area is weak.

Interest Rate

FIA's interest rate policy is impeding its lending to SMEs. The cost of borrowing from FIA is above commercial interest rates. The original feasibility study for FIA did not provide information on the supply of money for SMEs or the demand for financing, especially its elasticity vis-a-vis the interest rate. As is indicated elsewhere, FIA rates are now high enough that potential borrowers are not coming forward. Since informal rates are much higher, there may be a higher risk group of borrowers who would accept these loans, but FIA is not prepared to deal with them. This is a function of the limited group to which FIA is willing to lend. However, FIA's accomplishments in extending credit downward to a group slightly below that normally served by the commercial banks is not to be gainsaid.

Arrearage

Arrearage on interest payments and capital, while of concern to FIA, is considered acceptable by Honduran standards. Increasing arrearage is indicative more of FIA's lax policy on loan recuperation than the financial viability of the firms studied.

Administration

FIA has not developed an operational policy for writing off bad debt. FIA clients do not prepare consistent or standard financial statements for loan applications.

The PYME Program

The PYME program has enabled several organizations to assist SMEs in beginning new services and improving existing ones. While perhaps originally not the best choice to undertake the coordination of the BAS, ANDI has shown a lot of progress and goodwill toward the small business sector at both the program and institutional level. Administrative and programmatic systems that are crucial to the development of the program are in place and operational. Areas that will need continued outside support are management and coordination within the NGO community. Short-term technical assistance consultancies are appropriate to fill these needs.

Project Management

Project management is the major bottleneck to further program progress and new organizational initiatives. Staff at the officer level seem competent and well-informed.

PADF Technical Assistance

The PADF Advisor has contributed to the development of the ANDI/PYME program and support systems.

Grants Program

PYME has a consistently good reputation as an efficient and credible funder of management assistance organizations'

projects that benefit the small business sector. PYME has been selective in providing financing in a disinterested manner to a number of organizations that have good reputations working with diverse SME client groups.

Training Program

The most effective training and follow-up to SMEs can be provided by the PVO management assistance organizations. PVOs know the educational level of their clients, have mechanisms in place to assess clients' needs, and, through extension agents, can ensure a higher quality of follow-up. While INFOP courses have been reviewed as beneficial by a number of organizations generally, INFOP methodology and course content have been criticized as inappropriate and designed without a clear audience in mind.

Technical Assistance

Outside of FIA, PYME can be useful in its role as an indirect provider of technical assistance to small independent firms and cooperatives that are in a position to receive credit from commercial or government banks and lending agencies. This, however, is best coordinated through joint efforts with those organizations that have clients who may be ready to take advantage of commercial lending operations.

Institutional Development

ANDI can provide political and economic leverage to SMEs, and there are indications that it has already begun to do this. Because of experience gained in implementing the

project, ANDI is probably the best organization to continue supporting the PYME program.

Association Development

There appears to be a great deal of untapped potential in big business/small business joint ventures and support networks. ANDI is probably the best organization to carry out this type of activity.

USAID Policy

Given the importance of monetary, fiscal, and export regime policy reform, USAID/H's development policy stresses exports. However, the Mission's initiative in undertaking an innovative small and micro enterprise development project reflects its commitment to the development of the domestic economy as part of its integrated approach to development.

Though circumstances vary from country to country, SMEs' greatest potential market lies at home. In Honduras, 89 percent of small enterprises produce primarily for direct retail customers (Liedholm & Mead, 1986). These customers have, in most countries, a much higher income elasticity for the goods of small rather than large-scale industry.

USAID/H Project Support

During the project implementation phase, USAID/H support has been effective and appropriate.

Lessons Learned

To implement a novel, complex, and sophisticated project design in a relatively short period of time requires implementing organizations with established development programs and strong management track records. Both SBD project-implementing organizations were developing their credentials as institutions while attempting to implement a most difficult and innovative project. This led to considerable delays in project start-up.

Implementing organizations need to be involved in the design of the project they are subsequently to develop and implement. When two or more organizations take on joint responsibility for a project, roles and responsibilities need to be jointly discussed, defined, and agreed to in a formal way. To the extent this may not be done, some delays were to be expected.

High collateral requirements and lack of term credit are not the only barriers to institutional commercial credit access for SMEs. High interest rates appear to make them unattractive to borrowers in institutions like FIA.

When the spread between the cost of money and the interest rate charged to borrowers is sufficient for the lending institution to recover costs, technical assistance to credit clients can best be provided or arranged by the financial institution. Post-loan management and financial technical assistance needs are generally first detected by the financial institution, due primarily to the institution's profit motive and monitoring of loan recuperation.

Currently, few management assistance organizations' clients are able or willing to graduate through a credit system and qualify for commercial credit.

Conclusion

The emergence of two independent entities, with two distinct client populations, calls into question the rationale for continuing to support the SBD project as currently implemented. In a forced marriage of interests between two institutions, each serving different client populations, neither one will serve the originally targeted client population with the full complement of financial and technical services, as intended in the project design. The two institutions need not be programatically and financially tied to continue their support to micro-, small-, and medium-size enterprises.

The dual objective of FIA -- to work toward economic development and to make a profit in support of medium and small industry -- is a complex assignment. The objective of the PYME program -- to improve the quality and coverage of management assistance organizations' services in support of the SME sector -- is an equally complex and lengthy proposition. By devoting resources to improving the service delivery capability of each institution and area of activity, ANDI/PYME and FIA can build on their strengths in providing assistance to the small business sector as a whole.

Recommendations

Recommendations for USAID

1. Extend both components of the SBD project, but with certain modifications in design based on

the difference between those FIA activities that can become financially self-sustaining operations and the PYME program activities that are developmental in nature and should be financed from development assistance funds.

2. Continue to support FIA with counterpart funds, at inter-bank, real costs of money, consistent with AID policy of non-price rationing.
3. Continue to support the ANDI/PYME program with GOH counterpart funds in the form of development assistance grants.
4. Support the movement of FIA away from relying on ANDI/PYME-financed technical assistance.
5. Assist FIA in the development of its own technical assistance unit.
6. Make the separation of ANDI and FIA complete by removing the financing of ANDI via the FIA interest rate differential and channeling that differential back to FIA to be used in the following ways:
 - . To cover costs of FIA's technical assistance unit
 - . To cover the costs of FIA's hiring outside technical assistance for project analysis and technical support
 - . To reduce the final cost of money to FIA clients
 - . To investigate the feasibility of opening a window dedicated to small business and micro production enterprises
7. Use USAID's influence as a major donor in Honduras to rally both public and private sector support behind FIA, ANDI, and the overall SBD project.
8. Relinquish USAID's direct administrative and managerial role in the SBD project in favor of a Board of Directors role to provide more support on the broader issues of program

direction, management, and making linkages within the sector.

9. Pursue a balanced economic development approach in its support of private enterprise. Encourage the development of local economically and financially sound private enterprises that operate in the domestic free market, as well as export industries. These enterprises generate employment and provide for a greater measure of economic and social stability.

Recommendations for FIA

1. Undertake a definitive market analysis to determine the market segment and appropriate niche for FIA in support of SMEs.
2. Develop joint projects with FIDE.
3. Develop the originally planned co-financing with FIA shareholder banks.
4. Examine the timing and appropriate form for widening the ownership of FIA.
5. Change interest rates to reflect FIA's cost of money and on-lend at competitive rates.
6. Vest final authority for approval of loans of L.100,000 or less in FIA management.
7. Develop loan performance (recovery) incentives and disincentives to decrease current loan arrearage rates.
8. Develop regular weekly reporting of necessary loan performance data.
9. Establish an operational policy and procedures for writing off bad debt.
10. Standardize financial statement requirements for all current and future FIA clients to provide appropriate data for accurate financial internal rate-of-return analyses.

11. Add data on employment, material purchase, and sales to the current client data bank to complete the necessary information required for economic rate-of-return analyses.

Recommendations for PYME

1. Institute a slow and stable growth policy, restricting activities to current program strengths, building on these strengths, developing program priorities that fall exclusively within the program mandate, and trimming the program to a size manageable by PYME program staff.
2. Diversify funding sources at a rate that does not jeopardize the effectiveness of the program.
3. Learn about and visit other organizations where large and small businesses have developed support networks. One program is MIMEXA in Monterrey, Mexico that was developed with the support of Accion/AITEC. Other organizational resources of value are the Partners of the Americas, and the International Executive Service Corps. PADF should also have a wealth of experience in this area.
4. Initiate program manager recruitment efforts. The "self-audit" carried out by PYME in September 1986 identified the managerial and personal skills that are required of this important position.
5. Refine job descriptions to reflect the team work approach currently used by PYME. Project Officers with complementary technical skills acting as a multidisciplinary team seem to support the direction of the program better.
6. Expand and update staff knowledge of development issues and concerns within the sector, specifically, seminars on women in development and seminars covering the issues of technical assistance, training, and credit programs directed to the small business sector.

7. Program short-term technical assistance consultancies, perhaps through PADF, local agencies, or other international agencies that have a base in Honduras and offer short-term management assistance.
8. Re-examine the need for long-term technical assistance as the program develops and specific needs are identified.
9. Analyze what discrete projects the PADF Advisor can undertake and the time required to complete them. Some suggestions are made in the body of this report.
10. Develop mechanisms, along lines similar to the ANMPI project, to generate clients for FIA. To avoid duplicating the problems and low success rates of the ANMPI project, before project initiation it will be important for PYME to: (1) work closely with the management assistance organizations and the lending institutions that have expressed an interest in this kind of support; (2) determine the number of firms able and willing to apply for such credit, and the rates and terms they can afford; and (3) identify individual sources of credit, as well as the specific procedures and documentation required by each source.
11. Encourage technical assistance from one or more management assistance organizations with successful programs to those organizations that are initiating or having problems with similar programs. This type of collaboration can be developed through a number of mechanisms available to PYME, including: (1) surveying the need among management assistance organizations for this type of support; (2) updating information on existing PVO programs that includes an analysis (not merely a description) of services available and under what terms and conditions; and (3) financing small workshops with PVO staffs as instructor/participants, not only to exchange information and identify problems, but to plan joint efforts and programs, perhaps with subsequent PYME financial assistance.

12. Focus the scheduled evaluation of the INFOP courses on the importance of the PYME/INFOP agreement to support the small business sector. Analyze whether the benefits provided by the INFOP courses are worth the time PYME devotes to this activity. The evaluation should pay particular attention to: (1) whether the organizations that appear to value INFOP courses can access INFOP directly; (2) whether PYME can use its grants program to provide training funds to management assistance organizations that are then able to select their own instructors; and (3) how the scholarships (planned for the future) will complement or duplicate these efforts.
13. Encourage a more active role on the part of NGOs in client and staff development needs assessment, course design, and implementation.
14. Emphasize joint efforts by NGOs in initiating client and staff development programs. Specifically, PYME should explore the potential benefits of: (1) encouraging an organization to design a course specifically for its own clientele that will later be appropriate for others; (2) providing funds for outside resources, if necessary, as in the case of the FEHCIL marketing course; and (3) financing one or more organizations that have successfully designed and implemented their own courses (for clients or staff) to share these resources with other organizations, perhaps giving the courses themselves.

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CHAPTER I. PROJECT BACKGROUND

Socioeconomic Context

According to the Central Bank, the Honduran economy recovered from the oil shocks of 1974-75 to register significant gains in real GNP growth in 1978 and 1979 (7.4 and 6.8 percent, respectively). At that point, the economy turned downwards. Real GNP growth was negative in 1982 and 1983, and never exceeded population growth during the entire 1980-84 period. This signifies a yearly decline in real GNP per capita (John T. Vanderveen, 1985).

In 1983, the population in Honduras was 4.1 million, with an annual growth rate estimated at 3.4 percent and very low per capita income. Rural Honduras is extremely poor; 60 percent of the families earn annual incomes below US\$250 (or less than \$50 per person) (USAID/H FY 1988 Action Plan for Honduras, May 1986).

Open unemployment in Honduras is estimated at 25 percent by the World Bank (World Bank, 1986) and over 40 percent by the Central Bank. USAID/H estimates unemployment at 15-20 percent (interview with USAID economist). Honduras development prospects are highly uncertain as a result of:

- . Monetary, fiscal, and trade policy disorders
- . Tense regional political situation
- . Growing dependence on external aid flows
- . High dependency on limited export crops (bananas, coffee, sugar)

The major donors in Honduras have concluded that (1) the overriding macroeconomic policy question is how to accelerate growth and employment creation on the magnitude required by the country's demographic structure, and (2) a reconstruction of the economy could only be achieved through faster economic growth and by switching to more labor-intensive production methods.

The small business sector is considered extremely important in achieving balanced economic growth and employment. Small-scale enterprises are the most important subsector of the Honduras manufacturing sector; an estimated 37,000 firms employ fewer than five persons (World Bank, 1986).

Project Description

The Small Business Development Project (SBD) (No. 522-0205) was designed by USAID/H to expand financial and technical assistance to a segment of the private sector that had no access to the banking system. The project seeks to develop a source of technical and financial assistance for Honduras' small- and medium-scale enterprises, thereby increasing production and employment in these businesses. At the outset, the project anticipated establishing a well-managed, development-oriented business finance company, Financiera Industrial y

Agropecuario (FIA) and a complementary business assistance system (BAS).

The goals of the project over an eight-year period were:

- . To create approximately 2,000 jobs
- . To generate US\$25 million in value added to production

These goals are to be achieved by providing 170 loans to small- and medium-scale enterprises (SMEs) and technical assistance to 525 enterprises. The project agreement was signed in June 1984 and is currently expected to end on May 31, 1987.

The project supported two organizations -- FIA and PYME -- which were intended to be complementary.

FIA

Chartered as a commercial corporation, FIA is a private, development-oriented, financial institution that is a non-bank commercial source of credit. FIA's intended credit niche falls between the market currently attended to by (1) banks which provide one-year term loans and rely on high collateral and guarantee requirements; (2) the numerous small, non-bank financial institutions which are often unreliable as sources for credit; and (3) the moneylenders who provide limited high cost, short-term credit. FIA's goal is to augment the production and employment levels of economically and financially sound SMEs that have difficulty securing commercial bank credit.

FIA is owned by five commercial banks which also serve on its Board of Directors. Each bank originally contributed L.200,000 in share stocks. For the first 18 months of operation, FIA was managed by three professional staff members -- a General Manager, a Loan Officer, and an Operations Officer. FIA management primarily reviews loan applications, assists entrepreneurs with business and financial planning, works closely with the ANDI/PYME coordinated Business Assistance System, and make recommendations on loans for subsequent Board approval.

The BAS: The ANDI/PYME Program

The Business Assistance System (BAS) was designed to support management assistance organizations with expertise in providing technical assistance to small enterprises. BAS' main objective is to assist these organizations to increase the quality and scope of their services. The organizations were expected gradually to form a network through which small entrepreneurs could receive assistance from a number of easily accessible organizations. The system would enable the small entrepreneur to approach the management assistance organizations either directly or through referrals from FIA or ANDI.

In addition to assisting the client in developing loan applications, to be subsequently financed by FIA, the BAS was to provide courses and arrange for direct technical assistance to small businesses. Through the BAS, management assistance organizations and private technical management consultants were to provide follow-up and technical assistance to entrepreneurs who had already obtained FIA financing. Thus the system was designed to generate clients for FIA and provide technical assistance to FIA clients.

The project design incorporated a closed system approach with a continuous flow of services and assistance among the PYME program, the management assistance organizations qualified by PYME as service providers, FIA, and the small business client. Gradually new organizations were to be qualified by PYME as appropriate service providers and incorporated into the system.

The BAS Coordinator

As the BAS Coordinator, ANDI was charged with the following responsibilities: to assess the management, information, and technical assistance needs of small and medium enterprises; to finance the assistance activities of the management assistance organizations it qualifies as services providers; to evaluate management assistance organizations' effectiveness and increase resources for the most effective ones; to qualify new organizations to participate in the system; to train their personnel; to ensure coordination among all service providers; and to provide linkages to FIA and external sources of assistance (SBD Project Paper).

The PYME program is managed by four professional staff members: the Program Manager, a Training Officer (position currently vacant), a Monitoring and Evaluation Officer, and an Accountant. The PYME Committee, composed of five members of ANDI and one outside member, is the decision-making body for the PYME program. Outside technical assistance is provided by a Pan-American Development Foundation (PADF) Advisor who is assigned full-time to ANDI for a two-year period.

PYME Programs

PYME currently operates four programs: (1) the Business Assistance Services program provides grants to management assistance organizations that have developed projects to benefit the small business sector; (2) the training and technical assistance program arranges and provides courses and technical assistance to management assistance organization staff members and SMEs; (3) an inter-institutional information network publishes newsletters and holds seminars; and (4) a monitoring and evaluation program designed to monitor and evaluate PYME-funded projects and, on a national level, assess and evaluate SME support services.

Technical Assistance

Technical assistance financed by the PYME program has been delivered to (1) FIA clients at FIA's request, and (2) ANMPI through a grant to generate clients for FIA.

SBD Project Accomplishments

From mid-1985 to November 1985, the SBD project has accomplished the following:

- . FIA has extended credit to 35 SMEs with a total portfolio of L.3.5 million (US\$1.75 million equivalent).
- . Fifty percent of FIA clients are small enterprises and 50 percent are medium-sized enterprises.
- . Forty percent of FIA loans supported the establishment of new enterprises.
- . Sixty percent of approved loans were for working capital.

- . Forty-eight percent of the loans were for amounts under L.100,000 and 29 percent for amounts over L.200,000.
- . Employment gains projected by FIA for the 10 enterprises studied in depth amounted to 140 new jobs.
- . The cost per job generated is L.10,202 or US\$5,101.
- . Value-added projections of FIA-supported firms during the first year of operation amounts to L2.1 million for the ten FIA clients studied, and L5 million for the overall portfolio of 35 clients.

The PYME program has:

- . Approved 20 small business development grants with 13 management assistance organizations.
- . Financed technical assistance provided by FIDE and private firms to 15 FIA clients.
- . Generated four clients for FIA credit and three clients for other outside sources of credit.
- . Arranged for or financed 51 courses benefitting 1,085 participants. The majority of the courses have been provided by INFOP and the management assistance organizations receiving grant financing.
- . Although there are some problems with the validity and consistency of data, PYME program reports indicate that 891 jobs have been generated through program grant funding and technical assistance.
- . Training has been delivered to 199 SMEs through INFOP and 772 SME owners and employees through projects financed by PYME.

Modifications in Project Design

In 1984, the three-year project design called for resources to finance the Small Business Development Project (SBD) in the following manner:

- . \$600,000 USAID/H grant funds
 - . L.8.0 million in a GOH counterpart loan to FIA
 - . L.800,000 GOH counterpart grant to ANDI to support the BAS
- Subtotal -- \$5.0 million equivalent

FIA's contribution by its five stockholder banks was to be:

- . L.1.0 million paid-in capital stock in FIA
 - . L.4.0 million in co-financing among given member banks
- Subtotal -- \$2.5 million equivalent

ANDI's financial support for its technical assistance coordination role was to be generated by a 10.25 percent interest spread on the total interest charged FIA (11.0 percent) by the GOH. This interest income was estimated to be L.1.4 million over three years.

Subtotal -- \$0.7 million equivalent

Total sources of funds -- \$8.2 million equivalent

The original design included project costs of US\$600,000 for dollar-related costs including foreign assistance advisors

to FIA and ANDI. A loan portfolio over the three-year project was planned for just over US\$6.0 million equivalent, with the BAS utilizing US\$1.1 million.

In March 1985, USAID/H hired an outside consultant to conduct a review of the SBD Project. This review identified several project design problems and bottlenecks to project implementation. As a result of the review recommendations, USAID/H took the following actions: high-level discussions were held involving USAID/H, ANDI, and FIA; the first tripartite agreement was negotiated and signed in September 1985; and an SBD Project coordinating committee was formed. These actions contributed directly to project implementation by securing, for the first time, a mutual understanding of the role each party was to play.

Another positive USAID contribution to project implementation was the decision by Private Sector Office management to hire a Project Manager who had extensive experience in the commercial banking sector in Honduras. The Project Manager's knowledge of key actors and concerns in the banking industry, coupled with the development experience of Private Sector Office key staff members, has improved communications between USAID/H and the implementing agencies.

Further discussions among USAID/H, the Central Bank/FONDEI administering the counterpart funds to FIA, and FIA management and its Board members, resulted in important modifications to the project design during the first year and a half.

FIA management proposed that the remaining GOH counterpart funds of approximately L.4.5 million be deposited equally

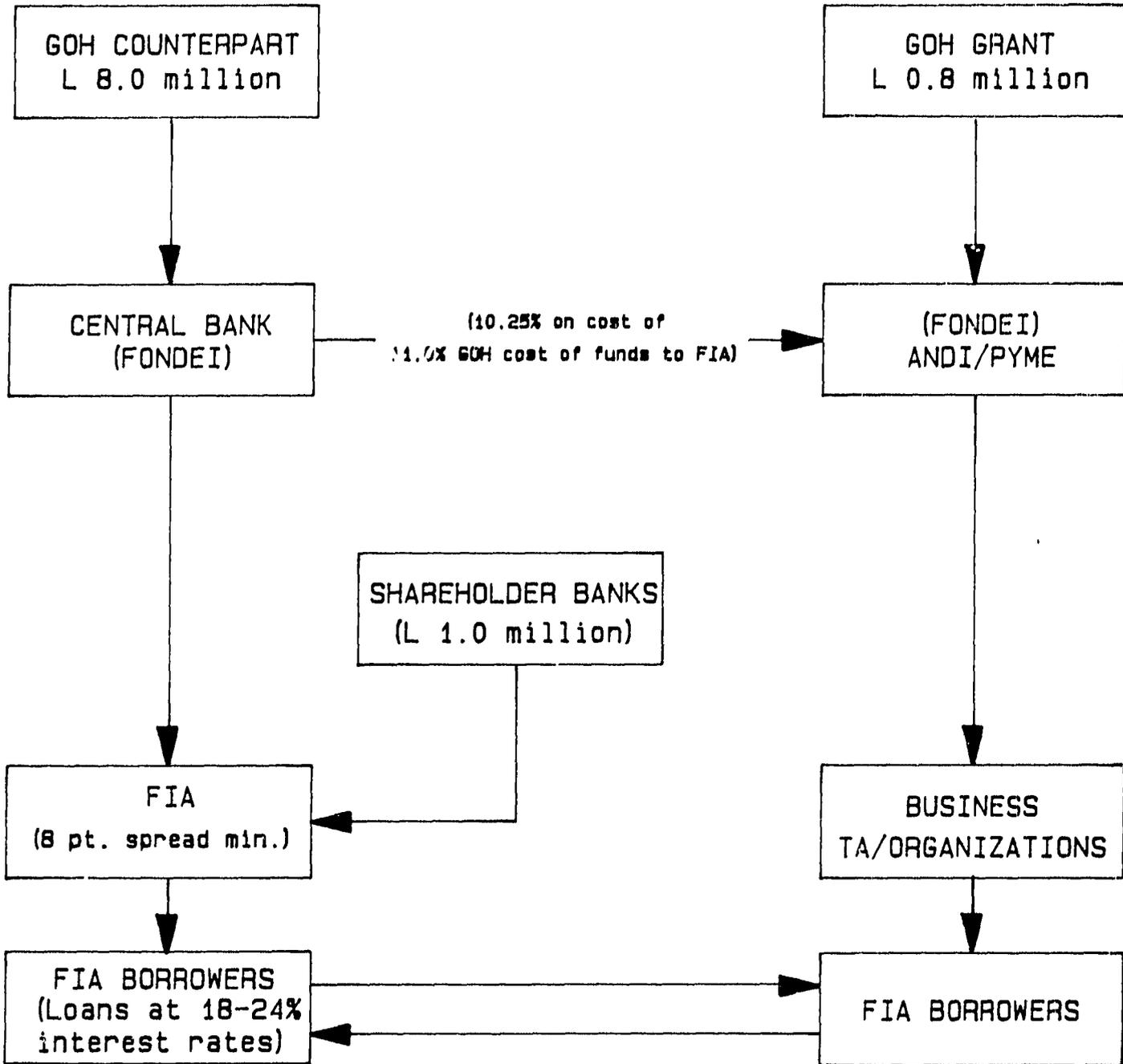
among the five member banks of FIA, rather than remain in the Central Bank (FONDEI) until drawn down. These unused loan funds generate 9 percent interest. From March 1985 to August 1986, these interest earnings were channeled to ANDI to support the PYME program. Later, the SBD participants decided to channel the earnings on these funds to FIA. This enabled FIA to start up its own technical assistance unit and to develop an appropriate loan loss reserve fund. FIA has hired a second loan officer and has shifted the senior loan officer to head up the new technical assistance unit.

A decision by the Central Bank to lower the discount rate to 9 percent decreased the cost of money for FIA. After FONDEI's 0.75 percent fee, the remaining 8.25 percent cost to FIA for the on-lending funds is channeled to ANDI/BAS to continue coordination and funding of technical assistance entities and agencies providing support to micro, small, and medium enterprises. FIA can now charge 17 percent interest to their clients.

To complete the important changes made on project financing, ANDI was granted an additional L.800,000 of ESF funds for PYME program support (see Diagram 1).

Diagram 1.

Original Project Design--1984



CHAPTER II. MAJOR FINDINGS

Project Design

Strengths of Project Design

While complicated, the design of the SBD Project is unique for a number of reasons. First, the FIA component of the project was originally designed with private sector collaboration. Banks and large private sector entrepreneurs joined together to address development issues confronting small- and medium-scale enterprises (SMEs). Their awareness of SME needs was heightened; monetary and human resource support was committed to the project.

Second, the project design relied on the private banking sector's ownership of FIA. Ownership required capital contributions and the assumption of risk. Although all of the start-up capital and GOH counterpart funds are AID capital flows to the project, the only FIA shareholders, the banks, have invested L.1.0 million into the venture. FIA is borrowing the loan funds through the Central Bank's Industrial Development Fund (FONDEI) on a 20-year term at the highest Central Bank discount rate for loans made by commercial banks. Until recently, FIA paid an 11 percent rate. This rate was considered the best proxy for the real cost of additional funds for lending purposes to the banking sector. This policy

supported USAID's goal of establishing FIA as a private sector finance company operating at real cost levels.

Third, the project design included a plan for financial sustainability for the technical assistance arm of the project. After FONDEI deducted a 0.75 percent fee, the remaining 10.25 percent was to be channeled to ANDI to support the BAS component. To date, the PYME program has provided timely funding of consultancies and non-government organizations for their support of pre-loan project analysis and technical assistance to a limited number of FIA clients.

Fourth, in order to prevent a conflict of interest, the project design indicated that an organization without its own operational program should be designated as the BAS System Coordinator. The National Association of Industrialists (ANDI), a powerful association of large industries in Honduras, provided a logical institutional link to coordinate technical assistance for new and expanding SMEs.

Fifth, through FIA, the project design anticipated the provision of investment and working capital loans to SMEs in the industrial and service sectors that had no access to the commercial banks. Loans were to be provided at terms and with payment plans that were thought to be more suitable for SME projects. The interest rate was to reflect the high risk nature of the loans. The interest rate established by USAID/H for FIA clients was to be no less than 8 percent above the Central Bank discount rate on FIA's loan. The minimum final interest rate to target beneficiaries is 19 percent.

Assumptions of Project Design

At least six crucial assumptions underlie the project's design. These assumptions deal with the (1) size of the SME client; (2) technical assistance; (3) excess demand for credit at high rates of interest; (4) co-financing; (5) role of the BAS Coordinator; and (6) role of the management assistance organizations. (Refer to Chart 1 for a summary.)

Size of SME Client

The lending policy adopted by FIA channels the bulk of credit to medium-sized enterprises. The size of the loan, application procedures, and targets set by size of the enterprise all assume that FIA will start credit at the top of its "borrower pyramid" and gradually move down. By FIA's third year of operation, 70 percent of its loans should go to small enterprises.

There is some concern that once a program is established, the momentum, lessons, and procedures attained in the first stage of implementation will prevail for the project's duration (Otero, 1985). As might be expected, the requests of larger, less risky enterprises were mostly approved at the outset of operations.

Role of Management Assistance Organizations

An assumption critical to SBD project design was that the management assistance organizations and FIA could reach the same client population. This means that management assistance organizations' clients are willing and able to graduate through the system to FIA quickly. While ANDI has funded

Chart 1

Assumptions of Project Design			
Assumption	Validity	Comments	Page #
Size of SMSE Client FIA will start lending to medium scale enterprises and gradually lend the bulk of its credit to small enterprise.	Partially valid	- less risky credit requests from larger enterprises have been approved at the outset; application procedures & an approval process skewed to favor medium sized enterprises.	page 14
Role of Management Assistance Organizations: Management assistance organizations and FIA reach the same client groups.	Not valid	FIA clients: Medium & larger small scale enterprises. NGO clients: small & micro. NGO clients have access to NGO credit funds.	page 14 - 16
Technical Assistance: Technical assistance is best provided outside the lending institution a) to avoid conflict regarding the responsibility of debt, and b) because a profit making lender has no incentive to provide TA for which there is no recovery.	a) Valid b) Not valid	There is sufficient spread between the cost of money and the interest charged.	page 16 - 17
Excess Demand for Credit at higher than market interest rates: SMSE's are willing & can afford to take longterm credit at higher than market rates.	excess demand not proven; Not valid	Higher than market interest rates remain a barrier to credit for SMSE's.	page 17 - 18
Co-financing will be provided by member banks.	Not valid	- difference in riskiness of FIA and bank clients; - FIA has excess funds, no need for bank co-financing.	page 18 - 19
Role of the BAS Coordinator: One organization can coordinate a complex TA and referral system while maintaining active interest & participation of four different groups.	Valid concept; assumption underestimated the difficulty in practice.	- lack of broad organizational participation in project design & understanding of project. - lack of program experience.	page 19 - 20

several management assistance organizations, few of these organizations' clients qualify for FIA credit. In addition, a great deal of PYME funding has gone to management assistance organizations with their own sources of credit. The referral of small enterprise clients to FIA has not developed as planned.

Among SMEs, FIA clients tend to be medium-sized and small enterprises, while the management assistance organizations' clients tend to be micro enterprises.

Within the parameters of the AID SBD Project, FIA and the PYME program now function as two totally different entities. With plans to establish a technical assistance unit within FIA and to rely on FIDE and independent contractors for feasibility studies, the operational divergence between PYME and FIA is likely to widen.

Technical Assistance

The SBD project design assumed that technical assistance is best provided by entities other than for-profit lending institutions. Profitmaking lenders have no interest or incentive in providing their clients with technical assistance, for which there is no recovery. Also, technical assistance provided to a client by the financial institution in pre-project feasibility can be misconstrued. It can be seen as a guarantee that the enterprise will succeed at the levels indicated in the feasibility study. Thus, the client can claim the feasibility study was faulty and question the responsibility for the debt. The first concern is valid when there is insufficient spread between the cost of money and the borrowers' interest rate for the lending institution to

recover the cost of technical assistance. This was not the case in the SBD Project. However, post-loan management and financial technical assistance needs are usually first detected by financial institutions, primarily because of the institution's profit motive and monitoring of loan repayment.

Excess Demand for Credit
at High Rates of Interest

The project design assumed a high demand for credit among SMEs. It further assumed that SMEs would tolerate an interest rate higher than the prevailing commercial rate to obtain term credit.

The feasibility study of the SBD Project assessed neither the supply of term financing in the formal and informal banking system nor the demand for term financing among SMEs. High collateral requirements and short-term credit, rather than high interest rates, were seen as the major barriers to commercial credit for these enterprises.

Contrary to prior assumptions, loans financed through private banks with resources from FONDEI have become options for FIA clients. FIA's market niche remains uncertain. To date, FIA has made 35 loans to SMEs. The Project Paper estimated that 140 loans would have been made by this time. FIA's high interest rate appears to hamper its pursuit of the market. The final interest rate for FIA-financed SMEs is at least 19 percent; the average portfolio reaches 21 percent. This places FIA rates consistently at or above commercial rates of interest, which are currently fluctuating between 11 percent and 15 percent.

Although there is a high level of liquidity in the banking system, term credit is available only to large enterprises and private banks that use the FONDEI rediscount line. Commercial banks currently charge between 11 and 13 percent on long-term loans rediscounted 100 percent through FONDEI. Of course, if FIA broadened its target market, it might obtain more clients, even at its present interest level.

One must not confuse what an SME will pay for informal market credit and formal market credit. The total cost of credit, rather than the rate, is an important consideration. While an SME will be willing to pay, for example, 24 percent annual interest on a three-month working capital loan for L.500, or even 1 percent a day on a working capital loan of L.50, the total cost of credit is relatively low and an amount the enterprise can afford. For an SME to afford 21 percent on a three-year loan for L.35,000 is quite another matter. Micro enterprises often pay the highest interest rates of 1 percent a day. These enterprises could not qualify for commercial credit and generally have no need to.

Co-Financing

USAID/H was interested in developing a financiera that the banking community would not view as direct competition. USAID/H sought private bank participation in FIA, with an ongoing working relationship and prospects for co-financing. USAID/H assumed that the five member banks that contributed L.1.0 million in share stock to the venture would, in time, provide L.4.0 million in co-financing of FIA projects. This has not occurred. The reasons given by FIA Board Members included: (1) FIA is a development-oriented financial institution seeking out clients that, by definition, do not meet

the banks' lending criteria; (2) FIA has approved a loan portfolio of L.3.5 million; L.4.5 million of its original capital remains for on-lending. There is no need to co-finance or utilize bank resources for market share expansion.

As designed, capital reflows are to be utilized only for lending purposes and to help assure non-USAID dependence for its capitalization. This will provide another source of loan capital.

The Role of BAS Coordinator

The project design assumed that the BAS Coordinator would (1) develop and manage a fairly complex technical assistance referral and support system and (2) coordinate and maintain active participation of four separate groups with individual different interests and biases. These groups are the owners of large industry, the small and medium-sized entrepreneurs, the NGO community, and commercial banks. No feasibility study assessed ANDI's institutional capacity to manage the PYME Project. Although an extensive survey of institutions supporting the small business sector was carried out as part of the SBD Project feasibility analysis, ANDI was not identified as a potential candidate for the role of BAS Coordinator. Both the Project Paper and the March 1985 review of the SBD Project point out that ANDI, the BAS System Coordinator, was approached by USAID/H only after the originally selected organization, Central American Institute of Business Administration (INCAE), declined the offer.

ANDI did not participate in the early design phases of the program component it was subsequently to develop and implement, due to its late arrival on the scene. This,

combined with ANDI's lack of experience and poor image among SMEs and NGO collaborator groups, contributed to a slow project start-up.

Prior to accepting the PYME Project and the role of BAS Coordinator, ANDI had no operational programs, no experience in the small business sector, and no experience with, or appreciation for, the NGO community from which the management assistance organizations would be selected. ANDI's image in both the small business sector and the NGO community was that of an organization composed of large industrialists who lobbied exclusively on their own behalf and had little interest in or knowledge of conditions affecting the small business sector. Considering its handicaps, ANDI has accomplished much in developing a small business support service for management assistance organizations and in enhancing its image vis-a-vis the small business sector.

Project Implementation

Project Start-Up

Although the project is considered by USAID/H to have gotten off to a slow start, a one-year start-up time seems reasonable considering the following factors: (1) the innovative design of the project; (2) the number of institutions involved (Central Bank/FONDEI, FIA, five member commercial banks, ANDI, and numerous management assistance organizations); and (3) the amount of time required to hire the FIA Manager (a decision involving all five banks), recruit staff, define internal policies and procedures, and negotiate agreements with FONDEI, USAID, ANDI, and the FIA Board. Other USAID-supported credit lending projects -- for example, the

Haitian Development Foundation, the Dominican Development Foundation, and financieras in Guatemala, Ecuador, and Bolivia -- have consumed similar or greater periods of start-up time. These projects also have no private banking sector support but aim to benefit similar clientele and develop new financial institutions.

The FIA Portfolio, Policies and Practices

General Characteristics of the Portfolio

In 1985, FIA financed 20 enterprises, with the lending portfolio reaching 35 as of November 1986 (see Table 1). Of the loans, 32, or over 90 percent, were extended to industry. One borrower was a cooperative, the others private firms. Three loans were extended to commerce and service enterprises, one of which was a trading company.

The market share has been fairly well distributed among furniture manufacturers (seven loans for 20 percent of the credit portfolio), the clothing industry (six loans for 17 percent), and the food products industry (five loans for 14 percent). Shoe manufacturers have received only two loans for 6 percent of the credits.

The majority of loans were placed with 21 enterprises seeking to expand, comprising 60 percent of the total portfolio. The remaining 40 percent went to new ventures: 13 manufacturing enterprises and one commerce/service company.

Table 1. Characteristics of FIA Loan Support

	Number	Percentage
<u>Enterprise sector</u>		
Industry	32	91
Commerce/service	<u>3</u>	<u>9</u>
Total	35	100
 <u>Loan type</u>		
<u>Expansionary</u>		
Industry	19	54
Commerce/service	<u>2</u>	<u>6</u>
Total	21	60
 <u>New Enterprise</u>		
Industry	13	37
Commerce/service	<u>1</u>	<u>3</u>
Total	14	40
 <u>Industry type</u>		
Furniture	7	20
Clothing	6	17
Food products	5	14
Shoes	<u>2</u>	<u>6</u>
Total	20	57
Other	<u>15</u>	<u>43</u>
Total	35	100

Quality of the Portfolio

The portfolio is made up of 35 business loans, as characterized earlier in Table 1. FIA's computer files on all clients enable it to trace the performance of its portfolio on a monthly basis. Company records are kept separately on both principal and interest payments. Table 2 outlines the enterprises, identified by number only, and their payment record as of June 30, 1986.

Defining arrears as the proportion of late payments to the total value of the portfolio is common practice throughout the banking community in Honduras. At the end of June 1986, the amount of arrears in FIA's portfolio was L.108,748.23, just 4.24 percent; L.78,573.89 of the late payments, or 72 percent, were 30 days or less behind in payments.

Interest payments are kept separately. As of June 1986, approximately 30 percent of the interest payments due were in arrears for 30 days or more. This adds up to approximately L.35,630, surpassing the capital accounts in arrears of 31 to 60 days (Table 2). Consistent with the Central Bank policy, FIA does not react to late payments until after 30 days. Arrearage is commonly measured the day after a loan payment is due and action taken within 15 days. FIA should tighten its arrearage policy generally, and not allow late payments at all during grace periods on principal, when only interest payments are due.

As of October 31, 1986, arrearage of principal payments had increased to 6.0 percent of the total portfolio; 43 percent of this amount is late by 30 days or less. For the same accounting period, interest payment arrearage of 30 days or more had increased to 54 percent, with 45 percent in the 31

Table 2. FIA's Late-Payment Report: June 30, 1986
(Lempiras)

Client	0-30 days	31-60	61-90	91-120	120+	Total
1.	2,777.78	2,777.78	2,777.78	2,396.56	-0-	10,729.90
2.	2,083.33	-0-	-0-	-0-	-0-	2,083.33
3.	46,333.67	-0-	-0-	-0-	-0-	46,333.67
4.	4,601.34	-0-	-0-	-0-	-0-	4,601.34
5.	8,333.33	8,333.33	-0-	-0-	-0-	16,666.66
6.	13,888.89	13,888.89	-0-	-0-	-0-	27,777.78
7.	555.55	-0-	-0-	-0-	-0-	555.55
Total	78,573.89	25,000.00	2,777.78	2,396.56	-0-	108,748.23

to 60 day category. This condition is more indicative of FIA's lax policy on loan recuperation than of the financial viability of the enterprise, as discussed later in this chapter.

For all practical purposes, interest earnings are FIA's only internal source of funds. Although the majority of these late interest payments are only 31 to 60 days behind scheduled payment, the matter is taken very seriously. Four firms have interest payments 60 to 90 days late, for a total of approximately L.9,500. Only one firm is late on its interest payments by more than 120 days.

FIA's arrearage and/or default policy is consistent with that of the banking community in Honduras. Clients 30 days late on any payment are contacted immediately to determine the reasons for payment delay. The accounts with longer payment delays are visited to clarify problems and to work out a payment plan. The Credit Officer and the General Manager have visited, sometimes repeatedly, all clients delinquent in their payments. FIA has not developed an operational policy for writing off bad debts. To date, only one company, Tiger International, has gone bankrupt; its assets being taken over by FIA. Only one company is rescheduling its debt to FIA.

Lending Policy

This section summarizes the SBD project's lending policy as originally planned in the Project Paper and in the AID-GOH Project Agreement of May 1984. Comments are made on changes in policy, where appropriate.

Target Beneficiaries

Medium-sized and small enterprises are the primary beneficiaries of this project. Medium-sized enterprises are defined as holding total assets of US\$125,001 to \$1.0 million, employing 20 to 100 people, and with average assets per worker of \$5,000 to \$15,000. Small enterprises hold assets of between \$5,000 and \$125,000, employing 5 to 20 people, with average assets per worker of \$1,000 to \$5,000. In all cases, beneficiaries operate in the small- and medium-scale industry sector, agriculture, and service sectors, and require financing with terms and other conditions that commercial banks will not meet.

Size of Loans

The minimum loan amount is L.10,000. The maximum loan amount is L.1.0 million or up to 80 percent of the total assets of the client, whichever is less. No single client can borrow more than 50 percent of FIA's total capital. Until recently (with the new pledge of additional capital by the owners), the maximum loan was L.250,000. FIA's practice is consistent with SBD lending policy.

Loan Categories

Loans are to be used for investment and working capital, including operating costs, raw materials, and machinery and equipment. FIA will not finance housing mortgages, refinance existing debts, or finance the purchase of vehicles, land, or buildings, "except under carefully controlled circumstances."

Terms of Loans

The actual terms are developed around the needs of the client. Terms cannot exceed three years for working capital, with up to a one-year grace period on the principal. Terms cannot exceed seven years for fixed asset investment, with up to a two-year grace period. Interest rates originating at no less than 8 percent (established by USAID/H) above the highest Central Bank Discount Rate, calculated in this project at 13 percent, resulted in a loan portfolio averaging 21 percent. The Central Bank Discount Rate has since been lowered to 9 percent and FIA is allowed to fix the interest rate to the final borrower at its discretion, but not less than the lowest rate currently charged by FONDEI (17 percent).

Collateral Requirements

FIA requires 100 percent collateral for the loan amount and will accept up to 80 percent of estimated market value of the assets pledged. The definition of collateral is broader than that of commercial banks and includes equipment, raw materials, and inventories.

Loan Approval Process

The FIA loan officers review loan applications to determine the accuracy of the information provided. The review focuses on the project's capacity to generate sufficient cash flow to pay for the loan as well as the entrepreneur's ability and honesty. This review includes a site visit. The General Manager receives the Loan Officer's recommendation and presents all loan requests to the Board of Directors for final decision. This is contrary to the Project Paper and the

Project Agreement, which provided that the General Manager was to have authority to approve credits up to L.100,000 (US\$50,000) and that an internal Loan Committee, consisting of FIA staff and two or three Board members, would approve all other loans. Loan disbursements and payments are made through banks.

Credit Application and Review Process

Depending on the complexity of the proposal and financing requirements, a loan can be approved within a month. With new enterprises, the owner(s) must provide 25 percent of the total financing; in the case of expansion proposals, a minimum of 10 percent is required. The average time from application to loan approval is 45 days. In 18 months of operations, FIA has financed 35 companies, or just under two a month. Fifteen of these entrepreneurs received technical assistance through the ANDI/PYME program. The majority of this support assisted entrepreneurs in preparing their project feasibility studies, financial statements, and business plans.

Currently, 18 loan applications are "on hold" for a variety of reasons. According to the General Manager, the majority lack sufficient documentation, market, and financial analysis. There is a real need to improve proposal preparation/analysis and standardize the accounting procedures of all clients.

The evaluation team was able to sit in on a credit review meeting in FIA and observe the loan approval process. This section summarizes the steps from loan application to loan approval.

The Credit Application

The application format is a straightforward, two-page request seeking general information about the company/entrepreneur, the project to which the loan will be applied, and collateral/guarantees with which to secure the loan. The use of collateral affects the interest rate that FIA charges its clients -- reduced to 18 percent rather than the average rate of 21 percent when the loans are guaranteed with machinery and/or co-signatures. Only six of FIA's 35 borrowers use real estate as collateral. Market feasibility studies are also requested, as well as detailed information on the following:

- . Actual and projected production figures
- . Detailed costs on production, administration, and sales
- . Raw materials: imported and national
- . Sales: national and export
- . Financial statements for last three years
- . Cash flow: current and projected for three years
- . Financial statements projected three years
- . Investment plan and sources of financing
- . Employment: male and female, current and projected
- . Legal papers of company

Prospective Client Visits

A potential borrower visits the FIA office to discuss the project. Often a consultant works with the entrepreneur to carry out the market feasibility study and assist in preparing

the business proposal. The consultant visits the FIA office with the prospective borrower. The enterprise is visited at least once by either the Loan Officer or by both the Loan Officer and General Manager.

FIA Credit Review Meeting

Every week, the General Manager, Credit Officer, and Operations Officer (entire professional staff) meet to discuss credit proposals completed for their review. The review is very thorough and open. Each application is presented by the staff person who has had the closest contact and working relationship with the prospective client. Questions on the project's soundness raised in previous reviews are addressed with a status update. Discussion concludes with a final recommendation made by the staff person managing the application. Positive recommendations are then referred to the Board of Directors.

Board of Directors Meeting

The FIA Board meets once a month to review the loan applications and proposals or more frequently if a special meeting is called. Currently, the FIA Board has the last word on approval or disapproval of all loans.

Depending on the complexity of the proposal and financing requirements -- with new enterprises, the owner(s) must provide 25 percent of the total financing, in the case of expansion proposals, a minimum of 10 percent is required -- a loan can be approved within a month, with 45 days stated as the average time for application to loan approval turnaround time.

In 18 months of operations, FIA has financed 35 companies, or just under two a month. Fifteen of these entrepreneurs received technical assistance financed by the ANDI/PYME program. The majority of this support was utilized to assist the entrepreneurs in preparing their project feasibility studies, financial statements, and business plans. Currently, 18 loan applications are "on hold" for a variety of reasons. According to the General Manager, the majority lack sufficient documentation, market, and financial analysis. There is a real need to improve proposal preparation and analysis, along with standardizing the accounting procedures of all clients.

From BAS to the PYME Program

While the main functions of the PYME program are grant-making and organizing INFOP training courses for management assistance organizations and directly for SMEs, the BAS does not function as an active and coordinated support network of small business assistance providers, as originally intended. Launching this type of coordinated network is a complex undertaking. It requires more time and expertise in the field; policy-directed, human and monetary resources program and research interventions; and the authority (within the community and USAID) to carry out the program.

ANDI has succeeded in developing components of a small business assistance program with design systems to support it. However, a comprehensive and unified program backed by strategic planning has not been developed. The remainder of this chapter analyzes those program components and concludes with a discussion of future program plans.

Grants to Management
Assistance Organizations

PYME has a consistently good reputation as an efficient and credible funder of projects that benefit the small business sector. PYME has also financed a number of management assistance organizations with good reputations in their work with diverse client groups.

Grantees

PYME approved its first grant to a management assistance organization in August 1985. To date, PYME has approved 20 projects with 13 management assistance organizations. (For a detailed description of the number and size of grants, refer to Table 3). Each project, with the possible exception of the Honduran Federation of Housing Cooperatives (FEHCOVIL) housing credit feasibility study, benefits clients within the SBD project target group. The bulk of PYME assistance, 43 percent, has gone to two national organizations that work directly with SMEs -- the National Association of Medium and Small Industries (ANMPI) and the Honduran Federation of Industrial Cooperatives (FEHCIL). In the last six months, PYME has attempted to extend its institutional and geographic coverage to include both new organizations and areas outside the main urban centers of Tegucigalpa and San Pedro Sula (see Table 4).

Gender Concerns

PYME does not maintain gender-specific data. Therefore, it is difficult to identify projects that benefit women entrepreneurs but are not sponsored by organizations focusing on women clients. Four approved and pending projects (14

Table 3. PYI E Program Grants to Management Assistance Organizations, 1985-1986

Organization	Project	Amount of Funds	Project Status
ANMPI	Accounting Training & TA	34,648	Complete. Final evaluation.
ANMPI	Credit Preparation & Industrial Classification	52,112	Complete.
ANMPI	Bank of Materials	4,000	
ANMPI	Credit Program Support	54,774	
ANMPI	Accounting Training & TA	66,307	Approved. Disbursement pending budget authorization.
AHDEJUMPUR	Regional Office Support	62,530	
ANAH	Central American Fair	11,162	Approved. Disbursement pending budget authorization.
ASESPADE	Marketing Training	31,600	
CIL	Feasibility Study	1,800	
Coop Sastres	Production TA	12,000	
FEHCIL	Marketing TA	31,900	
FEHCIL	Production TA	90,763	
FEHCIL	Institutional Analysis	35,800	
FEHCIL	Evaluation Training	3,550	Approved. Disbursement pending budget authorization.
FEHCOVIL	Housing Feasibility Study	10,000	
FUNADEH	Business Training	40,800	
FUNADEH	Marketing TA	12,650	
FUNDEMU	Credit Office Support	37,731	
IDH	Regional Office Support	16,899	
INHBIER	Org. Development/Training	25,799	Completed. Final evaluation.
INFOP	Accounts Training to ANMPI	3,940	
ODEF	Training Bus/Marketing	74,200	
FUNDAMU	Training-Credit Program	37,300	Pending approval.
INHBIER	Training-Business	85,375	Pending approval.
Fund Horizontes de Amistad	Training	<u>42,900</u>	Pending approval.
		880,540	

Table 4. PYME Support to Organizations: Amounts, Percent Portfolio, Rural/Urban Focus, WID Focus

Organization	Number of projects	Amount of funds	Percent of portfolio	Major project activity in rural areas	WID focus	New organization last 6 month
ANMPI	6 ^{a,b}	215,781.00	25			
FEHCIL	4 ^a	162,013.00	18			
INHBIER	2 ^a	111,174.00	13	X		
FUNDAMU	2 ^a	75,031.00	8		X	
ODEF	1	74,200.00	8	X	X	X
AHDEJUMPUR	1	62,530.00	7	X	X	X
FUNADEH	2	53,450.00	6	X	X ^c	
FUNDACION HORIZONTES	1 ^a	42,900.00	5	X		X
ASEPADE	1	31,600.00	4	X	X	X
IDH	1	16,899.00	2	X		
SASTRES	1	12,000.00	1			X
ANAH	1 ^a	11,162.00	1			X
FEHCOVIL	1	10,000.00	1			
CIL	1	1,800.00	---			
	29	880,540.00	99%	6	5	6

- a. Includes projects pending at the Committee level.
b. Includes grant made to INFOP to provide TA to ANMPI clients.
c. One project L. 12,650 benefitted mostly women entrepreneurs.

percent of all projects) and 24 percent of the grants portfolio are supported by organizations with a focus on women clients. At least three additional projects (an additional 10 percent of all projects) and an additional 6 percent of the grants portfolio have benefitted or are designed to benefit women entrepreneurs (see Table 4).

Projects and Selection Criteria

The bulk of PYME's current grant portfolio, 91 percent of designated funds, supports training programs, technical assistance activities, and credit program offices (see Table 5). Project selection criteria have been developed and are consistently applied to grant requests by PYME program staff and decisionmakers. Selection criteria favor small grants to management assistance organizations that work directly with SMEs in increasing or maintaining employment and income. Criteria favor (1) the expansion of management assistance activities that have proven effective in supporting SMEs, and (2) the development of new activities that provide technical and financial assistance to SMEs without access to these resources. New credit programs or regional credit and technical assistance offices are examples of such activities.

Grantor Efficiency

In interviews at three management assistance organizations, representing 50 percent of the PYME project portfolio, representatives indicated that they had not experienced any unexpected delays in any of the four crucial time periods for donors. These are the intervals between (1) project request and approval; (2) project approval and signing of the grant agreement; (3) signing of the grant agreement and disbursing funds; and (4) submitting reports and receiving subsequent

Table 5. PYME Project Portfolio by Program Area

Program area	Number of projects	Amount in L. (US\$ = 2L)	Percent of projects	Percent of portfolio
Training & technical assistance	12	476,719.00	54.5	67
Business development ^a	2	115,000.00		
Accounting	3	104,895.00		
Production	2	102,763.00		
Marketing	3	76,150.00		
Credit preparation	1	52,112.00		
Organizational development	1	25,799.00		
Credit program staff support	4	171,934.00	18	24
New programs	2	92,505.00		
New regional offices	2	79,429.00		
Institutional analysis & evaluation	2	39,350.00	9	5.5
Feasibility studies	3	15,000.00	14	2
Miscellaneous: international fair	<u>1</u>	<u>11,162.00</u>	<u>4.5</u>	<u>1</u>
	22	714,965.00	100	100

a. Includes elements of marketing, production, management, and accounting.

disbursements. Each of the organizations interviewed had one project pending with the PYME Committee due to delayed authorization of the 1986-87 PYME budget. The organizations' representatives indicated that this delay was not exceptional when compared with grant processing procedures of other donors.

Donor Collaboration

While donor collaboration is not a strength of the current PYME program, a number of PYME grants have benefitted organizations that subsequently received complementary credit program funding from FOPRIDEH. In addition, FOPRIDEH has requested PYME to co-finance two of its approved projects. To date, however, there has been little communication, other than an exchange of co-financing information, and little collaboration between PYME and FOPRIDEH on any other matters.

Technical Assistance

The bulk of technical assistance financed directly by the PYME program has been delivered to (1) FIA clients, at FIA's request, and (2) the National Association of Medium and Small Industries (ANMPI), through a grant to generate clients for FIA.

FIA Clients

Since June 1985, 15 FIA clients have benefitted from PYME-financed technical assistance consultancies. This represents 43 percent of total FIA clients and accounts for 23 percent of FIA's total portfolio. This amount also represents 50 percent of FIA small business clients (see Tables 6 and 7

Table 6. Technical Assistance Provided to FIA Clients and Other Enterprises

Name of business	PYME financing provided (lempiras)	TA organization	Size of business	Amount of FIA loan -----lempiras-----	Amount of other loan
FIA Clients					
Tiger International	34,500	FIDE	Medium	250,000	
MADETEX	7,000	FIDE	Medium	181,000	
Fibra-Plast	1,900	Ind.	Small	30,000	
Sol Y Verde	1,300	Ind.			
DIDA	2,750	Ind.	Medium	50,000	
Comercial Ericka	1,750	Ind.	Small	55,500	
Imp Y Pap Hond.	2,000	Ind.	Small	75,000	
Moda Marthy	600	Ind.	Small	10,000	
MAPRIMA	14,500	FIDE	Medium	250,000	
Tabor International	6,000	FIDE			
Suyapa			Small	25,000	
Mariol			Medium	65,000	
Subtotal	<u>72,300</u>			<u>991,500</u>	
Other^a					
Coop La Fraternidad	500		Small	25,000	
Zapateria Nancy	ANMPI grant	Ind.	Small	31,000	
Serv. Alimenticios	ANMPI grant	Ind.	Small	100,000	
Confecciones AGLOM	ANMPI grant	Ind.	Small	15,000	
Industria INDUMA	ANMPI grant	Ind.	Medium	105,000	
Coop Agro/Ind. Maya	UNICOCP grant	Ind.			250,000
Coop 20 de Marzo	UNICOOP grant	Ind.			<u>286,600</u>
Subtotal	<u>6,360</u>			<u>276,000</u>	<u>536,000</u>
Total	78,660			1,267,500	536,600

Note: The ANMPI grant for credit preparation and industrial classification totals L.52,112. L.18,750 has been disbursed to date to assist enterprises in credit preparation packages. 23 have submitted credit requests to FIA. L.3,260 is an average calculated for the four businesses listed.

a. Given technical assistance in order to generate FIA clients.

Sources: FIA computer print-out, October 1986; PYME reports "Asistencia Tecnica Prestatorios de FIA" and "Proyecto de Proyectos y en Marcha"; PYME Financial Statements, September 30, 1986; PYME

Table 7. FIA Clients Assisted and Generated by PYME Program:
 Number and Percent of Clients, Amount
 and Percent of Portfolio

	Number	Loan amount (lempiras)	Number	Loan amount (lempiras)	Percent amount	Percent clients
Total FIA clients:			PYME-assisted FIA clients:			
New business	14	1,594,400	6	480,000	30	43
Expansion	21	2,985,136	9	827,500	28	43
Total	35	4,579,536	15	1,037,500	23	43
Small	18	1,030,900	9	336,500	33	50
Small/medium	1	156,552	--	--	--	--
Medium	17	3,392,084	6	941,000	28	35
Total	35	4,579,536	15	1,037,500	23	43
Total FIA clients:			PYME-generated FIA clients:			
New business	14	1,594,400	2	125,000	8	1
Expansion	21	2,955,136	3	151,000	5	1
Total	35	4,579,536	5	276,000	6	1
Small business	18	1,030,900	4	171,000	17	2
Small/medium	1	156,551	--	--	--	--
Medium	17	3,392,084	1	105,000	3	6
Total	35	4,579,536	5	276,000	6	14

for details). The technical assistance consultancies were carried out by FIDE and a private firm, both selected by FIA. Most of the consultancies provided technical services in the analysis of project feasibility, accounting, and market analysis.

Generation of FIA Clients

PYME has had trouble referring clients to FIA, due to FIA's high interest rates. Although FIA collateral requirements are lower than commercial banks, and the repayment period longer, most of the management assistance organizations' clients are still not in a position to take advantage of FIA financing.

In order to generate new clients for FIA, PYME financed a project in credit preparation and industrial classification for those ANMPI clients best able to take advantage of FIA credit. Fifty firms were expected to receive credit from FIA and other sources. Only 30 firms prepared credit requests; 23 of these firms approached FIA for credit. To date, four ANMPI beneficiaries have received credit from FIA, one request was turned down, and the remaining requests await FIA's analysis and decision.

Other Technical Assistance Recipients

PYME has also financed feasibility studies for three cooperatives. One cooperative obtained FIA credit and the two others obtained credit from BANADESA, the Honduran Development Bank.

Training Program

INFOP Courses

The PYME program has reached approximately 60 percent of its targets in this area (see Table 8). In March 1986, PYME negotiated an agreement with INFOP, a government organization that provides management and vocational training courses. To date, PYME and INFOP have jointly sponsored 16 training courses for 245 SME owners and employees and management assistance organization staff members. PYME indicates that 199 of these course participants are SME owners (see Table 9).

INFOP courses have received mixed reviews regarding the quality of instructors, course materials, and course content. Since INFOP courses employ pre-packaged modules, it is up to the instructors to modify curriculum and course material. Quality of instructors tends to vary widely, although two instructors trained by Partnership for Productivity have been rated highly by PYME staff.

INFOP courses have been criticized for a theoretical approach and/or a course content above the heads of the participants. Courses have been criticized for merely reviewing basic material or previously acquired skills, and therefore not developing professional capabilities. Since course participants often have different educational levels and come from a variety of backgrounds, it is difficult to adjust course content, materials, and delivery style for the "average" participant.

PYME has found it difficult to track follow-on services to INFOP course participants systematically. The PYME/INFOP agreement specifies that follow-up is INFOP's responsibility.

Table 8. PYME-Sponsored Training Courses:
Planned/Accomplished 1985-1986

Area	Planned	Accomplished	Percent
Courses to NGO staff	11	7	63
Number of participants	163	68	42
Number of organizations	47	5	11
Courses directly to SMEs	30	16	53
Number of participants	425	245	57
Number of businesses	280	199	71
Courses given by NGOs to SMEs	30	28	93
Number of participants	600	772	100
Totals:			
Courses	71	51	
Participants	1,163	1,085	

Source: PYME Program Accomplishments, August 31, 1986.

Table 9. Training Courses INFOP/INCAE

Course provider	Course area	Number of courses	Number of participants	Number of organization personnel	Number of business personnel
INFOP	Marketing & sales	5	85	7	78
INFOP	Accounting	5	65	7	58
INFOP	Personnel management	2	40	24	16
INFOP	Production	2	33	6	27
INFOP	Administration	1	14	1	13
INCAE	Export markets ^a	1	8	1	7
Total		16	245	46	199

a. Courses given to FIA clients.

Source: ANDI/PYME Program Accomplishments as of August 31, 1986.

Currently this is not being carried out consistently. Some organizations, such as FEHCIL and ANMPI, receive INFOP assistance directly (at times financed by PYME) and through the PYME/INFOP training program. INFOP seems most likely to provide follow-on services when it works directly with the management assistance organization.

Management Assistance Organization
Staff Training Program

The PYME program has reached only 40 percent of its targets in this activity (Table 8 above). The management assistance organization staff training program has been the most difficult for PYME to develop and implement. PYME records indicate that seven courses have been held for eight different management assistance organizations (see Table 10).

There has been no organized effort to assess the staff development needs of the management assistance organizations. This may be attributable to the recent resignation of the Training Officer. Whatever the reason, PYME has not established a professional development needs assessment system. Although the staff development needs of management assistance organizations were assessed during a November 1985 seminar, this analysis may be dated. PYME records do not indicate that all of the courses identified by management assistance organization staff (financial analysis, planning, and credit programs) were carried out.

To date, PYME staff have not directly developed any courses for management assistance organization staffs. A course on financial administration was given by the PADF Advisor to three members of the ANMPI staff, and a course on evaluation was developed by the PADF Advisor and given to the

Table 10. Training Courses for Staffs of Management Assistance Organizations

Course	Organization	Number of participants	Reports
Financial Administration	ANMPI	3	Oct-Dec 85
Marketing	FEHCIL	10	Oct-Dec 85
Business Analysis	FUDEHMU	2	April-June 86
Human Resource Development	ODEF	4	April-June 86
Feasibility Study & Marketing	ODEF	4	April-June 86
Study of Work & Motivation: Communication	7 organizations	10	August 86
Total: 6 courses	7 organizations	33	

Note: Information was reconstructed from quarterly reports for the period. There are some discrepancies in reporting. Information through August 8, 1986 indicates that five courses were given but to 29 participants representing eight different organizations (see below). Summary of program achievements through August 31, 1986 indicates that seven courses were given to 68 participants representing only five organizations.

Organizations	Courses	Number of participants	Number of organizations
ANMPI	1	3	--
ODEF	2	8	--
Various	2	18	8
Total	5	29	8

Sources: Cursos realizados por el Programa ANDI-PYME para el personal de las organizaciones de desarrollo empresarial, August 8, 1986.

PYME staff. Plans are being finalized to give this course to interested management assistance organizations in early 1987.

PYME-Financed Management Assistance
Organization Training Programs

Management assistance organizations, such as FEHCIL, Overseas Education Fund (ODEF), ANMPI, and the Honduran National Development Foundation (FUNADEH) have received PYME grant financing to develop their own course methodology. In many cases, these organizations hired outside technical advisors, such as International Executive Service Corps (IESC) and local consultants, to develop course materials and a presentation style to suit a particular audience. These consultants worked directly with the management assistance organization's training staff. Their courses have been generally well received. This approach to training has several advantages:

- . The course trainer is more directly accountable to the management assistance organization.
- . Organization staff who have worked with course trainers become familiar with course content and can better provide subsequent technical assistance to the client.
- . These staff also begin to learn training methodology.
- . Information collection for monitoring, evaluation, and program management purposes becomes more thorough and reliable.

According to PYME records, which are based on management assistance organizations' reports and PYME monitoring and

evaluation reports, 772 SME owners and employees have benefited from 28 management assistance organization training courses financed by PYME. The PYME program has reached all of its targets in this activity.

Records are incomplete on follow-up and course impact on the operation, management, and profitability of SMEs. This is partly due to the recent approval of the majority of PYME-financed projects and the recent hiring of the Monitoring and Evaluation Officer. With this additional staff member, information collection and analysis of project impact are expected to improve.

Reports and interviews with beneficiaries indicate that SME owners are adopting practices introduced in the training courses. This seems to have affected SME operations, leading, in some cases, to a reduction of variable unit costs and an increase in sales volume. Improved production techniques have also led, in some cases, to an expansion of employment for previously unemployed and unskilled labor. (For a more detailed discussion of this topic, refer to the section on impact.)

Inter-Institutional Information Network

As reasonably expected during the first year of operation, the newsletters published and seminars held as a part of this activity have focused on promotional and informational exchange. The seminars have helped PYME identify management organizations active in the sector and SME needs. They have contributed more in this regard than in directly benefitting

the management assistance organizations or in developing opportunities for collaborative efforts and joint programs.

The challenge facing PYME in this program is how to modify the Inter-Institutional Network from its present information/promotional bias to a more active support system. The network should encourage management assistance organizations' collaborative efforts in responding to sector needs.

Monitoring and Evaluation Program

This program monitors and evaluates PYME-funded projects and seeks to develop a national service assessment and impact evaluation system. The latter is expected to be implemented in the coming year. Both systems include provisions for disaggregating data by gender.

Information on program results is collected in a fairly, comprehensive manner. Impact information has not yet been synthesized. However, PYME does establish concrete indicators for each project's success at the time of project analysis. This should enable PYME to use and disseminate the impact data.

The efficiency and effectiveness of the impact evaluation systems will depend on the compatibility of the individual management assistance organizations' evaluation systems. The evaluation team reviewed three impact evaluations of PYME-financed projects. The level of detail, substance, and coverage varied. This was due to the effectiveness of the implementing organizations' evaluation systems rather than the nature of the projects or the abilities of the evaluator. For example, many management assistance organizations do not regularly collect data of concern to PYME, such as the income

levels of the beneficiaries and the changes in enterprise performance due to technical assistance and training. PYME intends to remedy this situation through scheduled monitoring and evaluation program activities. However, producing impact evaluations with consistently valid and reliable information will be a frustrating and unmanageable tasks for PYME staff unless the grantee organizations have compatible data collection and evaluation systems.

Minor discrepancies between individual reports and reporting summaries can be remedied by cross checking figures. A tendency to double count program beneficiaries presents an inaccurate account of program coverage. Data on management assistance organization course participants focus on the number of course participants rather than the number of people trained. PYME staff may believe, for example, that eight ODEF staff members received training, when in fact four staff members attended two different courses. The same is true for data on SME course participants. These data must be disaggregated if the PYME program is to determine the number of SMEs it reaches and develop improved follow-up services.

It is too early to judge whether PYME will learn from its evaluation material how to develop better donors and program collaborators. There are some early indications that PYME will use its program experience to improve operations. For example, PYME has adjusted project selection criteria for financing feasibility studies.

ANDI/PYME Planning and Future Plans

Budget and program plans tend to include more than an organization can reasonably accomplish. Programmed activities, especially for the next three years, represent a range

of possibilities rather than an analysis of priorities. One of the reasons for a lack of analysis and priority-setting may be that PYME has always had more budget than it can reasonably spend. PYME has been under pressure to grow, in any direction.

The 1986-87 Annual Plan

The PYME program has developed an annual plan for Fiscal Year 1986-87 which expands the four program areas by increasing their number of activities and developing new activities within each area. The 1986-87 annual plan also contemplates doubling the budget and increasing the professional staff by two.

Stable and balanced program growth requires PYME to research new areas; it also requires PYME to analyze the patterns of its growth and the value of its programs. Given the program's past record in program development and its current management style, it seems highly unlikely that PYME will be able to complete its ambitious plan while continuing to develop quality support to management assistance organizations.

The Three-Year Strategy (1987-1990)

The three-year strategy (1987-1990) increases the budget by an additional 50 percent. While the majority of activities in the strategy seem consistent with the PYME program mandate, the strategy also includes areas inappropriate for PYME program expansion. These are: (1) a computerized credit data bank on management assistance organizations' SME clients, (2) a small library for the use of SME clients, and (3) the

provision of grants to organizations working with agricultural producers. While the library and data bank are interesting support services, they would be difficult to implement because they inappropriately centralize activities. They also add a PYME staff management burden for activities that may be best implemented by the organizations for their own clients.

PYME should extend more support to agro-industry and rural enterprises. However, it tends to include agricultural production, agricultural credit, and rural infrastructure (irrigation/water supply) in this target area as well. In the opinion of the evaluators, these areas are inappropriate for the PYME program. While a project analyst with experience in rural industry may be an appropriate addition to the PYME program staff, an agricultural extension agent is not.

In planning for the future, ANDI should (1) ensure that program development efforts fall within the PYME program's mandate and (2) resist temptation to respond to pressing needs outside the SME sector. PYME should look to its strengths, resources, and mandate rather than attempting to respond to every need. Taking the time to examine PYME's organization philosophy, operating principles, program options, and alternatives can prevent haphazard program growth.

Management and Institutional Development

FIA

Issues of FIA's Expansion

To accomplish the objectives of the SBD Project while operating in the private sector, FIA must adjust its internal policies and procedures to balance its development-oriented

charter and for-profit objectives. FIA's current bank ownership and the planned mobilization of share capital from other than commercial banks presents at least two potential obstacles to project implementation and expansion of FIA's portfolio.

First, despite personal interest in the development of Honduras, the bankowners and FIA's General Manager must be concerned with shareholders' capital and, therefore, must seek profitable investment with minimum risk. Second, assuming that FIA develops into a viable lending institution, it could be difficult to persuade the "founding" Board members to allow other interests to join the Board or to hold significant shares of stock when the banks alone took the up-front, start-up risks. According to a number of business people in Tegucigalpa, additional investment in FIA by other private sector interests will be required if FIA is to expand.

FIA interest rate policy is proving incompatible with lending to small enterprises. As of July 1986, FIA rejected nearly L.3.0 million in loan requests because their projected return was not high enough to cover FIA's 21 percent average interest rate. In most cases, the projected return was 16 or 17 percent.

The cost of borrowing, rather than collateral requirements, has become a major obstacle for small businesses obtaining credit at FIA. FIA's current administrative expenses amount to about 5 to 6 percent. With the current discount rate of FONDEI at 9 percent, FIA should be able to charge its clients a minimum rate of 15 to 17 percent. USAID has already taken action on this issue; rather than dictating a final rate to FIA, USAID will allow FIA to set its own rate

consistent with current market rates (Grossman, USAID Action Memo, July 1986).

The turnaround time for credit decisions has become exaggerated and has affected FIA expansion. The approval procedure was not part of the project design or agreement. While the Board wished the project to have a proper start, there is now broad confidence in FIA's management capacity and an awareness that the internal credit committee should have loan approval authority.

Financial Income and Viability

As a result of its conservative portfolio growth and lack of personnel to develop projects, supervise loans, and provide technical assistance, FIA's 1985 operating expenses had to be covered with a total portfolio of only L.2.3 million. FIA lost L.111.,000 and was unable to establish loan loss reserves. In March 1986, FIA broke even; the FIA Board agreed to invest an additional L.500,000 within nine months. Loan loss reserves were to be set aside from the interest FIA receives on the unused portion of loan funds deposited in the stockholders' banks.

In 1985, FIA's interest income was L.145,202. From January through August 1986, interest income registered L.379,138, an increase of over 2.6 times the 1985 total annual figure. Income from other sources is nearly non-existent.

In 1986, FIA nearly tripled its long-term liabilities over 1985, which helps explain the sharp increase in operating costs. FIA's current ratio has increased from 1.72 to 2.72 in 1986, a reasonable coverage of short-term liabilities. The total cost to lend one lempira was .11 centavos in 1985; this

increased to .34 in 1986 (5.5 to 17.0 U.S. cents equivalent for 1985-86). During this period, FIA staff was closely monitoring their clients to assure timely payback. With relatively few clients and increasing monitoring costs, the cost of lending can only increase.

Incidentally, the cost of 45 cents (equivalent) per dollar lent by a USAID-funded project in support of small and micro enterprises in the Dominican Republic was found to be "reasonable" compared to other AID-funded financial organizations supporting this target group in a half dozen countries (Sara Wines, 1985).

Staff Capacity and Management

FIA management and staff capacity are considered to be of the highest quality. The small staff works extremely well together; they have proven themselves, within their first year and a half of operation, under close scrutiny from the banking, private sector, and the donor community of Honduras. FIA has established an excellent computerized information system and has received top quality technical assistance in both development and use of this system. Financial information and socioeconomic data are collected on each client; this should allow FIA to track the financial and economic impact of the SBD project throughout its life and beyond. The FIA General Manager wants all of the credit officers and technical assistance staff to receive computer programming training. This will improve existing enterprise project analysis, supervision, and follow-up. It will also enable FIA staff to use and/or develop new methodologies appropriate to the client's needs.

The FIA General Manager and his staff visit each client at least once a month. According to entrepreneurs visited, FIA support is impressive. Specific areas of support mentioned included advice on a variety of production problems, financial and legal issues, and assistance in linking them to consultants or agencies (e.g., FIDE) who can answer marketing questions and explain procedures for exporting to the United States.

Future Plans

Technical assistance for FIA clients has been only marginally successful. The PYME program has worked with a number of PVOs to improve their ability to deliver services to small and medium enterprises, especially to those enterprises too small to fit into FIA's small to medium-sized enterprise clientele.

In October 1986, FIA presented a technical assistance plan to USAID for review and guidance in establishing its own technical assistance unit. The plan calls for the organization of three categories of technical assistance support to FIA clients and prospective clients.

Project development: The primary objective of this activity is to develop feasible small and medium-sized enterprise projects. FIA will organize workshops and contract agencies or individual consultants to provide assistance to prospective entrepreneurs in developing and presenting appropriate project proposals.

FIA management is well aware of the need to standardize both project proposal presentations and financial reporting methodologies. A recurring problem has been the lack of well

prepared proposals by prospective clients. When independent consultants assisted in proposal preparation, the proposals often did not address all of the FIA requirements and, at times, did not employ acceptable market and financial analysis methodologies. FIA is developing a brochure that will set forth the basic information required in presenting an appropriate project proposal.

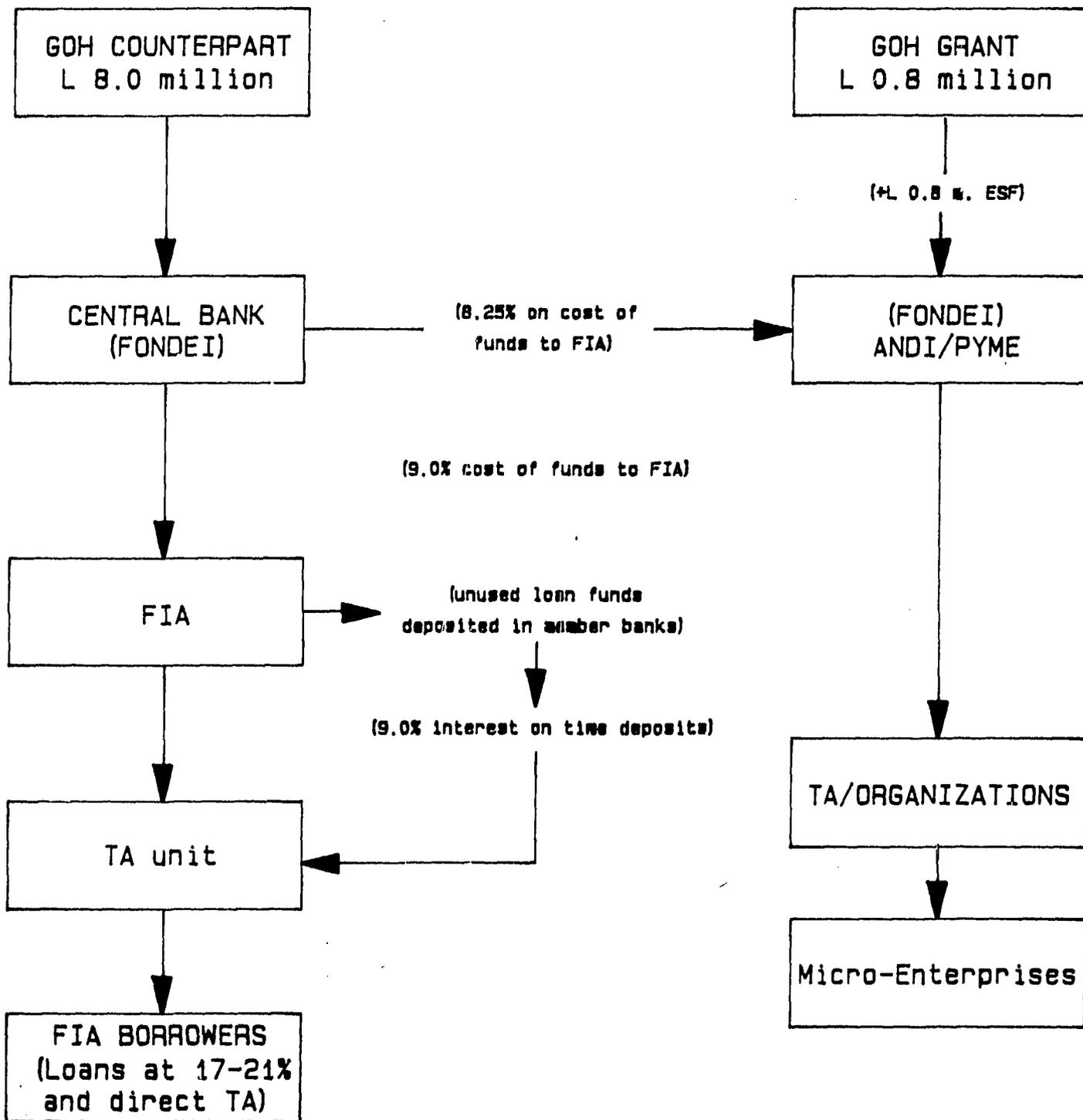
Supervision and follow-up: These activities, carried out by FIA staff, will concentrate on detecting problems within an enterprise that could affect its capacity to repay the loan. The primary objective is to minimize the risk in credit recovery. FIA staff will assure that loan funds are used according to the investment plan and credit agreement, while evaluating the enterprise's need for specific technical assistance.

Specialized technical assistance: Experience to date has demonstrated that a given enterprise often will have a very specific need for improving administrative systems, production, or quality control. FIA is developing evaluation tools that will help detect specific problems within an enterprise. FIA plans to provide financing to the entrepreneur to cover the costs of this specific technical assistance. At present, this is the only technical assistance component that is anticipated to be financially self-sufficient.

The costs of product development, supervision, and follow-up will be covered after start-up costs by the interest earned on the GOH funds deposited in the member banks (see Diagram 2).

Diagram 2.

Current Project Design--September 1986



The PYME Program

Organization Structure and Staffing

An organizational diagram of ANDI is presented in Diagram 3 and the PYME program is depicted in Diagram 4.

The Program Manager is responsible to both the Executive Secretary and the PYME Committee. The Executive Secretary is responsible to the Board of Directors of ANDI. Four of the seven PYME committee members also sit on the Board of ANDI; thus, there is a clear line of authority and responsibility within the program structure.

Staff Turnover

Since the beginning of the project in June 1984, all important staff positions within the PYME program, with the exception of the PADF Advisor, have been vacated at different times. These positions include the Executive Secretary of ANDI, the PYME Program Manager, and the Training Officer. The rest of the current staff members have been hired relatively recently. Complete staff turnover within the first year of the project contributed to early problems with program direction, identity, slow start-up, and progress.

The current staff seems well aware of the history of the program. This is due, in part, to the presence of the PADF Advisor throughout the project and the joint FIA/PYME/AID meetings held to discuss the project and negotiate the tripartite agreement during mid-1985. These meetings provided the first opportunity for many PYME Committee members to learn

Diagram 3: ANDI Organizational Structure

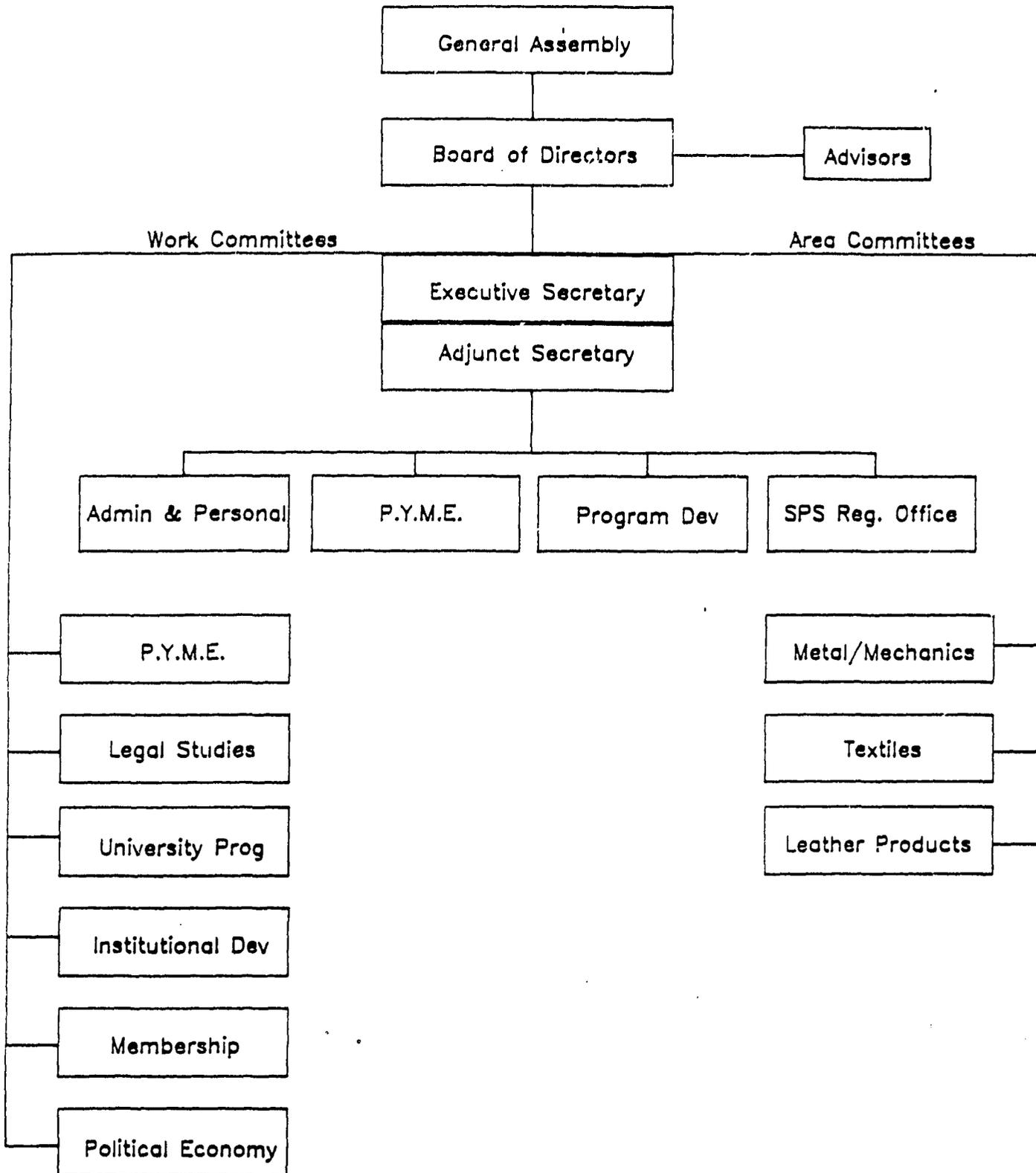
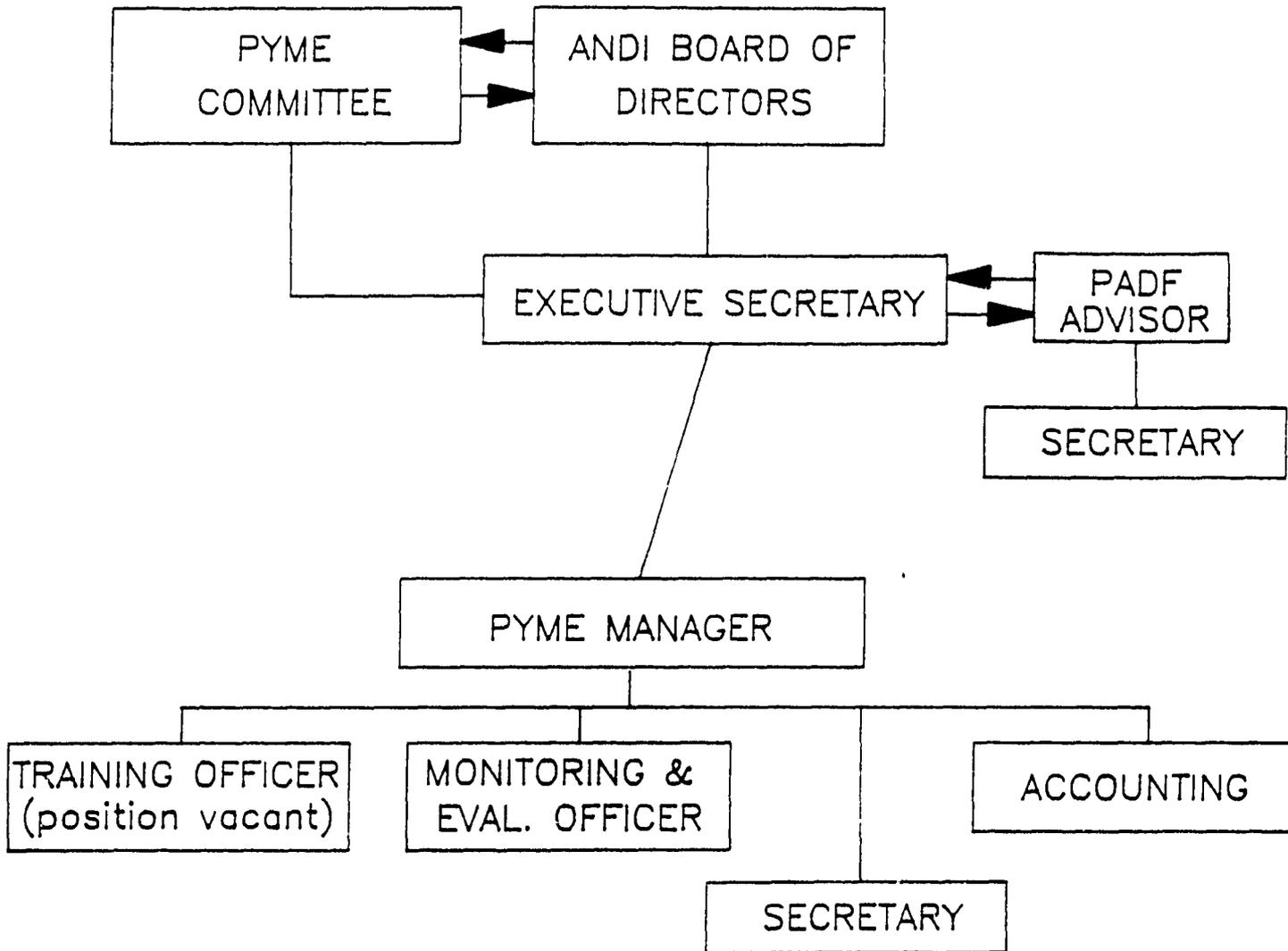


Diagram 4: PYME Program Structure



about and discuss the scope and nature of the project and what was expected of them as PYME Committee members.

The PYME Committee and the
Role of the ANDI Board

The PYME Committee has been relatively consistent since the beginning of the project. The President of ANMPI has a permanent seat on the PYME Committee, with equal voice and equal vote. The presidency of the Committee has been rotated once, to no ill effect. The former president continues his involvement in the work of the Committee and continues to support the program. The Committee does not meet at any set time. Attendance at PYME Committee meetings ranges from seven to three members, with an average of three participants at each meeting, and a core group of four.

The responsibilities of the PYME Committee members can be summarized as follows: (1) approve projects, plans, budgets, and financial statements; (2) approve hiring and firing staff; (3) define program direction; and (4) formulate program policy. While most of the PYME Committee's activity to date has focused on the approval of projects, there are signs that it will define a program strategy, analyze plans, and determine the PYME program's financial and managerial health.

The 1985 project review noted that ANDI Board members had little knowledge of or commitment to the PYME project. There have been a number of positive changes in this respect. The presence of the ANMPI representative on the PYME Committee and the attendance at a regional small business conference in Panama by one Committee member have deepened and broadened the

PYME Committee's understanding of the problems faced by the small business sector.

The PYME Committee members appear genuinely interested in and committed to the PYME program. They also have a sense of ownership and concern with the quality of the PYME program, as evidenced by their efforts to improve PYME program operations. The Committee has instituted new procedures regarding the timeliness and amount of information presented before project review sessions. In interviews, Committee members expressed concern regarding the level and extent of coverage of the PYME program based on both program priorities and the overall needs of the sector.

It would be erroneous to assume that the majority of ANDI members are interested in supporting the small business sector. There are several indications that significant changes have been made in this direction, due primarily to the influence of the PYME program.

An ANDI report to President Azcona in February 1986 indicated that the development of the SME sector should be a priority of the new government. Major recommendations by ANDI were based on experience in the PYME project. These recommendations included (1) a review of legal incentives to SMEs, (2) support of collective actions of private and governmental organizations to provide marketing, production, technical, and financial assistance to the SME sector, and (3) support of guarantee funds and credit lines that provide long-term loans at low interest rates.

ANDI has undertaken promotional efforts with private banks to encourage lending to SMEs. It has admitted the President of ANMPI to the Board of Directors of ANDI (voice

but no vote). ANDI recommended that CONSULPLAN consider a special chapter in its current plan for small and medium-sized industries.

In response to a fire that destroyed a carpentry shop, ANDI established an emergency loan fund open to all industries in similar situations. Each ANDI member will contribute L.3,000 to establish this fund.

ANDI continues to show interest in discussing joint ventures between large and small industries. Many larger firms have begun to export as a result of the advantages offered by the CBI. Industries are seeking to expand their export capacity without sinking large amounts of capital into fixed investment. The potential clearly exists for large industries to explore joint ventures with small businesses. Several PYME Committee members have expressed interest in investigating joint ventures with small businesses. Whether these ventures take the form of contracts for supplies and services, investment of risk capital, equity shares in the new activity, or a combination of these methods depends on further analysis of the issue and how it could best be developed in Honduras.

Role of ANDI Executive Secretary

The Executive Secretary of ANDI has demonstrated a commitment to PYME program support. The Executive Secretary represented the PYME program and ANDI at two regional small business conferences. He also initiated communications with BANHCASA, a private commercial bank, regarding its small business credit line. According to the PYME Manager, the Executive Secretary reviews and approves program and staff work plans on a quarterly basis. According to the PADF

Advisor, the Executive Secretary provides excellent technical oversight to the program.

Although the interest and involvement of ANDI's Executive Secretary in the PYME program is commendable and has certainly bolstered program progress, it is appropriate to question the amount of time the Executive Secretary devotes to program technical issues, planning, and staff management issues. These generally fall within a program manager's responsibility. The scope and detailed nature of the Executive Secretary's support of the PYME program indicates a weakness in program management, which has contributed to the increasing centralization of program decisionmaking and a decreasing delegation of authority. If these two trends continue, they are likely to inhibit program growth. The Executive Secretary's support of the PYME program should consist of high level negotiations and promotional efforts in the banking and industrial communities, rather than activities which are clearly the responsibility of program management.

Program Management

The original SBD project design anticipated that extraordinary managerial talents would be required of the Program Manager for the complete success of the SBD project. Unfortunately, this assumption has proven valid.

The major weakness in PYME program management is a narrow task orientation. The crucial elements for good program management, such as vision, managerial initiative (troubleshooting and creativity), and planning, are missing. The self-audit described it best: management embraces an approach

of "putting out fires." Program management tends to see its own strengths as technical rather than managerial.

"Task orientation" is a classic management dilemma that can become a serious bottleneck to organizational performance. Some of the major consequences of this type of management are found currently in the PYME program:

- . Management information is collected to prove specific points or for the sake of collecting information rather than to indicate progress and problems, form a basis for analysis, and use the results to improve the program operations.
- . There is no vision of what the organization can do or become. Time is devoted to developing activities without a sense of their importance.
- . There is no time for new initiatives or creative responses to problems.
- . Important organizational deadlines are missed because time is used to track details rather than assess the big picture.
- . Staff is harried, anxious, and overworked, resulting in low morale.

Program management is a crucial concern to staff and PYME Committee members. This concern was expressed in interviews, reports, and a PYME program "self-audit" conducted in September 1986 by PYME staff and Committee members. By identifying difficult problems in a straightforward manner, the program is on the way to corrective action. PYME should be commended for the foresight and integrity to conduct such a rigorous and honest "self-audit" that can only improve program operations.

Administrative Performance

For the past two years, the PYME program has operated considerably under budget and at high administrative cost. During the first year of operation (1984-85), the PYME program was approximately 65 percent under budget. In fiscal year 1985-86, the program was 4 percent under budget. Had the program not reimbursed interest funds to FIA, the program would have been 26 percent under its budgeted level.

To date, AID has calculated the percentage of PYME's administrative costs per program, based on the amount of grant funds disbursed by the PYME program, not the amount of funds obligated by grant agreements between PYME and the management assistance organizations. While the former method is generally appropriate to determine administrative costs for operating programs and loan funds, it may not present the most accurate picture of the administrative costs of a grant-making operation. Grant disbursements generally fall outside the period in which the commitment is made and the greatest administrative costs accrue. It is reasonable to present both methods of administrative cost calculation for comparison (see Table 11).

Administrative performance can be summarized as follows.

The percentage of administrative costs has decreased from 92 percent in 1984-85 to 30 percent in 1985-86, a 39 percent average over the two-year period. If the percentage of administrative costs is based on obligated rather than disbursed funds, the percentage of administrative costs for 1985-86 decreases to 21 percent for the two-year period.

Table 11. PYME Program Uses of Funds by Program Area:
 October 1984 - September 1985 &
 October 1985 - September 1986

	1984-85		1985-86		Total	
	Amount (lempiras)	Percent	Amount (lempiras)	Percent	Amount (lempiras)	Percent
<u>Obligated and approved funds</u>						
Support to NGOs ^a (projects)	10,025.00	8	588,434.00	58	598,459.00	53
TA to FIA clients/ generate clients	-0-		168,583.00	17	168,583.00	15
Training/conference	-0-		40,240.00	4	40,240.00	3
Subtotal, program	10,025.00	8	797,257.00	79	807,282.00	71
Administrative costs	177,600.00	92	211,579.00	21	329,179.00	29
TOTAL	127,625.00	100	1,008,836.00	100	1,136,461.00	100
<u>Disbursed funds</u>						
Support to NGOs (projects)	10,025.00	8	342,713.00		352,738.00	
TA to FIA clients/ generate clients	-0-		121,721.00		121,721.00	
Training/conference	-0-		39,096.00		39,096.00	
Subtotal, program	10,025.00	8	503,530.00	70	513,555.00	61
Administrative	177,600.00	92	211,579.00	30	329,179.00	39
TOTAL	127,625.00	100	715,109.00	100	844,734.00	100

Note: Includes October 1986 administrative costs (L3,371) and program costs (L11,946).

a. Management assistance organizations.

Source: PYME Program Budget/Financial Statement October 1984-September 1986.

The costs of the PADF Advisor have not been calculated into the administrative costs of the program. Adding these increases administrative costs to 30 percent, if calculated on obligated program costs, and 43 percent if calculated on disbursed program costs for the 1985-86 fiscal year.

During 1985-86, 20 projects were approved in the amount of L.880,540. Given current staff levels and the division of responsibilities, it is reasonable to expect that PYME staff will develop only a few more projects each year, perhaps with higher budgets. Direct program costs are likely to increase, while administrative costs are likely to remain the same.

Preliminary comments from the AID Auditor indicate that (1) the PYME program incorporates a good financial and administrative systems control, and (2) that the program accountant is well qualified in her field. Recommendations will be made on minor financial and administrative matters. The PYME program has followed the six recommendations made in the last AID audit, except for one where the difficulty may have been caused by a misinterpretation of wording.

Financial Viability

The PYME program may not be able to maintain self-sufficiency. The spread offered the PYME program by the Central Bank discount rate to FIA has decreased from 10.25 percent to 8.25 percent. FIA's current portfolio size does not generate enough income to cover all of the PYME program's costs. The initiation of FIA's own technical assistance unit and pressures to reduce the on-lending interest rate to borrowers could further decrease FIA-generated income for the PYME program. Income generated from training courses is negligible (L.1,390 in 1985-86) and is likely to remain so.

No PYME services can realistically be developed into financially self-supporting activities. Continued grant funding appears to be the only appropriate and realistic option if PYME is to continue its work.

To date, ANDI/PYME has not yet explored alternative sources of funding. Some donors have been identified, but none have been approached to assess the likelihood of providing future program support.

Relations with Participating
Organizations and Their Role
in Decisionmaking

ANDI's poor image vis-a-vis the small business community has undergone a dramatic change. ANDI has cultivated ANMPI and responded positively to ANMPI's requests to become involved in the organization. ANMPI now has access not only to the PYME program but to ANDI's broader organizational structure as well. Businesses have a certain natural affinity, regardless of size, and both ANDI and ANMPI have put a great deal of effort into developing their current relationship. In contrast, most organizations within the Honduran PVO community that manage PYME-funded programs suspect the motivation of large industrialists and an organization developed to lobby on their behalf. Nonetheless, they have worked with PYME.

Access to PYME decisionmaking comparable to ANMPI's is unlikely to be available to other management assistance organizations. This may not be desirable in any case; the organizations would be intimately concerned with each other's management and fund allocation.

To some extent, PYME Committee members have begun to appreciate the work of the PVO community through a review of submitted projects. However, the gap between the PVO and business community will be difficult to span. Closer collaboration between PYME program staff and management assistance organization staff should be encouraged before another set of decisionmakers is foisted on the organization. The PYME Committee should investigate the areas in which PVOs and ANDI can collaborate.

PADF Advisor

The PADF Advisor arrived in Honduras in March 1985 and will complete his two-year contract in the spring of 1987. The long-term technical assistance component was designed without the benefit of the host organization's participation. ANDI has been excluded from the decisionmaking process regarding (1) whether to have outside technical assistance, (2) the selection of the technical assistance provider organization, and (3) the content of the technical assistance to be provided.

There was no written job description for the PADF Advisor prior to his arrival in Honduras. This was later remedied as a result of the March 1985 project review. Because the Advisor's contract is with AID and he is not paid by ANDI, he is not clearly accountable and responsible to ANDI. This initially led to some confusion regarding the Advisor's role and responsibilities. Although these problems seem to have been resolved, the PADF Advisor is still more closely identified with AID than ANDI by the PYME Manager and some Committee members.

In general, problems of role definition, responsibility, and accountability of outside technical advisors to a local NGO are not uncommon. An advisor is often more closely identified with an international technical assistance organization or funding agency. As a consequence, host organizations often resist the work of the advisor, and technical assistance is not used to its fullest potential.

Certain provisions can prevent or limit these problems of accountability and responsibility. They include (1) involving the NGO in the identification and analysis of technical assistance; (2) involving the NGO in writing the job descriptions and reviewing applications of position candidates; (3) finalizing a local contract between the advisor and the host organization; and (4) providing for some in-country costs to be paid directly by the host organization.

Within ANDI, the initial problems of role clarification were compounded by the resignation of the first PYME Program Manager. Acting as Program Manager during the 1½-month interim, the PADF Advisor provided needed program continuity. However, this put the Advisor in a direct management position. The tendency for an advisor to relinquish an advisory position in favor of a more active position is also common. The advisor takes on permanent responsibilities in response to unfilled program staff positions or gaps in staff capabilities. This crossover from an advisory to a managerial position increases the NGO's dependency on outside technical assistance. It also decreases local program staff's potential to widen responsibilities and broaden professional capabilities. In the case of ANDI/PYME, the situation was heightened by the recruitment of a new Program Manager who had underdeveloped managerial skills and a technical background.

The PADF Advisor has contributed to the initiation, progress, and systems development of each of PYME's four program areas. According to PYME program staff, the Advisor has contributed most to project development, proposal preparation, and evaluation. These are the areas of PYME's strongest systems and greatest accomplishments. PYME staff also value the PADF Advisor's contributions to training and training strategy.

The PADF Advisor's open and frank assessment of the current Program Manager's capabilities has created conflicts within the organization and complicated the relationship between the Advisor and the Program Manager. This conflict has heightened awareness of managerial problems, which has spurred the organization to take corrective action. Since non-profit organizations generally tolerate weak management until it reaches crisis proportions, having forced this issue may be one of the PADF Advisor's greatest contributions to ANDI's organizational development. This contribution, however, commanded a high price.

During the time remaining on the Advisor's contract, PYME can profit from his skills in developing discrete projects, including: (1) completing PYME evaluation systems and evaluation training, (2) identifying future sources of funding, and (3) investigating a Honduran strategy for PVO/big business/small business linkages based on the experience of the PYME program and PADF-assisted projects in Honduras and other countries. An assessment of the time required to implement these and other tasks that may be deemed important should be made by the PYME Committee, staff, and the Advisor.

Beneficiary Profile

FIA Clients

In Honduras, small enterprises are defined as firms with total assets of L.10,000 to L.220,000 and five to 20 employees. Medium-sized firms have total assets of L.250,000 to 2.0 million and employ 20 to 100 persons. Under these definitions, FIA has financed exactly 50 percent small and medium enterprises; 56 percent small if the first 10 loan approvals are disregarded (to show a time trend). Forty percent of the 35 loans supported new enterprises, rather than established firms, and 71 percent of these loans financed small ventures.

Nearly 60 percent of FIA's loan portfolio was approved to finance working capital, the category of financing most difficult for small enterprises to obtain from the formal banking sector. Table 12 summarizes FIA's loan size categories. The first ranking loan size is under L.50,000, followed by the largest loan size of over L.200,000.

PYME Program Clients

Of the 14 organizations that received grant funding from PYME, 20 percent benefit SMEs, while approximately 80 percent benefit mainly micro entrepreneurs. To date, approximately 43 percent of the grants portfolio has gone to management assistance organizations benefitting mainly small business, while 57 percent has gone to organizations that benefit mainly micro entrepreneurs.

PYME program staff do not appear particularly conscious of gender-related factors that affect women entrepreneurs'

Table 12. FIA's Portfolio Loan Size Categories

Category (lempiras)	Number of loans	Percent of total	Rank
50,000 or less	11	31	1*
50,000 to under 100,000	6	17	4
100,000 to under 200,000	8	23	3
Over 200,000	<u>10</u>	<u>29</u>	2*
	35	100	

Note: The first ranking loan size is under L. 50,000 followed by the largest loan size of over L. 200,000. Nearly 60 percent of the approved loan amount was utilized for working capital, the category of financing most difficult for small enterprises to obtain from the formal banking sector.

access to technical and financial resources. However, approximately 40 percent of grant-financed organizations count women entrepreneurs as their main client focus. Because PYME program data are not disaggregated by sex, it is difficult to determine the extent that women entrepreneurs are benefitting from PYME-supported programs.

Socioeconomic Impact Attributable
to Project Support

Since improved performance of SMEs is the primary goal of most small and medium-scale enterprise support projects, it is important to know if client enterprises have improved their performance and whether the change, if any, can be attributed to the project.

In addition to determining standard income and employment impacts attributable to the project support, the USAID/H Mission expressed interest in obtaining profitability information on the enterprises supported by FIA. While the financial statements of these enterprises use inconsistent reporting formats and inadequate notes to explain specific entries, it is impressive that FIA has computer files on all of its clients' historic, current, and projected financial statements.

Work is underway to standardize accounts reporting (profit and loss and balance sheets) and expand the use of computerized investment planning and profitability reports. This will enable FIA to provide a sensitivity analysis for all of its clients. Data are not yet sufficient to provide a valid survey of economic impact, since most FIA loans were disbursed fairly recently.

Financial Viability of the
FIA-Financed Enterprises

Financial ratios on seven of the first ten companies to receive credit from FIA are presented in Table 13. Of the remaining three companies, one went bankrupt and two presented financial statements with incomplete or limited data (balance sheets and profit and loss statements that did not cover similar time periods), which precluded a reliable examination of company performance or profitability.

Basic financial ratios were determined, including indicators of company short-term liquidity and long-term leverage positions, by utilizing historic, current, and projected financial statement entries. Profitability was examined by calculating (1) the profit margin on sales before taxes, and (2) the return on net worth, or profits on taxes as a proportion of equity. The financial ratios followed standard principles of analysis. Client enterprises were compared with U.S. industry averages only as an approximate measure of an enterprise's financial viability.

Current Ratio/Company Leverage

The seven companies reported in Table 13 seem able to cover their short-term liabilities with liquid assets, but only three (Erika, Fibra, and Madetex) stand out with comfortable margins well above the industry average of 2.5. Note that Fibra financial figures are all projected figures. The company was started with an FIA loan in 1985 and its financial performance has greatly surpassed the financial projections in Table 13. Fibra is also pre-paying its loan to FIA.

Table 13. Financial Leverage and Profitability Ratios for Selected FIA Clients

Enterprise	Current ratio	Debt to total assets	Profit margin	Return on equity
			-----percent-----	
<u>Ericka</u> (furniture)				
1985: N/A	--	--	--	--
1986: projected	5.7 times	23	21	20
<u>Con. Pana.</u> (clothing)				
1985	1.44	76	14	56
1986: projected	1.81	59	18	76
<u>Fibra^a</u> (plastics)				
1985: projected	4.29	21	34	26
1986: projected	3.86	17	28	22
<u>Guantesa^a</u> (sports articles)				
1985	1.10	41	07	21
1986: Jan.-Sept.	1.63	34	13	29
1986: projected	5.62	17	21	11
<u>Escobas</u> (brooms)				
1984	1.62	48	10	26
1985	1.87	56	06	13
1986: projected	4.13	40	11	29
<u>Madetex^a</u> (furniture)				
1985	2.29	62	-04	neg.
1986: Jan.-June	2.47	71	-05	neg.
1986: projected	5.71	59	20	45
<u>Papeleria^a</u> (printing)				
1984	2.24	50	12	52
1985	1.14	47	02	04
1986: Jan.-March	1.08	51	08	03

a. Firms benefitting from PYME-financed technical assistance.

Note: A problem in this financial review is that the financial records of the enterprises tend to be incomplete. In certain cases, the records cover only a few months of the year. In one instance (see Erika), a balance sheet for 1985 was not available. The records also reveal that the accounting procedures themselves tend to be inconsistent.

Commercial banks in Honduras require a 3:1 to 5:1 collateral-to-loan ratio for securing short-term loans. FIA has a mandate to approve or reject loan applications on the basis of market and financial viability, rather than substantial collateral and liquid guarantee requirements. This is demonstrated in the current ratios in Table 13.

Total debt-to-total asset ratios are more than 1:2, or 50 percent. The industry average in the U.S. is only 33 percent. A highly leveraged debt-to-total assets position is considered good business practice by many, if not most, businesses today. On the other hand, many financial institutions wince at "these risky, highly leveraged companies." The tendency is to improve the debt-to-total assets ratio as reflected in the projected figures for 1986.

Enterprise Profitability

With the cost of money to the entrepreneurs averaging 21 percent, and inflation estimated at approximately 9-10 percent in 1985 and 1986, all of the enterprises listed in Table 13 demonstrate good profit margins. Profit margins -- profits before taxes (operating profits less financial charges), as a proportion of sales, at levels above 10 percent -- are considered better than average.

Utilizing a capitalization rate of 15 percent in the Honduran context, six of the seven companies demonstrate return on equity ratios at levels in excess of 20 percent. Note that Madetex, a furniture manufacturer with a negative return in equity in 1985, acquired contracts in 1986 for export to the United States. It is anticipated that by the end of 1986 more than 60 percent of its production will be exported to the U.S. The printing company, Papeleria, on the

other hand, has had large domestic orders cancelled recently and is undertaking a more aggressive marketing campaign to turn around its business locally.

Fixed asset investments (approximately 40 percent of all loans) carry a grace period of up to two years; the working capital portion has up to a one-year grace period. None of the enterprises are paying back the principal of the fixed asset portion of their loans. All of the enterprises are fully amortizing the working capital portion of their credit. As mentioned earlier, Fibra is pre-paying on the total of its L.30,000 loan.

Preliminary calculations indicate that most of the enterprises should experience positive rates of economic return. The prices that SMEs pay for unskilled labor and domestic inputs are likely to be much higher than the "shadow rates" (their real value), and their economic return will be higher than the financial rate. They earn a proportionately small premium on imports. One of the enterprises began exporting in 1986 (Madetex -- furniture). Another firm (Con. Pana. -- clothing), has established a U.S. client and plans to export 25 percent of its total sales in 1987. Here again, prices, and thus economic return, will be understated by profits.

Economic Impact of FIA- Financed Enterprises

The primary inputs of this impact analysis are the data of ten enterprises studied above.

Income

Through credit and management assistance from the SBD Project, beneficiaries generally improve their incomes in real terms: they usually start new enterprises or expand existing ones. All five entrepreneurs interviewed claimed that they could not have expanded or started their businesses without SBD financial and management support. The five entrepreneurs visited strongly endorsed FIA and the project, although they objected to the high cost of FIA money and to the time consumed in obtaining additional credit based on signed sales contracts for their incremental sales.

Most employees of the enterprises visited earned minimum wages. However, all had the opportunity to work overtime and earned total salaries considerably higher than the minimum wage. No sample surveys were administered to ascertain overall income impact among the SME employees.

Changes in Enterprise Asset Base

Of the L1.4 million in loans extended to the first ten enterprises within the FIA portfolio, 43 percent, or nearly L.618,000, was utilized to purchase machinery and equipment or otherwise add to the asset base of the firm. In terms of total assets before the loans and afterwards, fixed assets were increased by 16 percent.

Employment

Employment generation is the primary focus for many supporters of small and medium enterprise development. It was a primary objective of the SBD project when it was initiated

in 1984. FIA projected that 140 new jobs would be provided by the ten enterprises studied (see Table 14). In the firms visited by the evaluation team, employment exceeded the projected figure.

Over 50 percent of the newly employed were determined to be women. This compares favorably to 33 percent in the start-up employment figures. Employers were enthusiastic about women's participation in the labor force. According to the entrepreneurs, women's absenteeism is rare to non-existent, their learning level is rapid, their productivity is extremely high, and their level of morale and general enthusiasm is high.

One of the enterprises visited, Maprima, exports wood products to the U.S., due to an expansion loan from FIA. Maprima is experimenting with employing women in non-traditional roles in its plant. The women operate heavy machinery and equipment and, to the delight of one of the company owners and shop manager (also a woman), accidents, once frequent, have almost ceased to occur.

Maprima originally expected to increase its work force by eight; it has actually expanded its work force by 45. Of these new employees, 35 are women heads of households who had never been employed before working at Maprima. All of the new employees earn minimum wage. Because the plant operates 24 hours a day, seven days a week, nearly all employees work overtime (paid on a piecework basis) and substantially increase their take-home pay.

USAID/H deserves recognition for having hired a consultant to help "sensitize" the project design and the participating institutions to the issue of gender. As a result, the

Table 14. Economic Characteristics of Ten FIA Clients

Name	Product	Credit amount (lempiras)	Employment		Project value added (lempiras)
			Actual	New	
Guantesa ^a	Sports art.	100,000	28	18	400,000
Dida ^a	Furniture	90,000	33	7	288,000
Erika ^{a,b}	Furniture	55,000	18	6	140,000
Fibra ^a	Plastic products	30,000	0	7	113,000
Indescosa	Brooms	250,000	28	16	242,000
Pradi	Jams/jellies	147,400	0	12	162,000
Con. Pana.	Clothing	250,000	34	52	400,000
Papeler ^a	Printing	75,000	15	0	150,000
Tiger ^a	Exporter	250,000	0	0	Broke
Madetex ^a	Furniture	181,000	55	22	202,000
Totals		1,428,400	211	140	2,097,000

Note: Value added figures are projected using USAID/H approved methodology. Zero actual employment (Fibra, Pradi, and Tiger) are new enterprises.

a. Indicates PYME program financed technical assistance.

b. Visited by the consultant.

Source: FIA computer printout.

SBD project is much more responsive to the particular needs of, as an example, women heads of households (Otero, "A Review of Project Designs with Special Emphasis on Gender Considerations," SBD Project, March 1985).

By examining the total loan portfolio of the first ten companies that received FIA credit and comparing this figure to new employment generated, as shown in Table 12, one obtains the cost per new job as L.10,202 (US\$5,101). This figure compares favorably with World Bank, Inter-American Development Bank, and USAID Mission costs for new industry jobs throughout the hemisphere, which average between US\$5,000 and 10,000 per new job. (All figures are based on costs of new jobs by credit extended.) Unemployment estimates and skill levels of workers were determined by the evaluation team through site visits to FIA clients and discussions with plant management and FIA staff. According to these estimates, 60 percent of all new employment was comprised of previously unskilled and unemployed labor.

Impact of the PYME Program

Since the program has been operating for only 16 months, little observable impact is expected. However, there are early indications that the program can affect employment, enterprise stability, and institutional leverage and access for the SME sector as a whole.

Employment Generation and Strengthening of the Enterprise

The PYME program status report of August 1986 indicates that 891 jobs have been generated through grant financing and technical assistance. However, it is difficult to determine

(1) whether new jobs were created for previously unskilled and unemployed workers and (2) if management assistance organizations have calculated their employment generation figures with any consistency.

Reports and interviews with clients indicate that technical assistance and training have made a significant difference in the operation of SMEs. In turn, this has increased the employment of previously unemployed and unskilled workers. For example, two entrepreneurs participated in a course in shoe production technology by FEHCIL and IESC (a program financed by PYME). Both indicated that they had instituted changes in their enterprises based on approximately 45 percent of the course content. Conditions such as lack of space, equipment, and the layout of the factory prohibited adoption of other course principles. According to the entrepreneurs, production in both shops increased, on the average, by 80 percent, while costs of raw material and labor per unit produced decreased by 30-50 percent. These two enterprises, both with secure sales outlets, have generated 15 new jobs for previously unemployed and unskilled young male workers. These workers are trained on the job.

There are other indications that technical assistance and training have improved the financial health of the firm, even where increases in employment were not noted. For example, through an ANMPI project, an average of six enterprises improved operations in areas such as inventory control, accounts receivable, liquidity positions, and sales.

Institution Leverage and Access

Individual ANDI members, and ANDI as an organization, carry a great deal of political clout and economic leverage.

They have direct access to political decisionmakers, large private sector concerns, and commercial banks. This access is not generally enjoyed by PVOs and certainly not by small and medium-sized enterprises. Placing the PYME project within ANDI has had some unanticipated positive effects. Through ANMPI participation in the PYME program and on the Board of ANDI, concerns of small business have been integrated into ANDI's institutional agenda. ANDI has provided the small business sector with an institutional forum where its needs may be raised and problems addressed.

Measuring the Economic Impact
of the SBD Project

Measuring the economic impact of enterprise promotion programs like FIA and PYME requires several steps. First, measures of the improved state of these enterprises must be taken. Second, it must be proved that the improvements are attributable to project inputs and are a net addition to what would otherwise have occurred.

Two measures of improvement will be considered in this review:

1. Profits, or the financial rate of return, are the sine qua non for the survival of the enterprise. Profits are the incentive to which the entrepreneur responds. To the extent profits are not concealed to avoid income tax or other liability, they are usually reported clearly and regularly on balance sheets. In addition, profit is a concept familiar to even the least sophisticated accountants.
2. Value added is calculated through a cost-benefit analysis commonly used to evaluate public expenditure. It measures the net value they add to GDP (national income).

Using standard value added calculations -- gross output less purchased inputs from other firms -- FIA management projected nearly L.2.1 million in value added in the first year of operations for the ten clients analyzed above, and nearly L.5.0 million for the overall portfolio of 35 clients.

Beyond value added, benefits are also generated for enterprises and individuals outside the project through backward and forward linkages within the local economy. Among the first ten enterprises to receive FIA credit, 70 percent of inputs and nearly 100 percent of production output, or sales, are derived from, or sold to, local markets. These purchases (backward linkages) and sales (forward linkages) are considered benefits to the local economy; goods and services are new production within the country, rather than sales diverted from other customers.

Eventually, the data collected by FIA should permit them to calculate all of these benefits and compare them with the total capital employed in the enterprise. This will measure the efficiency with which an enterprise is operated. Profit or financial return may also be calculated as percentage of the owner's equity to determine the enterprise's profitability from the owner's point of view.

FIA's client enterprises have only recently begun operation, and it may be premature to make any assertions. In general, performance has been running ahead of projections, and profit is relatively high, as noted above. The rate of economic return is likely to be proportionately higher than for larger firms with the same level of profitability because larger firms use proportionately more unskilled labor and fewer imported inputs.

The Mission expressed interest in the nature of the new jobs created -- whether they could be classified as "job additionality" (net new jobs to the economy) or "job sustained or transferred" (employed persons shifting to another job).

Since half the respondents report that their enterprises/expansions would not have been launched in the absence of the FIA program, we can perhaps "attribute" the product to the program in that sense.

III. CONCLUSIONS AND RECOMMENDATIONS

The SBD Project Overall Conclusions

The emergence of two independent entities, with two distinct client populations, calls into question the rationale for continuing to support the SBD Project as currently implemented. The forced marriage of interests between the two institutions means that neither will serve its originally targeted client population with a full complement of financial and technical services as intended.

FIA clients tend to be medium-sized and larger small-sized enterprises, while the clients of the organizations supported by the PYME program tend to be small and micro enterprises. Both FIA and PYME reach the target population in the SME sector. However, their clients generally fall on opposite ends of the spectrum.

The two institutions need not be programatically and financially tied to provide needed support to micro, small, and medium-sized enterprises within the sector.

Technical assistance for FIA clients has been only marginally successful, with the PYME program working with a number of NGOs to improve their ability to deliver services to

SMEs. The orientation of the PYME program work has been heavily weighted in favor of micro and small enterprise support needs, too small to fit FIA's small to medium-sized business clientele. With the initiation of FIA's own technical assistance department, there is little reason to expect a continuation of a direct relationship between FIA and PYME. FIA can contract those technical services, such as feasibility studies, which are best provided outside of FIA, as PYME has done in the past.

At this point, there is no need for an intermediary organization such as PYME to become involved in the operation. In the past, this functional relationship between PYME and FIA led to an additional bureaucratic layering and an unnecessarily burdensome coordination and management task for both organizations. In addition, FIA is in a better position to evaluate the services of its own staff and/or independent contractors and hold them accountable for services rendered.

The dual objectives of FIA are: (1) to work toward economic development, and (2) to make a profit in support of medium-sized and small industry. The objective of the ANDI/PYME program is to improve the quality and coverage of management assistance organizations' services in support of the SME sector. Achieving these objectives is a complex and lengthy proposition. By devoting resources to improving the service delivery capability of each institution and area of activity, ANDI/PYME and FIA can build on their strengths in providing assistance to the small business sector as a whole.

The technical assistance and credit needs of women entrepreneurs were not taken into account during the project design phase. Many design components, such as the priority

given to medium-sized enterprises and choice of management assistance organizations, inhibited women's participation in the project. During the project implementation phase, developments occurred which enhanced the project's ability to reach women, such as PYME's support of organizations that benefit women entrepreneurs. While it is unlikely that FIA will benefit many women entrepreneurs directly as borrowers, FIA is enabling larger firms to generate more employment for the female labor force. The PYME program is already providing access to credit and technical assistance for women entrepreneurs, and as it expands into the rural industrial sector, it is likely to do more in that area.

During the project implementation phase, USAID/H support has been effective and appropriate.

Policy Conclusion

Given the importance of monetary, fiscal, and export regime policy reform, USAID/H's development policy stresses exports. However, the Mission's initiative in designing an innovative small and micro development project reflects its commitment to the development of the domestic economy as part of its integrated approach to development.

Though circumstances vary from country to country, SME's greatest potential market lies at home. In Honduras, 89 percent of small enterprises produce primarily for direct retail customers (Liedholm and Mead, 1986). These customers have, in most countries, a much higher income elasticity for the goods of small rather than large-scale industry. Export demand is rarely important for them. A far more common source

of growth has been dynamic backward and forward linkages with agriculture.

Recommendations for USAID

1. Extend both components of the SBD Project, but with certain modifications in design. These should be based on the difference between those FIA activities that can become financially self-sustaining operations, and the PYME program activities that are developmental in nature and should be financed from development assistance funds.
2. Continue to support FIA with counterpart funds, at inter-bank, real costs of money, consistent with AID policy of non-price rationing.
3. Continue to support the ANDI/PYME program with GOH counterpart funds in the form of development assistance grants.
4. Support the movement of FIA away from relying on ANDI/PYME-financed technical assistance.
5. Assist FIA in the development of its own technical assistance unit.
6. Complete the separation of ANDI and FIA by removing ANDI's financing via FIA's interest rate differential. Channel that differential back to FIA to be used in the following ways:

. To cover costs of FIA's technical assistance unit

- . To cover the costs of FIA's hiring outside technical assistance for project analysis and technical support
 - . To reduce the final cost of money to FIA clients
 - . To investigate the feasibility of opening a window dedicated to small business and production enterprises
7. Use USAID/H's influence as a major donor in Honduras to rally both public and private sector support behind FIA, ANDI, and the overall SBD Project.
8. Relinquish USAID/H's direct administrative and managerial role in the SBD Project in favor of a Board of Directors role to provide more support on the broader issues of program direction, management, and making linkages within the sector.
9. Pursue a balanced economic development approach in its support of private enterprise; encourage the development of local economically and financially sound private enterprises that operate in the domestic free market, as well as export industries, that generate employment; and provide for a greater measure of economic and social stability.

FIA Conclusions

FIA is a sound financial institution which has operated in a financially responsible and conservative manner. FIA has performed well considering the complexity of its goals, the difficulty of the local economic climate, and some inappropriate financial and decisionmaking structures.

FIA management is sound. After working out important project design and start-up problems, FIA is operating efficiently with a reasonably healthy, albeit limited, portfolio.

FIA needs to expand its portfolio and coverage of small industry, especially outside Tegucigalpa and San Pedro Sula. As an example, FIA is supporting only one production cooperative, and needs to be apprised of the economic and financial viability of the numerous rural cooperatives. This is an area in which FIA support is weak.

The original feasibility study for FIA provided neither information on the supply of money for SMEs nor information on the demand for financing, especially its elasticity vis-a-vis the interest rate.

FIA's interest rate policy and lending to SMEs is proving to be incompatible. The cost of borrowing, above commercial interest rates, has become a major obstacle for present, as well as potential, clients.

Turnaround time for decisions has become excessive and has discouraged potential clients.

Arrearage on interest payments and capital, while a concern to FIA, is considered acceptable by Honduran standards. Increasing arrearage is more indicative of FIA's lax policy on loan recuperation than the financial viability of the firms studied.

FIA has not developed an operational policy for writing off bad debt.

FIA clients do not prepare consistent or standard financial statement for loan applications.

Recommendations for FIA

1. Undertake a definitive market analysis to determine the market segment and appropriate niche for FIA in support of SMEs.
2. Develop joint projects with FIDE.
3. Develop the originally planned co-financing with FIA shareholder banks.
4. Examine the timing and appropriate form for widening the ownership of FIA.
5. Change interest rates to reflect FIA's cost of money and on-lend at competitive rates.
6. Vest final authority for approval of loans of L.100,000 or less in FIA management.
7. Develop loan performance (recovery) incentives and disincentives to decrease current loan arrearage rates.
8. Develop regular weekly reporting of necessary loan performance data.
9. Establish an operational policy and procedures for writing off bad debt.

10. Standardize financial statement requirements for all current and future FIA clients to provide appropriate data for accurate financial internal rate of return analyses.

11. Add data on employment, material purchase, and sales to the current client data bank to complete the necessary information required for economic rate of return analyses.

PYME Program Conclusions

The PYME program has enabled several organizations to provide assistance to SMEs to begin new services and improve existing ones. While perhaps originally not the best choice to undertake the coordination of the BAS, ANDI has shown a lot of progress and goodwill toward the small business sector at both the program and institutional level. ANDI can provide political and economic leverage to the sector and there are indications that it has already begun to do this. Because of experience gained in implementing the project, ANDI is probably the best organization to continue supporting the PYME program.

There appears to be a great deal of untapped potential in big business/small business joint ventures and support networks. ANDI is probably the best organization to carry out this type of activity.

Grants Program

PYME has a consistently good reputation as an efficient and credible funder of management assistance organizations' projects that benefit the small business sector. PYME has

been selective in providing financing in a disinterested manner to a number of organizations that have good reputations working with diverse SME client groups.

Project Management

Project management is the major bottleneck to further program progress and new organizational initiatives. Staff at the officer level seem competent and well-informed.

The PADF Advisor has contributed to the development of the ANDI/PYME program and support systems.

Administrative and programmatic systems that are crucial to the development of the program are in place and operational. Areas that will need continued outside support are management and coordination within the NGO community. Short-term technical assistance consultancies are appropriate to fill these needs.

Training Program

The most effective training and follow-up to SMEs can be provided by the PVO management assistance organizations. PVOs know the educational level of their clients, have mechanisms in place to assess clients' needs, and, through extension agents, can ensure a higher quality of follow-up. While INFOP courses have been reviewed as beneficial by a number of organizations, generally, INFOP methodology and course content have been criticized as inappropriate and designed without a clear audience in mind.

Technical Assistance

Outside of FIA, PYME can be useful in its role as an indirect provider of technical assistance to small independent firms and cooperatives that are in a position to receive credit from commercial or government banks and lending agencies. This, however, is best coordinated through joint efforts with those organizations that have clients who may be ready to take advantage of commercial lending operations.

Recommendations for PYME

1. Institute a slow and stable growth policy, restricting activities to current program strengths, building on these strengths, developing program priorities that fall exclusively within the program mandate, and trimming the program to a size manageable by PYME program staff.
2. Diversify funding sources at a rate that does not jeopardize the effectiveness of the program.
3. Learn about and visit other organizations where large and small businesses have developed support networks. One program is MIMEXA in Monterrey, Mexico, developed with the support of Accion/AITEC. Other organizational resources of value are the Partners of the Americas, and the International Executive Service Corps. PADF should also have a wealth of experience in this area.
4. Initiate program manager recruitment efforts. The "self-audit" carried out by PYME in September 1986 identified the managerial and personal skills that are required of this important position.

5. Refine job descriptions to reflect the team work approach currently used by PYME. Project Officers with complementary technical skills acting as a multidisciplinary team seem to support the direction of the program better.

6. Expand and update staff knowledge of development issues and concerns within the sector, specifically seminars on women in development and seminars covering the issues of technical assistance, training, and credit programs directed to the small business sector.

7. Program short-term technical assistance consultancies, perhaps through PADF, local agencies, or other international agencies that have a base in Honduras and offer short-term management assistance.

8. Re-examine the need for long-term technical assistance as the program develops and specific needs are identified.

9. Analyze what discrete projects the PADF Advisor can undertake and the time required to complete them. Some suggestions are made in the body of this report.

10. Develop mechanisms, along lines similar to the ANMPI project, to generate clients for FIA. To avoid duplicating the problems and low success rates of the ANMPI project, before project initiation it will be important for PYME to:

- . Work closely with the management assistance organizations and the lending institutions that have expressed an interest in this kind of support

- . Determine the number of firms able and willing to apply for such credit and the rates and terms they can afford
- . Identify individual sources of credit, as well as the specific procedures and documentation required by each source

11. Encourage technical assistance from one or more management assistance organizations with successful programs to those organizations that are initiating or having problems with similar programs. This type of collaboration can be developed through a number of mechanisms available to PYME, including:

- . Surveying the need among management assistance organizations for this type of support
- . Updating information on existing PVO programs that include an analysis (not merely a description) of services available, and under what terms and conditions
- . Financing small workshops with PVO staffs as instructor/participants, not only to exchange information and identify problems, but to plan joint efforts and programs, perhaps with subsequent PYME financial assistance.

12. Focus the scheduled evaluation of the INFOP courses on the importance of the PYME/INFOP agreement to supporting the small business sector and analyze whether the benefits provided by the INFOP courses are worth the time PYME devotes to

this activity. The evaluation should pay particular attention to:

- . Whether the organizations that appear to value INFOP courses can access INFOP directly
- . Whether PYME can use its grants program to provide training funds to management assistance organizations that are then in a position to select their own instructors
- . How the scholarships (planned for the future) will complement or duplicate these efforts

13. Encourage a more active role on the part of NGOs in client and staff development needs assessment, course design, and implementation.

14. Emphasize joint efforts by NGOs in initiating client and staff development programs. Specifically, PYME should explore the potential benefits of:

- . Encouraging an organization to design a course specifically for its own clientele that will later be appropriate for others
- . Providing funds for outside resources, if necessary, as in the case of the FEHCIL marketing course
- . Financing one or more organizations that have successfully designed and implemented their own courses (for clients or staff) to share these resources with other organizations, perhaps giving the courses themselves

APPENDIX A

APPENDIX A. SCOPE OF WORK

The Mission requests assistance under the ARIES contract for an evaluation of the Small Business Development Project (522-0205) beginning on or about November 15, 1986.

Background

The project was designed to increase production and employment in small- and medium-scale enterprises by developing a source of accessible financial and technical assistance for them. Under the project, a small business company (FIA) was established to provide loans to small- and medium-sized businesses which normally lack access to commercial bank credit due to high collateral requirements. FIA has a professional staff of three managing a loan portfolio of \$2.3 million with 35 borrowers. FIA's activities are complemented by technical and managerial support from a dozen organizations participating in a business assistance system coordinated by the National Association of Industries (ANDI). Pan American Development Foundation (PADF) provides a long-term technical advisor to ANDI. The project agreement was signed June 1984 and ends May 31, 1987. This evaluation will focus on the role and performance of FIA and ANDI, and their impact on project success. The report will help the Mission to decide whether to extend the project, changed or unchanged, and will assist in planning for new activities.

Specific Terms of Reference

Institutional Analysis and
Socioeconomic Impact

The key issues the evaluation must investigate in carrying out an analysis of the two implementing institutions, FIA and ANDI, are administrative and financial performance, client coverage, and sustainability.

For FIA, the evaluators will assess:

- . Administrative development and performance to date, efficiency in delivering credit to small enterprises
- . Organizational structure, coordination, and staffing
- . Decisionmaking procedures, role of the Board of Directors, and relations between management and the Board
- . Overall financial policies and past financial performance
- . Financial and administrative viability and sustainability, including a review of costs, profitability, and interest rates
- . Client profile to measure extent FIA is reaching the target group and whether credit policies are congruent with project goals
- . Outputs: number of loan applications received, loans made, amounts approved, amounts disbursed, quality of portfolio (data disaggregated by sex)

For ANDI, the evaluators will assess:

- . Administrative performance in quantitative and qualitative terms
- . Organizational structure and staffing
- . Decisionmaking procedures, role of Board of Directors, the small- and medium-sized enterprise (PYME) committee, and Executive Secretary of ANDI and their relations with project management
- . Relations with participating organizations and their role in decisionmaking
- . Financial viability and financial management
- . Training and technical assistance: curriculum design, quality of materials, promotion and outreach mechanisms, quality of trainers, and follow-up to training
- . Selection of participating organizations for consistency with the project's target group and the degree of coverage
- . Outputs: number of persons trained, number of training courses, quality of training, multiplier effect
- . Impact of long-term assistance on institutional development and current performance

The contractor will evaluate the development impact on the small enterprises assisted by the project with special attention to the financial management and technical changes within the enterprises. FIA and ANDI have sufficient data on their beneficiaries to provide the technical evaluator with quantitative information to be supplemented by not more than five interviews with FIA clients, three interviews with organizations participating in ANDI's business assistance system, and up to six interviews with technical assistance beneficiaries.

The contractor will describe the general development impact of the project on income, employment, national value added, and institutionalization, with special attention given to employment generation. In addition, the contractor must review whether the interests and role of women were taken into account in project design, whether gender-specific data is available, and whether the impact of the project on women's access to credit and technical assistance was positive or negative.

Conclusions and Recommendations

The contractor must prepare an overall assessment of the project and present the conclusions reached on its development impact.

The contractor will make specific recommendations regarding problems encountered in project design and implementation and possible remedies.

The Contractor will recommend whether future funding is merited; whether the project should be extended, modified, or continue as is; and what additional short- and long-term assistance may be needed.

The Contractor will interpret findings from a programmatic perspective, indicate what lessons have been learned from this experience, and suggest what aspects of design and implementation should be taken into account for future similar projects.

Reports

The Contractor will present preliminary findings and conclusions to AID/Washington, FIA, and ANDI in an oral briefing at the end of the field work period. The contractor's draft report must be submitted to AID/Honduras after six weeks for review of factual accuracy. The final report must be submitted by January 30, 1987. Ten (10) copies of the final evaluation report must be submitted to USAID/H in Spanish and English. The evaluation must include an executive summary, which includes the following sections:

- (1) Purpose of the evaluation
- (2) Methodology
- (3) Major findings including developmental impact
- (4) Conclusions
- (5) Lessons learned
- (6) Recommendations

Contract will require two small business development experts, one specialized in credit and financial analysis, the other in institutional analysis and training. Both must be fluent in Spanish, have solid experience in project design, implementation, and evaluation in LDCs; Master's Degree and Latin American experience preferred. We estimate that four person-weeks to draft report for a total of eight person-weeks to be divided between two team members.

Evaluation to start as soon as possible, but no later than November 15, 1986. Principal USAID contact is Margaret Membrano, Office for Private Sector Programs, telephone: 32-3120, extension 2610.

A-6.

USAID/Honduras will pouch in advance preliminary reading material (such as Project Paper) for evaluation team to Bigelow as soon as possible.

APPENDIX B

APPENDIX B. METHODOLOGY

Purpose

The purpose of this evaluation, as presented in the general terms of reference were:

1. To provide USAID/H with an objective analysis of the role and performance of FIA and ANDI and their impact on project success
2. To assist the Mission in its decision on project extension and planning new project activities

The scope of work is presented in Appendix A.

Evaluation Methodology

This evaluation was carried out in November 1986 by a two-person team contracted by Robert R. Nathan Associates, Inc. (RRNA) under the ARIES Project. The team of two small business development experts, one specialized in credit and financial analysis and one specialized in institutional analysis and training, was complemented in the field by the participation of the Accion/AITEC Regional Representative.

The methodology used in this evaluation included the following activities: (1) reviewing available documents; (2)

collecting relevant information; (3) interviewing key individuals; (4) internal team discussions on progress and analysis of data; (5) follow-up interviews with key individuals to determine the accuracy of information received, test hypotheses, and discuss preliminary findings; and (6) arriving at preliminary conclusions and recommendations based on analysis of information and a review of the project's intended purpose. Separate oral debriefing sessions with USAID/Honduras, FIA, and ANDI to present preliminary conclusions and receive feedback from each group.

The team spent two weeks in Honduras reviewing information, participating in meetings with USAID staff, and holding interviews with key individuals associated with the SBD Project. Interviews were held with (1) the FIA staff and Board; (2) the PYME program staff, Committee members; (3) the PADF Advisor; (4) FONDEI/Central Bank; (5) FIA loan clients, technical assistance recipients, training course participants; (6) staffs of three management assistance organizations receiving PYME program assistance; and (7) other NGOs collaborating with the project. A course currently being presented by one organization was attended. A complete list of interviews appears in Appendix C.

As suggested in the scope of work, questions addressed were concerned with the effectiveness of project design and implementation, how well FIA and ANDI had fulfilled their goals and objectives, how effective their management and operations have been, what has been the economic impact of the program on employment and the development of SMSEs in Honduras, and whether the interests and role of women were taken into account in the project design and implementation.

One evaluation team member focussed on the operations of FIA, and the other, the operations of ANDI and the PYME program. When time permitted, and when the team felt it would enhance their analysis of the project, both team members were present at meetings. The team met at least once a day to discuss progress, compare notes, and review findings. The report represents a joint effort by both team members.

A list of documents reviewed appears in Appendix D. In addition to these documents, written materials were obtained from ANDI and FIA regarding various aspects of their programs, administrative, and financial operations.

In addition to determining standard income and employment impacts attributable to the project support, the USAID/-Honduras Mission expressed interest in obtaining profitability information on the enterprises supported by FIA. Calculation of financial ratios followed standard methods of analysis and were developed by RRNA based on the FIA computerized information provided the evaluator.

Working in concert with one of the Mission's economists, the evaluator agreed to determine the economic rates of return, if possible. Economic prices of materials and labor were determined and the proportion of current and future export sales was estimated. Due to inconsistencies in reporting and difficulty in breaking down financial statements, it was deemed impossible to provide economic rates of return estimates; however, some comments were developed based on what data was available.

APPENDIX C

APPENDIX C. LIST OF CONTACTS

USAID/Honduras

Mr. Jack Miller - Deputy Mission Director
Mr. Bill Kaschak, DF
Ms. Mitzi Likar - Deputy Director, Private Sector Office
Ms. Margaret Membreno - Project Manager
Mr. Orlando Hernandez - PCR - AID
Mr. Danilo Cruz
Ms. Elisabeth Kvitashvili - Project Backstop Officer
Mr. Juan Butari - Economic Advisor, USAID/Honduras
Ms. Marcela de Moya - Auditor
Ms. Carolina Cuerva - Program Assistant

ANDI/PYME

PYME Committee

Sr. Jose Maria Covelo
Sr. Leonel Bendec
Sr. Felix Barahona
Sr. Felipe Peraza

PYME Staff

Sra. Maria Concepcion Lopez - Manager, PYME Program
Sra. Gladys de Enriquez - Monitoring/Evaluation Officer
Sra. Victoria Lagos - Program Accountant
Mr. Beto Brunn - PADF Advisor
Sra. Dorcas de Conzales = Executive Secretary, ANDI

Social NGOs

Sra. Maria Otero - Accion/AITEC Advisor to ASEPADE
Sra. Carla Flores Gomez - Director, Women's Bank
Sra. Nora de Martinez - FUNDAMU
- FEHCIL

Sr. Gerson David Mejia - FEHCIL Production Extension Agent
Sr. Efrain Calex - FEHCIL Production Extension Agent
Sr. Gustavo Hernandez - FEHCIL Marketing Extension Agent
Sra. Marta Mazier - FEHCIL Social Worker
Sr. Roberto Amaya - FEHCIL Administrator
Sra. Marcela Alvarez - FEHCIL Course Instructor
Sr. Rafael Cruz - ANMPI President
Sr. Manuel Herrera So - ANMPI Manager
Sr. Rolando Ramirez - ANMPI Credit Officer
Sra. Elvira Acosta - ROPRIDEH, Analysis & Follow-Up Officer
Mr. Thomas Membreno - FIDE Finance Department Director

Private Enterprise

Sr. Angel Antonio Mungia - Calzados Walter/ANMPI Source
Sr. Luis Gustavo Hernandez - Resortes de Honduras/ANMPI
Sr. Reis Hernandez - Resortes de Honduras/INGAC Source
Sr. Otilindo Rodriguez - Shoe Factory Owner/FEHCIL
Sr. Juar Ramon Zavala - Shoe Factory Owner/FEHCIL
Sr. Rene Becerra - Manager, Price Waterhouse
Mr. Erick Kaffie - Furniture Factory Owner

Banks

Central Bank

Sr. Rigoberto Pineda S. - Manager

Fondo Nacional de Desarrollo Industrial (FONDEI)

Sr. Sigfido Rivera C. - Deputy Director
Sra. Maria C. Cstejon de Shindo - Assistant to the Director

Banco CentroAmericano de Integracion Economica (BCIE)

Sr. Ramiro Irabien

Banco de Occidente

Sr. Marco Julio Cano - Manager

FICENSA

Sr. Jose Arturo Alvarado - General Manager

Banco de La Fuerza Armada

Sr. Roberto Periera - Manager

Financiera Industrial y Agropecuaria (FIA)

Sr. Wilfredo Modenessy - General Manager
Sr. Juan Torres - Credit Officer
Sr. Herberto Lopez - Director of Operations
Mr. Peter Livingston - Consultant to FIA, Computer Systems

APPENDIX D

APPENDIX D. DOCUMENTS REVIEWED

1. Project Paper, Honduras: Small Business Development (522-0205), 1983(?)
2. Draft Semi-Annual Project Report, April-September 1986
3. Review
4. Auditoria de la Gerencia del Programa PYME Analisis y Conclusiones de la Auditoria de la Gerencia del Programa PYME, Mayo-Septiembre 1986
5. Action Memorandum for The Mission Director, July 22, 1986, Project Description Amendment
6. "Supporting Small Enterprises, Orlando Hernandez, PCR-AID, June 1983
7. Maria Otero, "The Small Business Development Project," and Fundacion Nacional de Desarrollo Hondureno: A Review of Project Designs with Special Emphasis on Gender Considerations," March 1985
8. Contract for Design of Technical Assistance System for Small Entrepreneurs, Partnership for Productivity International, Inc., May 20, 1983
9. Karen White, Maria Otero, "Integrating Women into Development Programs: A Guide for Implementation for Latin America and the Caribbean," May 1986
10. Margaret Lycette, "Improving Women's Access to Credit in the Third World: Policy and Project Recommendations," June 1984
11. Evaluation of FIDE, RRNA, 1986

12. Maria Otero and Robert G. Blayney, "An Evaluation of the Dominican Development Foundation's Program for the Development of Micro Enterprise (PRODEME," Washington, D.C., November 1984
13. Gwen Eng, et al, Economic Analysis of Non-Formal Education: Four Case Studies, Washington, D.C., Agency for International Development, 1985
14. "Potential for Expansion of Credit Programs," AID Mission Honduras, no date