CAPITAL DEVELOPMENT INITIATIVE

FINANCIAL SERVICES COMPONENT
FINAL REPORT

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I. EXECUTIVE SUMMARY

The primary purpose of this final report for the Capital Development Initiative Financial Services Component is to summarize the achievements and insights of this $2.8 million program over the life of the program from March 1992 to December 1995. The report discusses those areas where project development was most successful and most disappointing. We have tried to indicate successful strategies and ideas born in CDI that could be applied in other programs designed to promote private sector development and investment.

The activities discussed in the report were provided as part of the U.S. Agency for International Development's Capital Development Initiative. CDI was part of the American Business Initiative (ABI) which was authorized by the Support of Eastern European Democracies (SEED) Act of 1989 in response to the needs for reform and assistance in the former eastern bloc countries of Central and Eastern Europe. The overall goal of the ABI was to promote privatization, the development of market economies and the establishment of democracies in Central Europe. Private sector investment was considered a major component of that program.

USAID sought to promote U.S. and local private sector investments in the region as a way to address the area's very serious infrastructure and economic problems, specifically for the areas of energy, environment and telecommunications. The Capital Development Initiative had four components administered by Washington, DC, based contractors -- Environment by Sanders, International; Telecommunications by Booz-Allen & Hamilton; Energy by ICF Clement International; and, Financial by Coopers & Lybrand. The Financial Services component was designed to assist in coordinating the three functional areas, as well as to provide assistance to both local companies and American firms in securing financing for promising investments. Coopers & Lybrand developed and administered a cost-sharing grant program to support the cost of feasibility studies as an inducement to American firms to evaluate potential investments in Central and Eastern Europe. The Financial Services contractor was also responsible for the development of financing resource guide for the region and for the administration of the CDI Regional Project Office in Warsaw. Technical assistance to U.S. and local firms was provided by the Regional Business Development Office Staff in Warsaw composed of two financial and local business specialists and F. John Paul Andrews, C&L's Regional Business Development Officer.

The program was implemented over a thirty three month period and total expenditures were approximately $1.65 million. The Development Cost Support Fund awarded over $3 million in cost sharing grants to nine American firms investigating projects in Central and Eastern Europe. Grant projects in contract or implementation are expected to generate over $110 million in the region . The RBDO Office delivered technical assistance to many of U.S. and local firms working with the technical RBDOs and by December '95 five joint ventures or letters of intent had been signed. At the request of regional Offices of AID Representatives, the RBDO Office developed numerous investment guides and specific financial reports as needed. The RBDO Office also developed *The Financing Guide for Central and Eastern Europe*. The Guide was widely distributed in the region and to U.S. commercial firms. It has been revised several times and each edition receives a wider distribution. USAID's Center for Trade and Investment Services will up-date and distribute the Guide in the future.

Many of the lessons learned in this project clearly support the initial assumptions of the CDI project planners. Access to finance is a critical element for project success and the targeted sectors of the CDI Program found many worth projects but scarce financial resources. U.S. investors need technical assistance not just to identify projects but to navigate the differences in business cultures. Limited financial assistance, as in a cost sharing grant, can provide essential help to U.S. firms investigating opportunities in emerging markets. Frequently American investors need time, patience and money to see an international project through to completion, especially if it is a joint venture. The CDI Project, with technical assistance in the RBDO Office and through the grant program, addressed several of these traditional concerns.

The CDI Program identified several consistent impediments to private sector growth and enterprise development. Governments in theregion are making progress to address many of these concerns but USAID can certainly play a role to expedite the process. Improvement in the commercial infrastructure of the region is critical to enterprise development and investment. An efficient and reliable banking system, a clear and consistent commercial code, enforceable contract law, civil law, development of public financing mechanisms and an effective equity market are just a few of the commercial infrastructure components that need to be in place for rapid economic growth. Fortunately, USAID has many projects active in the region to address these issues. A more severe constraint to enterprise development, however, is an erratic regulatory environment. A cultural legacy of central planning, the bureaucratic labyrinth of licensing and regulatory process is very confusing and frustrating to investors and entrepreneurs. USAID's effort to encourage host country governments to develop clear, consistent procedures can only result in economic benefits.

The primary goal of the Capital Development Initiative was the application of American technology and investment to the infrastructure problems of Central and Eastern Europe. Through technical assistance to U.S. and indigenous firms to facilitate joint ventures and through assistance to OARs for policy dialogue efforts, the CDI project achieved its goals. Through support for U.S. firms through the Development Cost Support Fund Grant Program and financing information distributed to the American private sector, the CDI project achieved its goals. The success of these new enterprises in the region is USAID's accomplishment as well.

II. OBJECTIVES OF THE FINANCIAL SERVICES COMPONENT

A. Overview of the Capital Development Initiative

The Support for Eastern European Democracies (SEED) Act of 1989 assigned the U.S. Agency for International Development wide ranging responsibilities for assisting the emerging democracies of Central and Eastern Europe (CEE). The Act, in addition to providing authority to establish enterprise funds in CEE countries, included an initiative for increasing the participation of U.S. businesses in the emerging economies. This initiative supported U.S. investment in the countries in the region and encouraged the participation of American firms in modernizing the infrastructure of the region.

Assistance to U.S. commercial interest was provided in the SEED Act through the American Business and Private Sector Development Initiative (ABI). The ABI assigned each of several U.S. Government agencies a role in promoting private sector development. The Department of Commerce, the Overseas Private Investment Corporation, the Trade and Development Agency as well as the US Agency for International Development (USAID) were each responsible for implementing a specific aspect of the ABI. Funding for all ABI activities was included in the USAID appropriation and then made available to the participating agencies through interagency agreements. The Department of Commerce administered three ABI projects: one to support U.S. trade associations in developing comparable industrial groups in CEE; a second which provided support services and temporary office space in business centers in several cities in the region; and a third which published and distributed information on business opportunities in the region to the U.S. business community. The Overseas Private Investment Corporation provided cost-sharing grants of up to $100,000 under the ABI to U.S. firms to defray the cost of feasibility studies for investment opportunities. A comparable program was carried out by the Trade and Development Agency to help U.S. firms defray the cost of investigating opportunities in the region that had significant export potential.

The Capital Development Initiative was the component of ABI carried out by USAID. The CDI was unique among the ABI activities in that it provided assistance exclusively for infrastructure projects in the energy, telecommunications and environmental sectors. The technical assistance project encouraged the application of U.S. investment and technology to the infrastructure needs in Central and Eastern Europe. This support was consistent with the development goals of USAID to support modernization of power and telecommunications systems and arresting the effects of pollution and widespread environmental damage. The CDI Project provided assistance to U.S. firms to leverage the time and money applied to development activities through technical assistance and financial support. Technical assistance was available to U.S. firms and their potential local partners to help them develop project opportunities. The Development Cost Support Fund, set up as part of CDI, provided grants covering up to 50% of the cost incurred by a U.S. firm investigating an opportunity in one of the three targeted sectors.

The activities of the Capital Development Initiative were carried out in close coordination with those of other ABI participants, particularly the Department of Commerce. Two DOC publications, *Eastern Europe Business Bulletin* and *Eastern Europe Looks for Partners*, were used to publicize the CDI and to announce specific investment opportunities. Many inquiries received during the operation of the Development Cost Support Fund were referred to the appropriate program at OPIC or TDA if the proposed activity did not meet the CDI criteria.

The CDI was carried out by four firm selected competitively to provide financial and technical services at no cost to U.S. businesses and potential local partners exploring opportunities in the CEE countries. Each firm had responsibility for a specific sub-component of the Capital Development Initiative.

Booz-Allen & Hamilton	Telecommunications
ICF Resources	Energy
Sanders International, Inc.	Environment
Coopers & Lybrand	Finance

Management and oversight for each sub-component of the CDI was provide by separate USAID project officers. Under the original project design and during the period the Development Cost Support Fund was in operation, the project officer for the financial services sub-component was responsible for coordinating the activities for all four sub-components. After the first eighteen months of implementation, project emphasis was directed to assistance to indigenous private sector firms in the region and policy reform initiatives. At that time the activities of each sub-component were subsumed under the appropriate sector portfolio and were managed separately by Technical Project Officers in USAID/Washington.

The Capital Development Initiative addressed the most serious of the constraints to increased U.S. business participation in the region, particularly the difficulties faced by small and medium sized firms -- insufficient funds to explore investment opportunities adequately and limited experience in conducting business relationships outside the United States. Under the CDI, U.S. firms that met the criteria could obtain grants of up to $500,000 from the Development Cost Support Fund to cover fifty percent of the cost of investigating opportunities in Central and Eastern Europe. Consistent with the development objectives of USAID, this assistance was only available for projects which contributed to the modernization of infrastructure in the critical sectors of energy, environment and telecommunications.

To help overcome the difficulties that U.S. firms often experience in pursuing opportunities overseas, the CDI made available technical specialists with knowledge of business conditions and practices in the region to work with these firms and their potential local partners. Regional Business Development Officers and their staffs identified project opportunities in each of the targeted sectors, broadcast information about opportunities and worked with the potential venture partners as necessary. The financial sector component of CDI worked with all the technical sectors in identifying potential sources for project finance, supporting U.S. firms' investigation of project opportunities and assisting local firms.

B. Role of the Financial Services Provider

The various components of the Capital Development Initiative were designed to encourage U.S. participation in the economic transition in Central and Eastern Europe as well as to address conditions that might discourage extensive participation by U.S. firms in the targeted sectors of energy, telecommunications and the environment. Involvement of U.S. industry in the region had been virtually non-existent for forty years because of the political and economic orientation of Central and Eastern Europe. Potential U.S. investors greeted the vast changes in the region with understandable caution. At the time CDI was developed there was widespread consensus that, given the conditions in the region, potential U.S. investment needed to be supported by U.S. Government assistance programs in order to realize levels of foreign investment that would bring about economic growth to the region, as well as ensure U.S. participation in markets that would become increasingly attractive and vigorous over the next ten to twenty years.

The financial services component of CDI sought to address both the need to leverage the limited resources available to explore investment opportunities in the CEE region and the need to identify alternative sources of project finance. It was evident at the time that both these concerns needed to be addressed in order to increase U.S. participation -- especially that of small and medium sized businesses -- in infrastructure projects. For these reasons the financial services component was a central part of the CDI that provided the link between sector specific business development assistance provided by the project technical sub-components and the financial resources needed to explore and consummate investment projects.

The financial services component had two main sets of separate, but inter-related activities. The first set involved the project financing and financial analysis activities headed by the Financial Services Regional Business Development Officer (RBDO). The second set was comprised of the cost-sharing grant activities embodied in the Development Cost Support Fund. These two sets of activities have been the responsibility of Coopers & Lybrand working under the direction of USAID technical officers and in coordination with other CDI technical assistance contractors. In addition to these two tasks, C&L was responsible for the operation of the regional project office in Warsaw and the publication of a financing guide for targeted sector projects in the region. (RBDO Project Office administration duties are discussed in the Government Property Report included in the Appendices of this report.) To be effective in fulfilling the purposes of the project, C&L worked with a range of organizations including the World Bank, IFC, OPIC, Department of Commerce, TDA, international donor organizations and international financial institutions, as well as indigenous government agencies and business organizations.

The expected results of the project include:

A resource document of financing sources for the region to be distributed to potential investors.

Viable projects out of the grant program which represent U.S. investment and application of appropriate technologies to address the infrastructure needs of the region.

Financial services technical assistance should have facilitated establishment of joint venture activities and provided assistance to regional Office of AID Representatives on specific financing needs as requested.

III. REGIONAL BUSINESS DEVELOPMENT OFFICER ACTIVITIES

The Capital Development Initiative program was conceived in a period of dramatic change in Central and Eastern Europe, when the euphoria over the collapse of communism led to a rush by American businesses into the region. The prospect of new, untapped markets fed this enthusiasm as did the clear need for rapid solutions of urgent infrastructure needs. However as the CDI Program began the euphoria began to wane as businesses ran up against the reality of severely limited and competing financing sources, the lack of commercial infrastructure and the absence of market oriented business expertise in the region.

The principal purpose of the Financial Services subcomponent of CDI was to identify financial resources for capital projects in the sectors of energy, telecommunications and environment. A primary assumption of the Initiative was that financing is a critical element in attracting U.S. and other investment into the emerging markets of Central and Eastern Europe. To address this need, the CDI program set up a Regional Business Development Office (RBDO) in Poland. The C&L Financial Services subcomponent was responsible for identifying potential sources of finance for capital projects and helping investors in structuring the project finance requirement to effect a transaction.

The initial focus of activities for the Financial Services RBDO was to identify potential sources of financing for projects in the targeted sectors which involved U.S. investors. These activities included finding European and U.S. private and multilateral sources of financing for infrastructure projects. *The Financing Guide for Central and Eastern Europe* was the result of these efforts and its development and distribution is discussed in another section of this report. The Financial Services RBDO also provided advisory services to U.S. firms and indigenous firms and organizations in cooperation with other CDI technical components. About eighteen months into CDI activities, project emphasis shifted from assistance and support for U.S. firms investment in the region to technical assistance to local, indigenous firms and work on the enabling environment to improve private sector growth and investment.

A. Financing CDI Projects

The experiences of the Financial Services Regional Business Development Office forcefully confirmed the initial assumptions of CDI about the need for financing to support infrastructure investments in the region. While there are many potential sources of financing in place, few are provided financing to the ventures targeted in the CDI Program.

There are several reasons for the lack of financing for CDI Program projects. One of the major reasons is the excessive foreign debt carried by most of the CEE countries and the skeptical view that many potential lenders have of the countries' ability to reduce the debt burdens in the face of current economic conditions. Most countries are looking at diminishing tax bases and growing budget deficits. Currencies are overvalued in most countries and there is an increasing need to provide more public services in the absence of any significant increase in public revenues.

There is also a large number of unpaid and rescheduled loans made by Western sources to the previous regimes in the region. For example, the Paris Club has forgiven fifty percent of Poland's debt to international donors, but none of the private debt has been reduced. Given this debt overhang most Western sources of capital are reluctant to increase their exposure.

Multilateral institutions such as the IFC and EBRD, and the US-financed Overseas Private Investment Corporation, which are mandated to support viable projects, provide some support. These organizations usually participate directly in projects requiring a minimum financing on their part of $5.0 million and where there participation is approximately 25%-35% of total project costs. This translates into a minimum project size of $15-$20 million. The financing requirements of most of the CDI projects are well below this amount. The EBRD and IFC recognize the shortcomings of the prevalent financing policies, and have formed associations with participating banks to address the need for smaller scale financing. The banks regard this business as riskier and less profitable and, therefore, do not pursue it aggressively.

Even in the case of larger projects, many potential financing sources are more interested in arranging financing and earning fees rather than advancing many of their own funds. Western groups that are willing to put in their own funds in the form of loans or share capital focus on larger projects that generate hard currency and are backed by other well capitalized investors. This is particularly the case for infrastructure projects where longer paybacks are generally the norm, because the bank's risk is reduced and the returns are higher for a given investment when other capital is involved as well.

The risks are greater and the rewards are less for supporting small projects even if they are well capitalized, a rare occurrence in the region. Few local or regional banks are interested in financing projects that require long-term commitments as is generally the case with most CDI projects. This reluctance stems from the fact that most banks have a large portfolio of non-performing loans. To offset these potential losses the banks must exact as much profit from their remaining capital as possible. A typical CDI project does not provide the rate of returns or low risk needed to compete with other investments. The USAID-financed enterprise funds in the region fill some of the gap in financing for small and medium sized enterprises, but they are not enough. Indigenous funding agencies, which would be an obvious source of funding for CDI projects, sometimes have difficulty with assessment of the business and financial aspects of a proposed project.

In many countries community environmental infrastructure projects could be funded through a municipal financing mechanism . However, in the central economies of the countries of Central and Eastern Europe municipal finance is a concept with which neither municipalities nor lending institutions are familiar. Communities that need a new water treatment facility, for example, must be extremely creative in finding finance for project development and construction costs. In one case, the technical subcomponent team brought in a municipal finance specialist for a project in the Czech Republic. In another instance, a project finance specialist supported by a USAID grant under the CDI Program, worked with the community leaders of several small towns in the Dunavarrsany region of Hungary for three years to develop a regional, cooperative municipal finance plan for a new waste water treatment facility.

In the course of reviewing financial projections for potential joint ventures the figures often did not justify investment. Frequently this was due to a reluctance of the relevant government Ministry to permit the enterprise an adequate share in the revenues arising from the proposed project. For example, most rural telecommunications projects need to share long distance revenue between the local company and the state operating authority in an appropriate proportion to allow the local firm a potential profit. Frequently projects which fell short of sufficient revenues to cover costs because the executing agency was unwilling to increase water or power charges in the local market to adequately reflect costs.

The contributions of the CDI Program in the area of financing for infrastructure projects has been to identify and get the attention of a number of financing sources including obvious sources and institutions that are more than suitable alternates to existing sources. The CDI has accomplished a great deal in bringing local firms along and improving the understanding of local entrepreneurs and managers in the areas of financing and their ability to attract investment.

B. Technical Assistance Coordination

The mandate of the CDI program was to respond to the infrastructure needs of the CEE countries by encouraging private investment in the targeted sectors. Although all countries in the region were eligible, emphasis was given to the economically advanced countries of the Czech and Slovak Republics, Hungary and Poland. The Regional Business Development Offices were responsible for identifying and responding to investment opportunities; assisting eligible CEE governments with policy, regulatory and institutional issues; and, providing prefeasibility advice in technical, policy and financial fields.

The primary role of the Financial Services RBDO was to support the technical RBDOs on a case by case basis by helping them put business plans together, review financial projections, help source potential financing requirements and, in general, provide whatever financial assistance was required. While the C&L RBDO was not expected to source projects, the office identified and turned over 57 leads to the technical RBDOs resulting in several opportunities. Three leads for environmental projects and four leads for telecom projects led to direct CDI Program support.

In the early stages of the program, emphasis was given to encouraging private sector investment by assisting qualified indigenous companies in finding suitable U.S. joint venture partners. At this time C&L's role was to support the technical RBDO's efforts by conducting preliminary financial analyses and to maintain contact with key personnel at international lending agencies, investment funds, bilateral donor agencies, commercial banks and others that could be potential sources for financing CDI projects. Examples of this type of assistance can be found in the case studies included in the appendices of this report. Brief illustrations of CDI team coordination are represented in two instances, a telecom project called TESA and an environmental project , Nowiny-CEVA.

TESA is a small firm located in Warsaw that, at the time of CDI Project initiation, held a private license to offer E-Mail services in Poland. The company operated successfully in 1991 and built a customer base of about 500 subscribers but then ran into financial difficulties. The firm approached the CDI Telecom RBDO to help identify potential joint venture partners or investors. Technical review of TESA's past operational system and proposed restart showed both were technically feasible and logical and the market for E-mail services was strong. The Financial Services RBDO was part of the project analysis team sent by Booz-Alan & Hamilton to evaluate the TESA project. The Financial Services RBDO worked with the Telecom team to develop financial projections and a capital structure for financing the local firm. The RBDO was also involved in identification of potential sources of finance. The team produced a fifty page investment memorandum to be distributed to potential investors. It provided specific information on the project including legal and regulatory matters, market and sales data, technical feasibility and financial management. The project opportunity was advertised in the Department of Commerce's *Eastern Europe Looks for Partners* and through a direct mailing. Several interested firms were identified and one U.S. company pursued a joint license with TESA's owner. The forward project is still under discussion and appears to be making progress through the legal and regulatory bureaucracies. The TESA project provided a real opportunity for incremental improvement in the Polish telecommunications infrastructure (and commensurate improvement in a wide spectrum of business operations) while providing a potentially profitable investment opportunity for U.S. firms.

The Nowiny-CEVA project is another example of technical team cooperation and project assistance. The Environmental RBDO for Sanders International had been working with a U.S. firm, CEVA International, Inc., to find appropriate joint venture partners in Poland, the Czech Republic and Slovakia for their hazardous waste disposal technology. CEVA had developed a methodology to burn hazardous and special waste in cement kilns which not only provided safe waste disposal but also provide an energy source for production facilities. Discussions were started with the Nowiny Cement Plant in Kielce. After some technical and legal research to support the technology, the Financial Services RBDO worked extensively with both parties on the business plan for the proposed joint venture and recommended possible sources of finance. On August 18, 1993 CEVA and Nowiny signed a Letter of Intent to set up a joint venture. The partners are currently pursuing a project at a steel plant to use the CEVA technology to dispose of hazardous waste as well as an energy source for the plant in lieu of brown coal

C. Technical Assistance to Indigenous Firms and Organizations

Most of the emphasis on the original design for the Capital Development Initiative was on assistance to U.S. firms in locating and negotiating projects. This emphasis underestimated the amount of assistance required by local firms in CEE in structuring projects and dealing with foreign investors. Sustainable economic growth in most economies comes from small and medium sized enterprises but many of these firms need assistance with management skills. Within any business, development of these skills can be critical to success. The experience of the CDI technical sector teams was that almost all enterprises (foreign, joint venture and indigenous firms) need help with licensing/regulatory issues and preparing western business documentation such as balance sheets, market studies, financial projections and business plans. Under the CDI Program the Financial Services subcomponent provided support to indigenous small and medium enterprises in the region in several ways.

Coopers & Lybrand worked with the technical RBDO teams to develop business plans and appropriate financial projections for local firms for potential joint ventures with foreign investors. Assistance to these firms frequently involved intensive work with firm management to develop basis business reporting documentation such as market research and production cost reports. The CDI Project provided direct assistance to over fifty firms and proposed joint ventures. As in any developing economy, the need for this technical assistance far exceeded the ability of any one program to provide it.

The limited experience of managers in CEE countries with profit-driven operations and with western business practices was sometimes a source of misunderstanding in negotiating with western investors. Language differences and terminology both contribute to the difficulty experienced by both sides in communicating. Frequently discussions and negotiations are carried out through interpreters who can vary widely in their ability to interpret and to translate. Even relatively common business terms such as "balance sheet" or "cost of production" may not convey accurately. Inaccurate translations of key phrases can lead to serious misunderstandings between potential partners.

The pace of negotiations could also be a problem in dealings between U.S. investors and local partners. Western investors are generally confident in their positions and are eager to get on with the deal. Local partners would usually be operating in an arena new to them and would move slowly and cautiously to make sure they clearly understood what was being offered or asked. Uncertainty about legal or regulatory issues could also prolong the process and add to the frustration of western investors. The important role that CDI played in this process was to facilitate misunderstandings arising from language or differences in business cultures.

Potential western investors frequently found that basis business practices and documentation were lacking in indigenous firms. Because of the importance central planning placed on meeting output quotas, most enterprises in Central and Eastern Europe have detailed information available on material inputs and production statistics. However, there is usually little information available on labor inputs and other production costs. Assistance provided through CDI was particularly helpful in this area both to local firms and to potential investors. Western businesses new to Eastern Europe and unfamiliar with the legacies of central planning might overlook promising opportunities.

The CDI Financial Services RBDO office used local project annalists to counsel inbound investors on what they should expect in looking at the financial performance of a prospective partner. The RBDO office also worked extensively with managers of local firms to develop typical western business documentation and performance reports. The RBDO Office team was composed of the Financial Services RBDO and two local assistants who provided facilitation with local business custom and financial analysis and help with financial packaging. Most of the local enterprises assisted by the Financial Services RBDO Office were small to medium sized companies, or even more so, small micro enterprises (SMEs).

The office worked closely with numerous local firms to develop business plans and financial projections. Examples of this assistance include Telecom Lublin, Telecom Torun, Retel Bailystok -- all rural telephone companies -- and Stock Board, a database information system. Two environmental projects, Wzormet and Envira,Exbud 22-Enercon Systems, also received assistance. Development of business plans and financial projections was a labor intensive cooperative effort between the local business, the technical RBDO and the financial analyst. Basic business documentation was needed to market these firms to potential investors and potential lenders. Assistance frequently involved working with the enterprise to establish new accounting procedures, management tracking tools and cost evaluation information. Five of the projects resulted in joint ventures or letter of intent, a clear indication of private sector investment. These projects are described in the case studies included in the Appendices of this report.

The C&L project team also worked with local business organizations and government agencies, particularly in Poland, to develop ways to leverage scares assistance resources to the greatest number of beneficiaries. Working with the Environmental subcomponent team, C&L met frequently with the Polish National Fund for Environmental Protection and Water Management to discuss specific projects. The RBDO office also met with them to discuss the financial aspects of project evaluation for activities under consideration for funding by the agency. Members of the RBDO staff discussed small and mediums sized business interests with the Ministry of Trade and Industry, the Department of Small and Medium Sized Enterprises and the Ministry of Labor and Social Policy. They worked with multilateral donor programs like USAID's Gemini Project and the U.K's Knowhow Fund to expand the contact network for enterprise assistance. The RBDO staff also worked with Solidarity's Business Foundation, the Enterprise Development Center and the Foundation for Social and Economic Initiatives to present seminars on business plan development and basic business documentation. Members of the staff spoke often at management seminars and classes conducted by education institutions like Warsaw University.

For example, the project office worked with the Foundations for Social and Economic Initiatives (FISE) and the Enterprise Development Center conducting seminars on basic business documentation, business plan preparation, financial forecasts, market research and production cost analysis for enterprises. However, as essential as management skills and reporting tools are to a business' success, the ability of the lending community and the licensing community to correctly evaluate financial information of a company or for a project is a critical for economic development. The C&L project team met with 13 local directors of FISE for sessions on evaluation of business plans and business documentation. These individuals directed limited funding and technical assistance based on the prospects of success for an enterprise so these evaluation techniques were particularly helpful. The C&L team worked with Warsaw University to develop and conduct seminars on financial evaluation of prospective projects for the environmental directors of 180 gminas throughout Poland. The participants found financial analysis a vital indicator of proposed project success and an important assessment tool in evaluating comparable worthy projects for funding.

D. Assistance to Regional Offices of USAID Representative

Although CDI's primary initial emphasis was to support the technical RBDOs in the identification, and assistance to specific infrastructure projects, in the fulfillment of this mandate the C&L Financial Services RBDO team also contributed to policy reform in the region. This was done whenever the opportunity presented itself by encouraging governmental bodies, either directly or indirectly at meeting, seminars, or via companies we assisted to provide an enabling environment that would encourage private sector investment in the CDI designated areas.

The Financial Services RBDO Office provided assistance to the regional Offices of the USAID Representative (OAR) by conducting assessments of the business climate and capital availability. In the Czech Republic the RBDO prepared a study of the Investment Climate that was distributed not only by the OAR but also the Foreign Commercial Service (FSC) Office of the Department of Commerce. A similar guide was developed for the Slovak Republic. The RBDO Office worked with local consultants to produce a finance guide for small and medium sized business enterprises in Hungary. For the OAR in Poland, the RBDO produced a financing guide for environmental projects and conducted a primary data research project to identify support resources for small and medium sized enterprises. The SME data resource project resulted in a new USAID project to maintain the database and provide small business resource information centers in several cities in Poland.

The investment climate reports were provided in order to assist prospective U.S. investors in deciding to invest in the country concerned. They were written from the perspective of potential long-term investors and emphasizes issues of significant importance to them. The information for the assessments was gathered through interviews with U.S. investors, lawyers, investment and commercial bankers, accountants, management consultants, commentators and U.S. and Czech government officials. The reports included an assessment of the investment climate, taxes, legal considerations, workforce, banking and capital markets and the bureaucracy. The OAR Offices and the FCS Offices distributed the guide to potential investors and used the impartial appraisal of the investment climates to further policy discussions already underway with counterparts in the Czech and Slovak government.

The Hungarian Office of the USAID Representative requested a financing guide for local small and medium sized businesses for presentation at an enterprise conference. The Hungarian guide was prepared with the assistance of local consultants who helped identify specific financial resources for small firms. The guide included descriptions of resources such as Hungarian government programs, international donor resources and financial institutions. The report also identified venture capitalists who provide risk capital to smaller entities It included not only the application procedures to source the funds, but also the individuals and contact numbers at each o the institutions identified. The guide was distributed at a Small Business Seminar in Budapest in July, 1993.

One of the conclusive findings of the CDI project was a dramatic need for support to indigenous firms to develop business plans and financial projections. The CDI project was available to provide this support in a very limited way. Recognizing the growing small and medium sized enterprise sector of the Polish economy, the OAR in Warsaw asked C&L to develop a database to identify and describe assistance available to that sector. The RBDO Office worked closely with the OAR Office to develop a database of support resources for small and medium sized firms in Poland.

The primary research project included identification of potential resources, development of an information questionnaire, database system configuration that could be updated and maintained for future use. Working with local enterprise and systems consultants, C&L designed and distributed a survey instrument to capture the information required . The project identified over 1200 possible service providers including bi-lateral and multi-lateral institutions, local governments bodies and development agencies, chambers of commerce, foundations and other organizations and individuals. Over five hundred of these firms and institutions responded to the data inquiry. The responses were entered into a database and reported in the format developed by C&L in cooperation with the OAR office. The database, documentation and project report were delivered to the OAR office in October, 1994, along with 300 copies of an abreviated hard copy version of the data base. The comprehensive source book was printed in Polish and distributed to various Polish agencies and institutions.. The database is quite detailed and is an important part of a follow on SME Satellite Project sponsored by USAID/Warsaw. The SME Satellite Project is currently operating in three cities in Poland.

Frequently when reviewing indigenous company's business plan or financial projections, the RBDO found that the projects were not good prospects for project finance because the regulatory environment in which they were required to operate would not allow the enterprise enough return to provide an adequate profit margin. Another problem, particularly for environmental projects, was a reluctance on the part of regulatory bodies to allow the enterprise to charge adequate fees for product (i.e. clean water, electric power, etc.). Both of these difficulties address the issue of the enabling environment for private sector growth.

The C&L RBDO Office worked carefully with the OARs in the region to reinforce the need for an enabling environment for private sector development. Areas of discussion included elements that private sector investors look for in making investment decisions.

- o A stable economic and political environment
- o A level playing field for all investors, foreign and domestic, large or small
- o A supportive legal system
- o Realistic taxes
- o The lessening of control to permit private investors to make a fair return on investment

The RBDO also discussed the parameters required for any provider of funds to seriously consider a proposed investment.

- o A market has been identified for the product

- o The sponsors have the capacity and support to execute the project
- o The sponsors have the financial resources to commit to the project
- o Projected revenues indicate an ability to repay lenders and provide investors with an adequate return on their money

Discussions of these issues took place on several occasions with the Polish Agency for Foreign Investment (PAZ), CzechInvest, the Slovak Agency for Foreign Investment, as well as with the State Property Agency in Budapest which is charged with selling state assets. These views were further expressed at meetings held with other government officials in Poland, Hungary and the Czech Republic and Slovakia.

IV. FINANCIAL SOURCE GUIDE

One of the tasks included in the scope for work for the Financial Service subcomponent of the Capital Development Initiative was the development of a financial source guide for Central and Eastern Europe. Coopers & Lybrand was asked to identify public and private sources of debt and equipment financing, domestic and international, required for infrastructure development and joint ventures and to facilitate U.S. industry access to these sources. To fulfill this requirement, C&L put together a *Financing Guide for Central and Eastern Europe*. The guide identifies various sources of financial support for potential investors in the region. The guide, which has now gone through four editions, identifies responsible individuals at the respective institutions, and their contact numbers as well as a brief description of the institution.

The purpose of the guide is to provide potential investors in Central and Eastern Europe (CEE) with a ready reference to possible sources of finance and related support for their projects. The guide is particularly concerned with the energy, environmental and telecommunications sectors covered by the Capital Development Initiative Program. However, it can, of course, be used by potential investors in other non-related industries. The guide concentrates on potential sources of finance for investments by U.S. companies (either singly or in joint ventures with local partners) and its geographical focus in the Czech Republic, Hungary, Poland and the Slovak Republic where most of the region's investment activity is presently taking place. The report breaks down sources into the following components: U.S. government sources; multilateral sources; private banks; private investment funds and advisory services; and, host country support. The source book is an indication of potential sources of financial support available to investors in the region and not a complete listing.

The *Financing Guide for Central and Eastern Europe* was developed by C&L's Regional Business Development Officer through a series of extensive interviews. The research for each entry included identification of the institution's organization, area of primary interest, countries of operation, financial support available and criteria for funding consideration. The Financial Services RBDO met with bankers, government agencies, investment counselors, fund managers, multilateral organizations and government officials to gather information for the guide and to introduce the CDI Program to these institutions. The second part of C&L's mandate was to provide access to potential investors to possible sources of finance. The development of the guide and subsequent revisions provided an excellent opportunity to fulfill the needs of the each task.

Interviews were conducted over a six week period in London, Paris, Geneva, Vienna, Amsterdam and Berlin, as well as in Prague, Bratislava, Warsaw and Budapest. As discussion of the CDI Program would progress, the banker or manager would frequently identify additional funding sources or mechanisms for investigation. Each time the Financial Services RBDO visited the countries in CEE in any capacity, additional programs or services might be identified and new information added to the next edition of the guide.

Throughout the life of the CDI Program, the Financial Services RBDO maintained close relationships with potential funding sources. Potential joint venture partners were introduced to appropriate groups or institutions to explore project finance. Frequently the C&L RBDO Office assisted local firms or joint venture partners to fill out applications or compile financial documentation required for project review. The guide was particularly useful to potential investors trying to work within the region for the first time.

As the countries of Central and Eastern Europe continue to evolve from planned to market economies, their capital requirements, in the form of both loans and equity, as well as related services continue to increase. Some financial assistance for sound, private sector investment comes from external sources such as the U. S. government, multilateral institutions and private commercial and investment banks. Nevertheless, there is a gap between worthy projects in the region and sources to finance these projects.

In addition many private sector entities are more interested in advising prospective investors and arranging financing than in providing the requisite funds particularly for smaller and medium sized enterprises where the credit risk are greatest. Of the activities supported by private sector sources, most involve larger projects where partners are Western and projected cash flows generate hard currency. By focusing on such projects, the private sector sources ensure profitability and mitigate the risk associated with long payback periods for infrastructure capital investments. Another factor that contributes to fewer private sector loans in the region is the large number of unpaid and re-scheduled loans made by Western sources to the former regimes. A portion of this gap is filled by U.S. funded entities, bilateral agencies and multilateral organizations which encourage investments in CEE by assuming a portion of a project's risk.

At present, the indigenous banks are not readily filling this gap. Few local or regional banks aggressively pursue finance projects that require long-term commitments. Reasons for local bank's reluctance include a large existing portfolio of bad loans and inadequate returns to compensate risk. For example, these banks receive returns by investing in government securities or providing trade related and other services equal to or greater than they do from project financing. Sometimes a local lending organization's reluctance may be due to an inability to properly analyze project finance credits. However, a positive trend is emerging.

With the assistance of foreign advisors many indigenous banks are quickly moving up the learning curve and will, it is expected, become more active in the project finance arena in the new future.

The guide was provided directly to potential investors through the RBDO office in Warsaw and through C&L Washington. It was provided through USAID and the US Commercial Services offices in the region. Both USAID and the Commercial Services offices found the guide to be a very useful and practical tool for prospective U.S. investors considering an investment in the region. This was particularly the case with regard to small to medium sized companies that did not have the resources of larger companies to source finance for their projects. Over 5000 copies of the various editions of the guide have been distributed through this network to potential investors.

Additionally, the *Financing Guide for Central and Eastern Europe* was distributed at several conferences and meetings in the U.S. and abroad. For example, Hagleer-Bailly Consulting, Inc.

included the guide in their briefing book for U.S. exhibitors at a conference sponsored by USAID in Budapest in June '95. The conference, "Energy Efficiency: Expanding the Market in Central & Eastern Europe," was also an exhibition for U.S. suppliers of energy efficiency equipment. The guide was also included in the materials distributed at a meeting conducted by the Department of Commerce and sponsored by the White House. 'The White House Conference on Small Business: Opportunities in Central and Eastern Europe," was held in January '95 in Cleveland, Ohio. The Department of Commerce included the guide on its electronic bulletin board in March '95 and it has been available through USAID's Center for Trade and Investment Services for the past two years.

Revisions of the guide over the last two years have been conducted by desk survey. Over the life of the CDI Program, as additional financial sources were identified, information was collected for the next edition of the financing source guide. As new editions were prepared, each institution would be contacted in writing to confirm the information included in the guide. Corrections and up-dates were incorporated along with information about new sources and programs. The first edition of the guide listed 48 possible sources of finance for CDI targeted infrastructure projects in Central and Eastern Europe. The latest edition, September '95, was distributed in November' 95 and included information on 68 institutions and organizations.

USAID's Center for Trade and Investment Services will distribute and up-date the Financing Guide for Central and Eastern Europe in the future. On May 12, 1996, C&L provided CTIS with the latest edition of the guide in hard copy and on disk. We also provided our current distribution list and source contact list for their use. Coopers & Lybrand sent letters to the institutions and individuals who receive the guide directly from us and advised them that CTIS would distribute the document in the future. A letter was also sent to all the institutions and organizations included in the financing guide identifying the contact person at CTIS for corrections, additions and up-dates.

The *Financing Guide for Central and Eastern Europe* received wide distribution within the American business community. Serious investors, businesses interested in a market for their goods and services, and the mildly curious found the guide a helpful resource. It may have been provided the greatest value and broadest assistance of the CDI Program. The latest edition of the guide, as well as a sample of comment letters are included in the Appendices of this report.

V. THE DEVELOPMENT COST SUPPORT FUND

The various components fo the Captial Development Initiative were designed to encourage U.S. participation in the economic transition in Central and Eastern Europe as well as to address conditions that might discourage extensive participation by U.S. firms in the targeted infrastructure sectors of energy, telecommunications and environment. Involvement for U.S. industry in the region had been virtually non-existent for forty years because of the potlitical and economic orientation of the region, and potential U.S. investors greeted the vast changes in Central and Eastern Europe with understandable caution. At the time the CDI was developed there was widespread consensus that, given conditions in the region, potential U.S. investors needed to be supported by the U.S. Government assistance programs for the region to realize levels of foreign growth that would bring about economic growth, as well as to ensure U.S. participation in markest that would become increasingly attractive and vigorous over the next 10-20 years. The Financial Services component of CDI sought to adress both the need to leverage the limited resources available to explore investment opportunities in the CEE region and the need to identify alertnative sources of project finance. It was evident that these concerns needed to be addressed in order to increase U.S. participation -- especially that of small and medium sized firms -- in infrastructure projects. The techncial asssitance activities of the Financial Serivces Regional Businesss Development Office focused on indentifying sources of finance. The cost sharing grant assistance activities embodied in the Development Cost Support Fund helped U.S. firms extend their financial resources to investigate and develop projects.

A. Purpose of the Fund

The objective of USAID's Development Cost Support Fund (DCSF) was to encourage the participation of U.S. firms in the emerging markets of Central and Eastern Europe by leveraging the resources of firms to investigate investment opportunities in these countries. By offering grants covering up to 50% of the cost incurred in investigating the feasibility of an investment project in the region, the DCSF in effect doubled the dollars a U.S. firm could devote to developing a specific project or potential joint venture.

Even though large firms were not excluded from participation in thge DCSF, the fund was intended especially for small and medium sized U.S. firms, which were more likely to need the leverage (and inducement) offered by a cost sharing grant for feasibility studies. While many recognized that the three critical sectors targeted by CDI were more likely to attract large companies, the emphasis on small and medium sized firms was considered important for developmental purposes.

The Development Cost Support Fund was launched in April '92 with an announcement in the *Commerce Business Daily*. The Fund accepted applications until August '93 when it closed as USAID shifted the emphasis of the CDI program from support for U.S. participation in the region to assistance that would strengthen indigenous private sector businesses and the private sector enabling environment. During its short life, the Fund received approximately 1500 inquiries from U.S. firms, and more than half of those requested applications for grant assistance. The Fund awarded over three million dollars in grants to U.S. firms for investment projects in energy, telecommuunications and the evnironment. These projects are bringing to the region new technologies that will contribute to reduce pollution, increased energy efficiency, and improved communications for rural communities and other areas.

B. Principal Activities of the Fund

The Development Cost Support Fund provided grants covering up to 50% of the costs incurred in investigating an opportunity and developing a project in the region. USAID's participation was limited to a maximum of $500,000 in each grant situation. Only infrastructure projects in energy, telecommunications and environment sectors were eligible for a DCSF grant. Prospective applicants for grants involving projects in other sectors were refeed to other ABI participants, OPIC or TDA.

To be eligible for a grant the applicant had to be a U.S. firm (more than 50% beneficial U.S. ownership) and demonstrate sufficient business and technical resources for the forward project. The applicant present a grant proposal based on a specific project the firm had identified and investigated. The grant funds were used to conduct feasibility studies or project development activities needed to secure finance for the proposed project. The project had to utilize a commercially proven technology and the applicant had to provide reasonalbe evidence that an investment would result if the prospective project proved feasible. Projects were expected to have a positive development effect and were reviewed to assure that no adverse environmental impact would result. With the addition of Section 599 to the Foreign Assistance Act, applicants were also required to certify that the proposed project would not result in any loss or transfer of U.S. jobs. Grants provided by the Fund covered only the agreed upon share of the actual cost incurred in carrying out the activities specified in the project budget agreed upon during grant negotiations. The grant also required the firm to delliver specific project reports as part of the payment schedule.

Sixteen grant applications were received and processed up until August 18, 1993, when the program was offically closed to new applications by USAID through an announcement in the *Commerce Business Daily*. Nine grants were awarded for energy, telecommunications and environmental projects in Poland, Hungary, Bulgaria, Romania and the Czech Republic. Development Cost Support Fund grants were awarded to the following firms.

· Future Water International of Chicago, was a consortium of engineering, construction and water resource design firms investigating two project opportunities in Poland and Hungary.

· U.S. West of Denver, recieved a DCSF grant to support its bid preparation for the privatization of the Hungarian Telephone Company.

· ITEC, Inc., a small telecommunications manufacturing firm in Hunstville, AL, requested funding to support a feasibility study of the installation of its equipment to facilitate commercial billing practices for the Bulgarian Telephone Company.

· Fail, Inc. of Bay Springs, MS, was investigating numerous opportunities for rural telecommunications systems in Poland and Hungary that would untilize the technologies they were using with their U.S. clients.

· Maguire Group, an engineering firm in Foxborough, MA, was the lead firm in a consortium of firms pursuing two similar projects in Romania and in the Czech Republic. They received two DCSF grants to conduct feasibility studies to convert landfill gas to electricity at municipal landfills in Prague and in Bucharest.

· Genesis Coals, Ltd. of Pittsburgh, received a grant to conduct a feasibility study for a coal cleaning project in Poland

· J. Makowski Co. of Boston, formed a joint venture firm in Poland, Elektrogaz, to explore a coal bed methane to electricity project at a large coal field. Makowski recevied a grant to conduct a feasibiltiy study for the project

· Citizens Power & Light, Corporation of Boston received a grant to conduct a feasibility study for a natural gas to electricity project in Hungary. The project would utilize a developed but under utilized natural gas field and would provide power for several local facilities.

A press release from Future Water International clearly describes AID's intent for the Development Cost Support Fund grant program. The information provided on the forward project expresses AID's best hope for the project.

> "The first CDI grant was awarded to Future Water International (FWI), and Illinois based consortium, to help pay some of the cost associated with the final design of a new waste water relcaimation and reuse system in Glogow, Poland and to support the cost of feasibility studies for similar systems in Hungary. In the words on Dr. John R. Schaeffer, one of four FWI partners, "The new facility will employ state-of-the-art American technology which has been refined and proven over 50 projects in the U.S. during the past two decades." This new system will recycle wastewater on the land and eliminate the discharge of pollutants into the waterways, thus helping emerging

market economies obtain clean water and advancing USAID's sustainable economic development goals."
Future Water International, Press release, July 4, 1993.

The Future Water International Project in the Dunavarsany region of Hungary broke ground for construction of a new regional wastewater treatment/reuse facility on May 13, 1996.

1. Outreach

The sucess of an initiative like CDI depends to a large extent on the effectiveness of an outreach program. This was particularly the case for the Development Cost Support Funds since its main obejctive was to attract and support potential U.S. investors. As a first step, the Development Cost Support Fund was announced in the *Commerce Business Daily* on April 22, 1992. An announcement also appeared in the *Wall Street Journal* on July 15, 1992. Plans to add agribusiness and housing to the projects eligible for assistance from the DCSF, as proposed in the original design for CDI, were canceled as a result of the decision on August 18, 1993, to terminate the DCSF. Implementation of a comprehensive marketing plan developed by the four CDI contractors to bring the Fund to the attentionl of more investors and U.S. firms was also held up by uncertainty regarding the USAID role in supporting U.S. business interests. The plan was to be a marketing strategy which would include an active program to promote the CDI with articles in trade journals, publication of regional activities, referral workshops and coordination of marketing efforts with other ABI participants. It was designed to bring the DCSF to the attention of businesses throughout the United States.

As part of the decision to terminate the Development Cost Support Fund, USAID canceled the proposed marketing effort as support within the Agency for DCSF diminished. As a result, the announcement in the *Wall Street Journal* was the only mass media publicity given to the Fund, and neither the regional workshops nor other activties in the marketing plan were given the opportunity to increase investor demand for the program. Moreover, the first announcement regarding the CDI in the *Commerce Business Daily* was of limited value because it reaches a much smaller commercial audience and one that is comprised mostly of governmental service industries. Copies of the CBD and WSJ announcements are included in the Appendicies.

Nonetheless, during the period the Fund was in operation, approximately 1500 inquireies were received. Out of the total inquireies, 893 U.S. firms requested a DCSF Grant Application Package. Sixteen firms submitted applications and nine grants totalling over three million dollars were awarded. Several awards were for projects with more than one potential site in the region.

GRANT AWARD BY COUNTRY AND SECTOR

Country	Energy	Environment	Telecom	Total	Total Grant Award

Poland	2	1	1	4	$1,441,000
Hungary	1	1	2	4	$ 991,000
Czech Repbulic	1			1	$ 201,000
Bulgaria			1	1	$ 263,000
Romanian	1			1	$ 126,000

2. Fund Administration and Operations

Coopers & Lybrand served as the Fund Administrator for the Development Cost Support Fund. In this role C&L was responsible for providing information about the Captial Development Initiative and grant requirements to potential applicants, assisting applicants with application preparation and coordinating financial and technical reviews of applications received. Other responsibilities of C&L included drafting grant agreements and supporting documentation, and monitoring compliance with the performance requirements set for the grantee by USAID.

All of the application materials and procedures used for the DCSF were developed by C&L in coordination with the USAID Technical Project Officers and the CDI technical contractors. Coopers also worked with USAID General Counsel and the Office of Contracts in developing the grant application package. The package included CDI program information, eligibility criteria and comprehensive applicaiton materials. To support the application process, C&L also developed operating and administrative guidelines, and implemented a system for tracking and reporting the status of applications and grants. A copy of the DCSF grant application package is included in Appendicies of this report.

Application processing included preliminiary reivew for eligibility, financial and tecnical review of the applicant and proposed project, and a recommendation to USAID. Coopers & Lybrand conducted a preliminary assessment of each application as it was received to assure it met the basic eligibility criteria. The preliminary review was discussed with the sector Technical Project Officer to determine if the proposed project was suitable under the sector's development guidelines. The financial review assessed the applicant firm's business and financial qualificiations to conduct the study and the proposed forward project. The technical review was conducted by the technical contractor for the sector and it examined the viability of the forward project and the firm's techncial qualifications. These reviews wer coordinated by C&L, an activitiy that also involved notifying the appropriate Office of the AID Representative and the Regional Business Development Officers in the field. Throughout the the process C&L worked with the applicants to get clarification of technical and financial issues raised by the reviewers. The results of the technical and fiancial reviews were summarized by C&L in the form of a recommendation to USAID to award or deny the grant. The recommendation was submitted to the USAID Review Committee for its final determination regarding grant award.

Total processing time, which typically consumed several weeks of calendar time in obtaining information from applicants, was about three months for an application. Considerable effort was

devoted by the C&L and the CDI Project Officer to reduce the time required to process an application and a number of procedural changes were made. As one example, all applications had to undergo a review by the Bureau's Environmental Office and once an applicaiton was demed to be a strong candidate for a grant, this Environmental Office review was conducted simultaneously with the techncial and financial review instead of sequentially. Also, agreement was reached with the Office of Contracts to expedite gathering information about the company that would be needed if the grant application was successful. Coopers would send a letter to the firm describing additonal information that would be required should the application
be successful. The company then had several weeks to prepare information that OP/EE would need to negotiate a grant agreement while the review process was underway.

To streamline and expedite the award process, C&L and the CDI Project Officer worked with the Office of Procurment to indentify various documents that C&L could draft to reduce the demands of the DCSF program on the Office's workload. As a result, Coopers conducted a cost analysis and preliminary budget negotiations with the applicant following the award decision. To expedite the actual award of the grant, C&L prepared a grant negotiation package for use by OP/EE in their negotiation with the successful applicant. The package consisted of a cost analysis of the proposed grant budget, a draft grant agreement including an itemized budget, scope of work, reporting requirements and a schedule for deliverables. Also included in the package was a memorandum of negotiation describing any issues discussed and resolved with the applicant based on USAID's parameters of the award decision. The grant award package was provided to OP/EE in hard copy and on disk in a format consistent with the data processing systems in use in their office.

Accountability and other performance measurments of the grantee were determined by the CDI Project Officer and other USAID techncial and contract officers and were included in the grant agreement. Coopers & Lybrand developed a Grant Monitor Report for tracking each grantee's compliance with the deliverables and cost schedules specified in the grant agreement. Also, each grantee was provided with an information package prepared by C&L listing key personnel for reports and various USAID travel and cost control requirements.

As the Fund Administrator, C&L provided additional support by reviewing all reimbursement requests, monthly status reports from the grantees and all reports required by grant agreements. Reviewing the reimbursement requests provided the CDI Project Officer with assurance that expenditures under the grant were in compliance with the conditions of the grant and were appropriate under USAID regulations. Reports and other deliverables were reviewed byu C&L and, as required, by the sectoral technical contractor, to make sure grant requirements were satisfied. The current performance and buget status of each grant was included in the Grant Monitor Report submitted monthly to the CDI Project Officer and the USAID technical project officers. A sample of the documentation used to track the status of DCSF grants in included in the Appendices of this report as well as brief description of each DCSF project.

C. Investor Demand for DCSF Assistance

The Development Cost Support Fund received 893 requests for applications. No attempt was made to screen requests, even when it was clear from the name of type of firm that it was interested in providing advisory services rather than developing a project. The vat majority of requests from firms that saw the announcement of the Fund in the *Commerce Business Daily* were service firms. These firms also dominated the request statistics in the first few months following the announcements. Manufacturing firms and investors were slower in requesting applications, probably having learned of the CDI and the Fund more through word of mouth than publications, but soon became the dominant group of requestors.

Sixteen applications for a DCSF grant were recived between April '92 and the closing of the Fund from firms in twelve states. Three of the applicants were large, multinational companies. As might be expected, the largest number of applications was received int he calendar quarter immediately following the public announcements of the Fund in the summer of 1992. The number of applications recieved in subsequent quarters ranged between one and four. In terms of ssectoral distribution, eight applications were received for energy projects, six were for environmental projects and three were for telecommunications projects. A total of eighteen projects were proposed in the sixteen applications. Poland attracted the most project interest and accounted for 60% of the projects in the applications.Nine of sixteen grant applications to the DCSF were approved. The largest number of grants, five, have been made for projects in the energy sector which is also the sector that originated the most applications.

D. Principal Accomplishments of the Fund

Considering the short life and the limitations imposed by restrictions on the marketing campaign, the DCSF accomplished a great deal. It has supported eight firms through nine awards for developing projects that have investment potential of 50-60 times the total grants extended by the Fund. More importantly, it has enabled seven small firms to investigate and possibly take advantage of opportunities they are not likely to have pursued in the absence of the Capital Development Initiative and the DCSF. The experience of these firms points up the importantce of initiatives like CDI in supporting and augmenting U.S. participation in markets that will become increasingly important over the next decades, while contributing to the emerging economies at the same time. The Development Cost Support Fund provided U.S. firms with a way to leverage their project development resources to pursue investments in Central and Eastern Europe. This assistance was particularly valuable to small and medium sized firms, but obviously was also an incentive to the the three multinational firms that applied for grants.

> "The costs of planning, engineering and construction inspection (for this project) was reduced from a typical 15% of construction cost to 10%. This reduction relfects the availability of the US Agency for International Development (CDI) Development Cost Support Fund for the model project in Hungary." Future Water International, Inc., DCSF Grant Report - Hungarian Project Engineering Report, Dec. '93.

The projects funded under the DCSF can make an ecnomic and technological contribution to the emerging markets of Central and Eastern Europe. These projects bring state-of-the-art technologies to advance developments in critical areas and provide solutions to energy, envrionmental and telecommuncitionas problems. The DCSF program provides an execellent example of the goal of CDI: to facilitate the application of U.S. technology and capital to the infrastructure problems in the region. The final project report of the environmental technical contractor makes this comment about the Fund.

> " The existence of the CDI Development Cost Support Fund managed by Coopers & Lybrand was a useful concept for interesting U. S. environomental companies int he potential of Central Europe in the early stages of the project. The decision to terminate the Fund almost certainly had an adverse impact on the CDI Environmental Sub-component because it took away one "recruiting"tool and because the difficulty in securing feasibiltiy study funding is a constraint on developing projects in the region." Final Report of Sanders International, Inc., March '95

The participation by these firms in exploring project opportunties in an emerging market has a long term benefit for both the firm and USAID's development goals. Each of the firms awarded a Development Cost Support Fund grant continues to pursue projects and marketing activities in Central and Easter Europe. Even if the particular project they initially identified did not come to fruitiion, these firms are building on the professional and commercial relationships established during their work together to explore additional opportunities. Several firms are now exploring opportunities in emerging market countries in Latin America and Asia based on their experiences in Central and Easter Europe. This intangile benefit holds the possibility of profit for the individual firm and the private sector community in the developing country. A brief description of each grant award and current project status is included in the Appendicies of this report.

VI. LESSONS LEARNED

The Capital Development Initiative offers a model of a results-oriented program that has not only made measurable improvements in the infrastructure in the region, but has also helped to strengthen the competitive position of the American business community in the targeted areas. The CDI Program helped USAID to identify barriers that were preventing private sector development and solutions to infrastructure needs as well as impediments to US commercial participation in the region. As a result the Program has helped develop a base of understanding which will prove useful in designing future projects in the region.

USAID's strategy of building local business capacity by facilitating sustainable linkages with U.S. firms proved appropriate and sound. Building relationships between U.S. and local firms is not only a cost-effective way of supporting long-term progress in the region, but also promotes U.S. competitiveness in by creating a demand-pull for ongoing U.S. merchandise and service exports to the region.

Projects take a long time to develop in any emerging economy and staying power is critical to their success. The shortest time to develop project under the CDI project was nine months for an environmental project, while some projects which were already being considered at the start of the CDI Program still had not be successfully launched at the Program's conclusion despite substantial assistance from CDI staff in Washington and the field. Most projects take 18 to 36 months to gestate and the failure rate is high. Both the U.S. and local partners need assistance throughout the process.

This chapter will examine the expected results of the project and lessons learned for future programs in the region.

A. Expected Program Results

1. Production of a financing resource guide for the region.

The Financing Guide for Central and Eastern Europe provided U.S. firms with important contact information about potential financing sources for projects in the region. Based on the requests received by Coopers & Lybrand from OAR offices in the region, U.S. Government agencies and American businesses, the extensive distribution of this document may have provided the CDI Program with its greatest success. The Guide was well received by the U.S. private sector that the Department of Commerce included it on its Electronic Bulletin Board. USAID's Center for Trade and Investment Services received so many requests for similar resource information about other regions of the world that they are currently compiling similar information for other USAID Bureau countries. The Center for Trade and Investment Services will be responsible for all future distribution of the Guide.

2. Facilitation of joint ventures and specific technical assistance to regional OARs.

The RBDO Office provided support to many U.S. and local firms seeking joint venture partners. Assistance was provided to review business plans, create balance sheets and income statements, as well as to devleop cash flows and marketing strategies. In most of the projects assisted, potential sources of funding were identified and introductions were also provided. Five of the projects assisted resulted in joint ventures or letters of intent, key indicative steps signaling private sector investment.

Nowiny-Ceva: A project in which a steel plant substituted waste incineration for brown coal for its energy supply. The RBDO office worked with the Environment RBDO office over several months to review and refine the business plan and to identify potential sources of finance. Nowiny, the Polish partner, and Ceva, a U.S. firm, signed a letter of intent.

Segi-PBG, Intergeo-Mayfair Petroleum: A letter of intent has been signed between Segi-PBG, a Polish firm, and the U.S. firm, Mayfair, to market and eventually produce software to control air pollution. The RBDO Office worked extensively with these firms to identify funding sources.

Narbu, Wamag, Romfama - Natural Resources Recovery and World Energy Fuels: This project is a joint venture between Polish and US firms to produce biobriquettes and attendant equipment. The RBDO Office worked with the partners to review business plans and contact potential sources of finance for the joint venture.

Envira, Exbudd-22 - Enercon Systems: This joint venture between two Polish firms and a U.S. manufacturer was established to produce mobile incinerators. The RBDO office worked with these firms over a seven month period to develop the business plan, financial projects and possible funding sources.

Progres - Carpco: The RBDO Office prepared the business plan and introduced financing sources for this joint venture to produce clean coal product and rehabilitate spent sulfur mines in Poland.

The RBDO office in Warsaw also provided direct assistance to the OAR Offices in the Region. The Warsaw OAR requested assistance to identify specific funding sources for environmental projects in Poland. The presumption was that, given the emphasis placed on environmental clean-up and integrity by the Polish population, financing for environmental projects would be plentiful and easy to access. The resulting study clearly identified lending constraints for this sector and was useful to the OAR in policy discussions with Polish counterparts as well as for future USAID project planning.

The private sector officer in the OAR Office in Prague along with the DOC Foreign Commercial Service Officer instigated a request to the RBDO Office for an investment climate guide for the Czech Republic. This impartial review of investment constraints written from the prospective of a long-term investor was particularly helpful to the OAR and DOC offices in policy discussions with the Czech government about the investment environment. The guide was also distributed to U.S. firms investigating opportunities in the Czech Republic.

The financial management assistance the CDI Program was able to provide a limited number of indigenous firms indicated a clear need for this specific type of assistance. The OAR Office in Warsaw asked the RBDO Office to develop a survey instrument and a database to identify sources of management assistance available in Poland. The primary data research project then became a SME support project in USAID/Warsaw's private sector portfolio.

3 Application of U.S. Technology and U.S. investment in region from the grant program.

The Development Cost Support Fund provided financial assistance to U.S. firms in the form of cost sharing grants. Most of the firms that received grant awards are still pursing projects in the region, and five of the projects clearly demonstrate the goals of the Capital Development Initiative, use of U.S. technology and investment to address the infrastructure needs of the region.

Future Water International: This consortium investigated two waste-water reuse projects, one in Poland and one in Hungary. The Polish project is slowly working its way to reality through a very difficult bureaucratic barrier. The Hungarian project broke ground in May '96 on a $15-20 million regional waste water treatment and reuse facility. Schaffer and Roland, the lead firm in the FWI consortium, is still involved in the project consulting on production materials and methodologies as well as completing the final design elements of the facility.

Genesis Coals: This U.S. firm has developed a coal cleaning process that markets its product to mines in the U.S. The refinement process increases the yield of high quality coal from a processing run. They received a grant to investigate coal cleaning projects in Poland. They found that their best client in Poland was not the mines, but the power plants burning the coal. The Genesis methodology could help the Polish power grid meet EC air quality standards more quickly and at less cost than conventional scrubbers. Genesis Coal is in negotiation with three regional power plants to construct a facility to provide clean coal and long term purchase agreements are under discussion. Estimated cost for each plant would be approximately $30 million.

Maguire Group: Maguire received two grants, one for a landfill gas to electricity project in Prague and one in Bucharest. The Bucharest project is proceeding under the direction of Power Management Corporation which is pursuing funding for final design and construction. The Bucharest project will be a $10-15 million power generation project that also controls the environmentally hazardous methane gas in the region.

ITEC, Inc.: The DCSF Grant for this small Alabama firm was to conduct a feasibility study for a telecommunications bridge technology project. ITEC manufactures telecom monitoring equipment that can provide digital billing capability on analog telephone systems. This enables the telecom provider to enhance its billing capabilities as one revenue source to finance the transition to digital equipment. Over the next five years ITEC expects to sell the Bulgarian Telephone Company $8 million worth of ITEC Equipment. The firm hopes to establish a manufacturing facility in Bulgaria during that time to support additional projects in the region.

Fail, Inc.: Fail specializes in remote location, rural telecommunications systems in the U.S. The DCSF Grant awarded this firm was for nine feasibility studies for rural telecommunications projects in Poland and Hungary. Three of the studies were for regions in Hungary where Fail won development concession awards from the Government of Hungary. The three projects represented service to over 150, 000 households, almost three times their U.S. market. The firm set up the joint venture structure for the operating companies and will participate in the forward development as a 40% partner with another US firm, HTTC. Fail's investment in the region to date is approximately $12 million.

B. LESSONS LEARNED

Many of the lessons learned in this project clearly reflected the initial assumptions of project planners: financing is a critical element; potential investors need information about the business environment not just the business venture; and, limited financial assistance can provide essential leverage for small U.S. firms interested in the region. Additional lessons learned include identification of impediments to private sector development and implications of program administration on future projects in the region.

1. Financing is a critical element for project success.

Despite much talk about numerous program and substantial amounts of money available, very little financing is effectively available for infrastructure projects in Central and Eastern Europe. The requirements imposed by lenders (collateral, equity, minimum size, etc.) as well as the reticence of lenders to risk limited capital are particularly difficult for small environmental and telecommunications projects. The first question that must be asked in evaluating potential projects is how will it be financed. The funding criteria for projects in the emerging markets of Central and Eastern Europe are the same as for projects anywhere in the world.

The sponsors have the capacity and support to execute the project.
The sponsors have the financial resources to commit to the project.
Projected revenues indicate an ability to repay lenders and provide investors with an adequate return on their money.
A market has been identified for the product.

The multilateral development banks have long project development cycles and many CDI projects, especially environmental and rural telecommunications projects, are below their multimillion dollar project size cut-offs, or are too risky to qualify for their programs. Most CEE country governments are unwilling to provide the sovereign guarantees many programs or lenders require. Municipal financing mechanisms prevalent in community infrastructure projects in the U.S. are non existent in the region. Many planners and business people in the both the U.S. and the region fail to distinguish clearly between public sector versus private sector projects and the very different types of financial management's that each requires. Local project sponsors often assume that the foreign party will bring funding for a project. However, if a project is a public sector project, municipalities are often unwilling, unable or too inexperienced to impose user fees or to allocate scarce funds to service the debt. Private sector firms in the region often lack cash flow to pay for capital investments and expect the foreign partner to provide all the financing.

Over the almost three year course of the CDI Program substantial change has occurred in the region. Most of the economies have begun to recover, market oriented institutions are emerging, and local business sophistication is increasing with exposure to the West and growth of local enterprise. These changes contribute to the economic stability necessary to increase capital circulation for project finance. USAID's continued efforts to support the commercial infrastructure development of CEE countries can be its most significant contribution to resolving critical financial needs for infrastructure projects in the region.

2. Knowledge of local business infrastructure is critical to investment and enterprise development.

An enduring and consistent lesson from the CDI Program experience is that investor's need to know about the local business environment. Many U.S. business people were disappointed to learn the basic western business practices and documentation are lacking. They also found that differences in business cultures can create impediments.

Potential joint venture partners were put off by the difficulty in gaining reliable information from their prospective local partner. Most of this frustration stems from the incomplete or unorthodox nature of the information that is provided to outside investors. Because of the importance central planning placed upon meeting quotas, most enterprises in CEE have detailed information available on material inputs and production statistics. Typically, however, there is little information available on labor inputs and other costs of production. Lack of adequate information on efficiency, and an apparent lack of concern with cost is worrisome to most investors and cast enterprises and their management's in a worse light than some deserve. Investors new to the region and unfamiliar with the legacies of central planning often do not get these perceptions and overlook what may be a promising opportunity. Assistance provided through the RBDO Office was helpful in moving otherwise well matched potential partners beyond the concern with management information.

The limited experience of managers in the CEE countries with profit-driven operations and with western business practices were sources of misunderstanding in negotiation with western investors. Language differences and terminology both contribute to the difficulty experienced by both sides in communicating. Frequently discussions and negotiations are carried on through interpreters. Interpreters can vary widely in their ability to interpret and, particularly, in their ability to translate business terminology, including even relatively common terms such as "balance sheet" or "cost of production." Inaccurate translations of key phrases was often at the heart of serious misunderstandings between potential partners, because each side may leave the discussion table having reached agreement on what turns out to be totally different conditions. The pace of negotiations was almost always a source of difficulty in dealings between U.S. investors and local partners. Unlike Western investors who are generally confident of their position and eager to get on with deal, local partners were operating in an arena that is new to them and move slowly out of caution and the need to thoroughly understand what is being offered or asked. The important role that CDI played in this process is to meet with both parties and verify that misunderstandings do not arise in negotiations because of differences in business cultures.

3. Limited financial assistance can provide essential help to small firms interested in the region.

One lesson of the CDI Program was that getting finance to actually implement a worthwhile project was really the second step. Helping U.S. firms investigate potential projects was the first step. Financial assistance to these firms to share the expense of feasibility studies and project development cost provided an important benefit. The Development Cost Support Fund grant program enabled U.S. firms to leverage their project development dollars by up to 50% and was a useful concept for interesting firms in the potential for Central Europe in the early stages of the CDI Program. This assistance gave many of them the staying power needed to see projects to completion.

The CDI Program was changed from its original direction about 18 months into the project. As a result of the changes, the Development Cost Support Fund grant program was closed to new applications. Many of the CDI teams in the field believed that the decision to terminate the DCSF almost certainly had an adverse impact on their sector specific activities of CDI because it took away a significant "recruiting" tool. The Environmental Sub-component and the Telecommunications Sub-component were particularly concerned because the termination came just as they were seeing the greatest need for this assistance. Many of their projects had completed initial investigation, pre-feasibility, activities and were ready to move to feasibility work necessary for financing.

USAID worked very hard to implement this innovative program. The Technical Project Office did an outstanding job coordinating the USAID internal reviews, discussions and bureaucratic procedures. The success of individual firms in achieving their commerial goals as well as the objectives of the Capital Development Initiative is USAID's accomplishment as well.

4. Impediments to investment and private sector development.

Some of the impediments to investment and private sector development in the region are temporary: weak banking systems, unsophisticated financial markets, erratic regulatory environment. Host congry governments are addressing them as they are able.

Accessing adequate capital, either in loan or equity form, is a critical need for private sector development in the region but is difficult in the local banking environment. Although some financing is provided by bi-lateral and multi-lateral institutions such as EBRD, IFC and OPIC, for example, as well as some private commercial banks, a gap remains between worthy projects and sources to finance these projects.

Many Western financial institutions, both government and private sources, have a preference to support larger projects, involving major companies that are able to generate revenues in hard currency to repay funding provided on that basis. Local banks are burdened with non-performing loans from previous regimes and have limited capital available for lending. The banking system itself is clumsy and inefficient. Traditional Western banking procedures and lending mechanisms are only slowly working their way into standard practice in the region. With limited resources and new imperatives to generate profit, local banks face a daunting task. The type of small enterprise, start-up business lending most CDI projects need presented special difficulties for these indigenous institutions. However, they are working their way up the learning curve, particularly as it applies to extending financing for longer term periods. (In CEE this can mean any lending agreement with more than 3-6 months duration.) Banks currently have little recourse with defaulted borrowers, creating a further disincentive for long term lending. As commercial code revision and stonger contract laws gain ground in the region, this will improve. USAID should continue bank training and commercial policy reform initiatives in the region.

The absence of conventional financing methodologies for infrastructure projects was especially difficult for environmental projects and for some rural telecom projects. Limitations of the financial markets in CEE countries account for much of this problem. When a community wanted to build a new waste water treatment facility, there was no municipal finance tool that could be used. When a U.S. partner and local firm formed a joint venture to develop a rural telecommunications system, there is no venture capital option or equity market option available to them. The community needing the water treatment plant worked for three years to get around or change existing restrictions to generate municipal funds needed for construction and operation. The level of sophistication of the financial markets in the region will advance, in many countries rapidly and in others at a slower pace. However, this is indicative of the importance of the commercial infrastructure for private sector development in any emerging market. Warsaw has a stock exchange that conducts maybe a hundred trades a week primarily between broker accounts. As need for an equity market grows, this will change, but slowly. In contrast, however, USAID is conducting a multi-lateral project in Romania to facilitate the mass privatization program on a project that will establish a NASDAQ type over the counter market for trading newly registered shares. They expect initial activity on this market to generate as much as 16,000,000 trades.

An erratic regulatory environment is particularly troublesome to investors. Western entrepreneurs and investors are accustomed to certainty and consistent adherence to regulations and procedures in their dealing with licensing authorities and regulatory agencies. Obtaining approvals at all levels of government in CEE countries is a much more confusion and uncertain process. Every CDI project in any sector required some licensing or regulatory authority to proceed. Getting those approvals was one of the most time consuming and frustrating activities for U.S. investigators. One of the legacies of the previous regimes in Central and Eastern Europe is an obsessive concern with rules and strict adherence to those rules. In the past, knowing "the system" and conforming to it provided a certain degree of security for the typical citizens. For others knowing the system and how to manipulate it was a profitable activity. The concern with rules is still pervasive, even after independence, but the system did not anticipate the need for the rules and procedures that are required to deal with the many investments and other business transactions that are being carried out in most CEE countries. Given the previous tendency to be governed by "the system", the lack of appropriate, consistent procedures for dealing with what should be routine licensing and business related transactions creates significant delays. There are also some officials or others with access to officials who see the confusion regarding the steps necessary to get approvals as an opportunity to profit from their knowledge, real or claimed, of how to obtain approvals. In this environment investors, foreign and domestic, are confronted with a confusing array of advice and instructions on how to complete various steps in, for example, forming a joint venture or initiating a project. Often the potential joint venture partners are given conflicting advice by different officials in the same Ministry, or must deal with the totally uncoordinated requirements of agencies at the national and local levels. The contribution of CDI was to work with key officials to make them award of the deterrents of investment created by the erratic situation. USAID has an important, on-going role to play in addressing the need for clear, consistent licensing and regulatory environonments in the countries of the region.

Investors look for several critical factors in considering a project in Central and Eastern Europe: a stable economic and political environment; a level playing field for investors, foreign and domestic, regardless of size; a supportive legal system; realistic taxes; and, a policy environment to permit private investors to make a fair return on investment. USAID's efforts to address issues that are impediments to private sector growth can only work to benefit investment and enterprise development in the region.

5. Implications of CDI Program administration for future USAID projects.

It is important to consider the lessons learned from the CDI Program that could benefit future project planning. Several design aspects should be noted and several implementation decisions had significant impacts.

The original design for the Capital Development Initiative designated Warsaw as the site of the regional project office for the Initiative. It was expected that the RBDO's would travel to other countries in CEE on a regular basis to address project needs. Experience proved that this was difficult to provide adequate converage and develop appropriate knowledge of local business conditions in the other countries through short term visits. Similar future programs should provide for a network of offices rather than relying on one regional office.

Most of the emphasis in the original design for CDI as on assistance to U.S. firms in locating , negotiating and financing projects. This emphasis underestimated the amount of assistance required by local firms in structuring projects and dealing with foreign investors. Future efforts should provide for at least equal amount of assistance to U.S. and local firms to assure adequate consideration of potential projects. As a minimum this assistance should include help in developing business and marketing plans. Marketing plans are particularly important because they force managers more accustomed to central planning to consider seriously where the output of their enterprise will be going.

Efforts like CDI rely on promotion for success, particularly the Development Cost Support Fund. The Initiative was limited by the lack of adequate promotion and marketing of program. In a word, few of the U.S. companies that were the target of CDI assistance knew that CDI existed. A large scale marketing effort was developed by the CDI team, but was canceled when USAID changed the program emphasis and direction. At that same time, the DCSF grant program was closed to new applications. Many on the CDI team felt the time frame allowed for theDCSF program was too short. Particularly the technical contractors believed that it was closed just when their sectors were seeing the greatest demand for this CDI assistance.

The experiences with the CDI make it clear that the Initiative addressed a real need and the solutions offered by CDI were appropriate and successful. However, within USAID there were always concerns with the role of the Agency in promoting U.S. investment abroad. During implementation of CDI, there were several television presentations which incorrectly blamed the Agency for costing U.S. workers their jobs. Theses presentations cast a cloud over USAID activities like the CDI and precipitated amendment to the Foreign Assistance Act to include Section 599. The procedural requirements that Section 599 presented for the CDI made it awkward to promote the program and reach the major segments of the U.S. business community that were looking for opportunities in Central and Eastern Europe. The success of future efforts like CDI will benefit greatly from recognition that assistance to U.S. investment in emerging markets can achieve significant benefits for both the U.S. and target economies, and that this assistance is consistent with the USAID mission of sustainable economic development.

APPENDIX I.

CASE STUDIES

CASE STUDIES

The Regional Business Development Office for the Capital Development Initiative Program was open in Warsaw from September 1993 through August 1995. Coopers & Lybrand's Regional Business Development Officer, F. John Paul Andrews, and his staff fo financial analysts were active in Warsaw until January 1995. Services they provided included coordination with CDI technical component teams, information briefings for U.S. business people, intensive work with indigenous entrepreneurs, and conducting financial management skills seminars for local business groups and universities. The RBDO Office also maintained an extensive network of contacts in all branches of the international lending community. This network provided a useful conduit to funding for enterprises in the CDI Program. The Financial Services RBDO worked primarily with the Environmental and Telecommunications components which were located in the Regional Project Office. Frequent exchanges occurred between the Energy RBDO and Coopers & Lybrand's team to relay information about an institution or program, or to check on the status of a project. However, most the staff time and effort was devoted to working with environmental and telecommunications projects.

The original design of the CDI Program was for technical teams and the finance team to U.S. investors with appropriate joint venture partners in the region. Technical teams were to find worthy projects and publicize them in the U.S. When an interested party surfaced the financial team would assist with joint venture negotiation and help find project financing. Regional office staffs would be composed of a Regional Business Development Officer and local personnel hired for their technical skills and their knowledge of the local industry environment.

Project planners could not have anticipated the vast amount of preparation needed by local firms before joint ventures could be discussed. The finance team worked with the technical team and enterprise managers over an extended period of time to develop basic business information western investors would need to evaluate an opportunity. The teams worked jointly with the American business people to help them get the information they needed and to assist with the pace of negotiations.

It would not be possible to list every firm the Financial Services RBDO Office helped, but a brief description is provided of the work conducted. Several case studied follow to further illustrate the activities of the staff.

Nowiny Cement Plant-CEVA: As described previously, this is a joint venture between a Polish company and an American firm to establish a waste disposal/recyling system at a steel plant in Kielce. The plant will burn hazardous waste while generating heat for plant fuel. The system reduces the plant's reliance on polluting brown coal and so accomplishes two environmental goals. The Environmental RBDO office had been working with CEVA in the Czech Republic when the Polish firm was contacted. The organizations signed a joint venture and construction is underway. The financial team worked with this project over several months to refine the financial projections and business plan as well as to identify potential sources of finance.

Progres - Carpco: The finance team worked with the technical team over several months to identify potential sources of finance for this U.S. Polish joint venture. The U.S. partner has provided the equipment (spirals) for a coal cleaning demonstration. A demonstration project is underway to validate to feasibility of this U.S. low cost technology.

Exbud - Envira: This U.S. Polish joint venture provides mobile incinerators for use in disposing of hazardous waste. The finance team work with these partners to develop business plans, financial projections and to complete applications for funding. This firm plans to import one incinerator and produce two in Poland. Funding has been secured for the first project to dispose of stored pesticides.

Worzmet: This small Polish company provides chemical samples for measuring equipment such as gas chronometers, air quality control instruments, medical equipment. The finance team worked with firm for several months, in coordination with the Environmental team, to write the business plan and financial projections for the firm.

CEMG - EkoEfekt: This U.S. Polish joint venture firm is working on a project to reproduce PET bottles. The finance team reviewed the business plan and helped with funding applications. The firm is in the pilot phase of collection and sorting and has received initial funding for the project. The plant will recycle 2,000 tpd of PET plastic bottles, saving resources and landfill space.

Telecom Lublin: The finance team worked with the Telecom team to help this firm produce balance sheets, financial projections and a business plan to try to attract investment. Several U.S. telecom firms had investigated numerous rural telephone systems and Lublin represented an excellent opportunity for relatively little investment, but the absence of basic management information was too daunting for most. Telecom Lublin was talking with Fail, Inc. of Bay Springs, MS, about investment in March '96.

Stock Board: This Polish firm was a start-up firm to provide a database information services. There were several problems with licensing issues to be resolved, but the finance team worked with this company and the Telecom team to develop a business plan. They also assisted with preparation of bank lending forms. The Polish Enterprise Fund is considering the loan application of StockBoard.

HTCC: This is a rural telecom project in Hungary. The finance team met with them numerous times to review their business plan and marketing strategy. The regulatory environment was unwilling to allow the small telecom system enough revenue from long distance calls to attract investment.

Telzut and Ortel: These are rural telecom firms in Poland the finance and the Telecom team worked with to prepare business plans and financial projections. In each case, the small firm could not convince the National Telephone Company to share its long distance revenue or to allow local traffic costs high enough to support the enterprises.

Mescomp: This Polish firm wanted to get into the cable TV and telephone business. The financial team reviewed the business plan and translated them into English for several potential investors. The firm had no problem getting a license from the regulatory agency, they just could not enforce their contract for access with this same institution.

SEGI-Mayfair

The story of this Polish and American joint venture is an interesting study in the way the CDI project provided services to U.S. firms and indigenous enterprises. The principal of Mayfair Environmental Services was employed by a different firm when he initially contacted the CDI Washington based staff in May '93 to obtain CDI support in screening business opportunities in CEE. His interest, which he eventually pursued for Mayfair, was in entering the CEE market with environmental software, especially utilizing the GIS/Key system, a premiere PC based application for environmental site characterization. GIS/Key represents the state of the art in environmental site modeling and assessment, and provides a database necessary to quantify the extent of surface and sub-surface pollution, and to prepare remediation plans. This technology provides a basis for the evaluation and selection of cost-effective technology for monitoring and clean-up. The Environmental team screened at least two dozen firms and the finance team assisted with preliminary financial assessments of each.

One of the candidate firms identified was SEGI-PBG Ltd., a small private Polish company in Warsaw. SEGI-PBG was founded in 1992 as a result of restructuring of the leading Polish state geophysical prospecting company. It is a consulting-service company with a staff of 30 specializing in services for applied geophysics, including environmental monitoring and environmental software applications.

Mayfair and SEGI-PBG signed a letter of intent in October '93 to form a limited liability company or other appropriate business entity in Poland to conduct the business of environmental software translation, installation, maintenance and training. The two partners announced their agreement at the International Ecological Fair in November '93 in Poznan. A joint venture company has since been formed and the new enterprise is operational. Through December '95 the new firm had realized $500,000 in sales of GIS software and remediation services.

The Financial Services RBDO Office worked with the Environmental technical team to review potential partners for the Mayfair venture. They worked with SEGI-PBG to develop appropriate financial information for a western investor and they worked with the joint venture enterprise to develop a business plan. At several points in negotiation, misunderstandings about financial records or business terminology almost ended the discussions. The facilitation provided by the technical and the financial team kept negotiations on track.

EuroSarm

EuroSarm, a private Slovak company based in Martin was established in August '92. It is a strong, well capitalized firm specializing in the storage and wholesale delivery of durable foodstuffs. In June '92 the firm was investigating the possibility of tire recycling project when they met the CDI Environmental Team. EuroSarm proposed to set up a rubber tire recycling facility in the Czech Republic as part of its operations. This decision was based on an economically motivated desire to create a profitable business which would provide environmentally beneficial services. The firm invested in a American marketing specialist to help determine possible markets for end products. The proposed project envisioned a fully integrated rubber tire collection system in Slovakia, because there was no existing waste tire collection organization in Slovakia and no organized scrap tire collection system. There was, however, a rapidly growing demand for crumb rubber products on a commercial basis. The new enterprise would set up a national collection system, acquire the technical skills and equipment for the granulation of waste rubber tires, and contract for the sale of the processed product. Based on their market analysis for its proposed crumb rubber product EuroSarm received several letters of intent from potential buyers. There was good evidence to believe that the product was economically viable and would succeed.

The firm sought help from the CDI team to create a business plan needed to seek funding for the project. Based on technical assistance received from the Environmental team, EuroSarm decided not to locate the processing plant on land it owned in the Czech Repbulic, but to build the facility in Martin, Slovakia. The CDI team continued to work with the firm to create the business plan and to prepare an application for the Slovak-American Enterprise Fund. The application was well received by the Enterprise Fund, but they felt that the identification of an equity partner would improve the likelihood of approval. The CDI team worked with EuroSarm to identify a potential

U.S. partner and a major American waste management firm with state of the art technology expressed interest in the project.

At this point the project stalled. Planned meetings were postponed or rescheduled. A visit by the proposed equity partner was deferred, further meetings with the Enterprise Fund were delayed. The Fund requested a new marketing study. EuroSarm 's inexperience in western financial matters and the Fund's reluctance to commit to an investment in the project caused frustrations on all sides. Seven months after their first review of the EuroSarm project, the Enterprise Fund rejected the application as too risky for its portfolio.

There was significant evidence that the EuroSarm project could have succeeded. There were risks in unforeseen regulatory constraints, or that the EuroSarm management team was not up to the tasks of following through on such a departure from its core business. But these risks had been evaluated and did not seem insurmountable. The Fund could indicated early on that they considered the project too risky and that the chances of a loan were slim. The CDI Team was perhaps to enthusiastic in their support for the project and could have used more conservative evaluation criteria to determine financibility of this potential project. The difficulty in Central Europe is that so much up-front work must be done to provide a basis for any fair assessment of the financibility of a project. The inexperience of the company and the reluctance of the lender proved to be fatal as this project riddled with indecision and misunderstanding among the primary players finally failed.

Rural Telecom Systems in Poland

Rural telecommunications projects in Central and Eastern Europe have the potential to be quite lucrative for the firm that can effectively deliver services to this hungry market. There are two large constraints with any such project: first, getting the state-owned national telecom systems to share appropriate revenue from long distance calls to make the venture profitable; and, second, to find financing for projects that are not billion dollar, national system renovations. The parties in these ventures ususally need intense technical assistance to develop basic business documentation. Each of these firms had received a license to establish rural telecommunications systems in their regions of Poland. The regulatory environment for this industry is such that it is relatively easy to get permission to establish a business, but extremely difficult to get the authority to charge profitable rates.

Retel Bialystock is a firm organized by small private investors to develop a rural telecommunications network in the Bialystok region of Poland. The enterprise would provide both telephone and cable television services to a potential market of 90,000-120,000 subscribers. The Financial Services RBDO office introduced the project to the CDI Telecoms team in July '93 and participated in project investigation team sent to evaluate Retel Bialystok. The Financial Services team worked extensively with the enterprise managers and with the Telecom technical team to develop a business plan, marketing strategy and financial projections.

Over the course of several months, the RDBO Office provided Retel Bialystok with information on the Polish tax system and worked with their financial team to investigate tax liabilities and postures that could provide maximum benefit to the firm. The previous local experience of the RBDO Office staff with the telecom industry in Poland was particularly helpful. To support the marketing strategy of the firm, the RBDO Office prepared several studies for the CDI Telecom team including a review of fee rates for local telephone and cable TV operators and a review of the telecommunications market in Poland. They also identified the requirements for applications for loans from multilateral financial institutions and opportunities for financial support for private telecommunications firms. The Office also identified three potential sources of finance and assisted with applications and introductions. Retel Bialystok is pursuing several financing options at this time.

Telekom Torun is a rural telecommunications project with 200,000 potential subscribers in the Torun region of northern Poland. The office provided the same level of support for this project as for Retel Bialystok and was involved in all aspects of financial documentation preparation from development of the business plan to revising the projected cash flows based upon new information sourced by the RBDO Office. Telekom Torun is seeking financing from two multilateral lenders.

The rate structure review report prepared by C&L was a critical negotiation document as these firms built their enterprise structure. In the erratic regulatory environment, the study made a clear and unbiased case for the rate structure the firms were proposing from the state-owned telecommunications firm that controls long distance revenue. The review of the telecommunications market in Poland was a persuasive document to support the financial viability of these projects. Finally, the financial management assistance and training the firms received working with RBDO Office on the financial packages for these projects can have long term benefits for the successful management of the enterprises.

OMG and Graphnet

Max Ebenstein is an American businessman whose family was from Poland. His firm, Overseas Magagement Group had been looking into investment opportunities of all sorts when the CDI Regional Project Office was opened in September '92. He called on the Telecom team in November of that year right after he received a license to establish a E-Mail system in Warsaw. He was seeking

additional investors in the new Polish enterprise and the Financial Services team reviewed the business documentation for the new firm and the Telecom team looked for potential partners in the U.S. through the Department of Commerce, "Eastern Europe Looks for Partners."
Any potential partner would have to be approved by the state-owned telecommunications authority. Several possible investors were identified and the difficult review process began. Over the next seven month various partners were rejected by the Polish telecom authority. Finally a joint venture with the Polish Postal System was proposed and after many meetings, was approved as the partner with OMG for the Graphnet Project.

Now the new enterprise had to secure approval for its proposed rate structure for subscribers. The Financial Services RBDO Office and the Telecom team worked with Graphnet to support its rate application. This firm didn't need the usual financial management support most Polish firms required, but it needed marketing, fee structure and financial analysis support to pursuade the licensing authority to grant its request. The Financial Services team and the Telecom team met frequently with managers at the Ministry of Communications to resolve questions they might have over the Graphnet application. Eight months latter Graphnet was granted a license providing the rates it needed to insure the profitability of the enterprise. In December '94, the firm secured a financing from private investors and the Polish American Enterprise Fund for capital equipment. The support the CDI team provided through the regulatory problems was critical this venture.

APPENDIX II.

DEVELOPMENT COST SUPPORT FUND

GRANT REPORTS

APPENDIX III.

FINANCING GUIDE FOR CENTRAL AND EASTERN EUROPE

APPENDIX IV.

CAPITAL DEVELOPMENT INTIATIVE

GOVERNMENT PROPERTY REPORT